ARMED SERVICES BOARD OF CONTRACT APPEALS

Appeal of --	)	
	)	
Lockheed Martin Corporation	)	ASBCA No. 53822
	)	
Under Contract No. F33657-91-C-0006	)	

APPEARANCES FOR THE APPELLANT: Terry L. Albertson, Esq.
Linda S. Bruggeman, Esq.
Crowell & Moring
Washington, DC

APPEARANCES FOR THE GOVERNMENT: E. Michael Chiaparas, Esq.
Chief Trial Attorney
Charles W. Goeke, Esq.
Senior Trial Attorney
Defense Contract Management Agency
Philadelphia, PA

OPINION BY ADMINISTRATIVE JUDGE PEACOCK

This timely appeal presents the issue of whether the Cost Accounting Standards (CAS) provisions in the F-22 contract and associated regulations required that contract to be included in the analysis of cost impacts associated with certain changes in cost accounting practice implemented in 1993. Only entitlement is before us for decision. We determine that the F-22 contract as repriced and rephased after implementation of the changed practices was not an "affected contract." Therefore, it was not required to be included in the detailed cost impact study evaluating the cost shifts associated with those changed practices. Accordingly, we sustain the appeal.

FINDINGS OF FACT

1. The United States Air Force (Air Force) awarded the referenced contract to Lockheed Corporation, now Lockheed Martin Corporation (appellant or LMC), on 2 August 1991 for engineering and manufacturing development (EMD) of the Air Force's next generation air superiority fighter, the F-22. The cost-plus-award-fee contract (hereinafter sometimes referred to as the F-22 contract) had an estimated value at award of $9.55 billion with performance scheduled over an eight to nine year period. (R4, tab 1)

2. Among the clauses incorporated into the F-22 contract by reference were FAR 52.230-2, COST ACCOUNTING STANDARDS (AUG 1992) (hereinafter the CAS clause) and FAR 52.230-4, ADMINISTRATION OF COST ACCOUNTING STANDARDS (SEP 1987) (hereinafter the Administration of CAS clause) (R4, tab 1, s*ee* Appendix).[1] Lockheed Aeronautical Systems Company (LASC) was the "business unit" (for purposes of the CAS clauses) of Lockheed Corporation involved in the performance of the contract that submitted the changes in cost accounting practice involved in this appeal (R4, tabs 39, 50). Also of relevance is FAR 30.602-3, VOLUNTARY CHANGES (JAN 1989), relating to disclosed or established cost accounting practices (R4, tab 68).

3. On 19 August 1992, the Air Force Procurement Contracting Officer (PCO) advised LASC of an expected funding shortfall for the F-22 program in fiscal year (FY) 1993. In September 1992, LASC provided to the Air Force "budgetary cost and schedule information for five potential rephased programs," including the F-22. (R4, tab 25)

4. By letter dated 18 November 1992, "Request for Proposal (RFP) for Rephasing of F-22 Program" (RFP letter), the Air Force PCO asked LASC to prepare a proposal for the rephasing of the F-22 contract to accommodate funding constraints so as to match or "fit within . . . [the Air Force's] revised . . . funding profile" for each fiscal year from 1993 through 2001. LASC was to submit its proposal with an estimated cost and not-to-exceed (NTE) base and award fees by 19 March 1993 with several interim milestones. (R4, tab 23) The RFP letter identified the following technical and schedule changes to the F-22 contract:

> (1) Delete 2 EMD Flight Test Aircraft
> (2) Move 2-seat aircraft to #7 and #9
> (3) First avionics aircraft is #4
> (4) Move CDR [critical design review] 6-9 months
> (5) Move first flight date of aircraft #1 11 months
> (6) Move first avionics flight 11 months
> (7) Move LRIP [low rate initial production] contract award 11 months
> (8) Move PPV [pre-production vehicles] aircraft 11 months
> (9) Move milestone III 18 months
> (10) Move required assets available 11 months

(R4, tab 23 at 1-2 of 8)

[1] The CAS clauses and regulations have been revised. Pertinent portions of the CAS clauses and regulations applicable to this contract are included in an Appendix to this opinion.

5. The RFP letter required appellant to prepare the cost proposal in five separate sections, commonly referred to by the parties as "buckets," as follows (R4, tab 23 at 2-3 of 8):

> 5. The contractor shall prepare the cost proposal in five sections as follows. The five sections are a) Two Aircraft Deletion, b) Revised Program Baseline, c) Hazards, d) Program Rephase Impacts, and e) Revised EMD Program. The proposal shall be organized using the IPT [Integrated Product Team] structure identified in Attachment 1, with visibility to the level III Work Breakdown Structure (WBS). The cost data shall start at the lower tier IPTs, and shall roll up to the next tier IPT level until it reaches the Weapon System IPT and shall be traceable accordingly. For areas which do not fit in the outlined IPT structure, (e.g., Test and F-22 Information Resource Management) the Contractor shall propose these accordingly with an ultimate roll up into the Weapon System IPT. The proposal shall include the proposed rephrased hours with narrative substantiation including a discussion comparing the proposed changes to the current program. . . .
>
> Section a. Two Aircraft Deletion. This section shall provide the details of deleting two EMD aircraft, moving the 2 seat-aircraft to #7 and #9, and moving the first avionics aircraft to #4. It shall include a breakout of cost/labor hour by IPT structure as identified in Attachment 1, showing the major functional categories involved. Each IPT cost breakout shall have visibility at the level 3 WBS and level 4 in WBS 1400. Nonrecurring and recurring costs should also be identified. This section should also include a description of assumptions used in formulating the costs to be deleted for the two aircraft.
>
> Section b. Revised Program Baseline. This section shall provide details of the current program EAC [estimate at completion]. This detail shall include an expenditure breakout/labor hour by IPT structure . . . . Each IPT cost breakout shall have visibility at the level 3 WBS and level 4 in WBS 1400, showing the major functional categories involved. . . . This section shall also include a description of the EAC process to include assumptions and methodologies.

> Section c. Hazards. This section shall provide the details of each current program hazard not incorporated into the program EAC discussed in section b. In addition to a technical/programmatic description, this detail shall include a breakout of cost/labor hour by IPT structure . . . . Each IPT cost breakout shall have visibility at the level 3 WBS and level 4 in WBS 1400.
>
> Section d. Program Rephase Impacts. This section shall provide the details of rephrasing the program to accomplish the rephrasing as stated in paragraph 3 (4) through (10). Separately identified shall be the costs of inflation, assumed inefficiencies, added effort, and any other costs necessary for rephrasing of the program. This detail shall include a breakout of cost/labor hour by IPT structure . . . . Each IPT cost breakout shall have visibility at the level 3 WBS and level 4 in WBS 1400. . . .
>
> Section e. Revised EMD Program. This section shall provide the summary detail for the Revised EMD Program. This detail shall include a summary breakout of cost/labor hour by IPT structure as identified . . . . Each IPT cost breakout shall have visibility at the level 3 WBS and level 4 in WBS 1400. Nonrecurring and recurring costs shall also be identified. . . . This section shall also include a complete documentation of all estimating assumptions to include updated wrap rates and factors, escalation indices, and changes in methodologies.

6. The third bucket, "Hazards" was later renamed "Other Cost Changes or "Other Costs." In addition, LASC was later required to submit data identifying the cost impact of an engineering change proposal regarding reducing the aircraft's weight. (R4, tab 25 at 5, tab 27 at 3, tab 29; tr. 3/67-68)

7. On 22 December 1992, the Air Force PCO unilaterally issued Modification No. P00059 (Mod. 59) as an undefinitized contract action (UCA) pursuant to the Termination (Cost Reimbursement) and Changes clauses of the F-22 contract. Mod. 59 required LASC to implement the rephasing of the contract (with additional revisions and details) at a total estimated cost of $1.025 billion, a NTE base fee of $23.2 million and a NTE award fee of $61.8 million. The modification incorporated FAR 52.216-25, CONTRACT DEFINITIZATION (APR 1984) (modified as appropriate for a UCA as opposed

to a letter contract) that, among other things, rescheduled the date for submission of LASC's proposal to 23 April 1993. (R4, tab 26)

8. By letters dated 23 December 1992 and 22 January 1993, the Air Force issued additional instructions for the rephase proposal. Among other things, each letter reiterated the requirement for a summary of the build-up of man hours by calendar year for every Tier IV IPT. (R4, tab 27 at 2, tab 28 at 2)

9. On 23 April 1993, LASC submitted its initial rephase proposal, designated "CONTRACT CHANGE PROPOSAL (CCP 0015) FOR REPHASING OF F-22 PROGRAM" (R4, tab 38 at G-00137, -00156). Including amounts attributable to additional changes that the parties agreed to include, the total increase in cost plus base fee for the F-22 contract was $1,091,320,311 (*id.* at G-00139). The intent of the proposal was to comprehensively "reprice" the rephrased F-22 contract so as to realistically reflect its entire current cost, including all escalation, changes in rates, hours, factors and other cost impacts (R4, tabs 59, 65; tr. 1/163-64, 3/65, 73, 176-80, 182-83).

10. Contemporaneously with the RFP letter and rephase proposal process, LASC's accounting system and cost accounting practices were analyzed as part of a comprehensive Overhead Cost Analysis and Control Review (OCACR) process instituted by the Secretary of the Air Force and performed in 1992-93. The OCACR involved establishing two Overhead Review Teams (ORT), one staffed by LASC's representatives and the second by representatives from various government agencies. (App. supp. R4, tabs 1, 3, 4, 5) A primary purpose of the OCACR was to "identify opportunities to shift overhead to direct costs for better visibility, tracking and control" (app. supp. R4, tab 3 at 2, tab 5 at 2). The government ORT made extensive recommendations for changes to LASC's cost accounting system and practices. Certain of these recommended revisions concerned direct charging of certain personnel costs to the F-22 contract that had previously been classified and allocated as indirect costs. (App. supp. R4, tab 8 at 2, 4, tab 10 at 4, tab 18 at 52, 81-82; tr. 2/248-49, 264, 268, 273, 3/11, 63-64, 110) LASC initially raised both practical and legal objections to many of the recommendations (app. supp. R4, tab 6 at 2, 5, tab 7 at 2, 4, 19). In particular, LASC expressed significant concerns about the potential increased cost impact of making the changes and informed the Air Force that it might agree to institute them if the government would consent to an equitable adjustment for the impact. It also objected to the government ORT's quantification of projected cost savings over time. (R4, tab 22; app. supp. R4, tab 6 at 3, tab 7 at 2-3, tab 15 at 1, tab 18 at 11, tab 19 at 3, 4, tab 25 at 2, 5, 7-8, 21 25, tab 28 at 8; tr. 3/8-14, 27-36, 56) LASC eventually was pressured by the government to implement accounting changes that reclassified indirect personnel costs and charged them directly, including those involved in this dispute. Although other factors also influenced the decision to direct charge the personnel costs in question, the government pressure was the primary reason for the change. (*Id;* tr. 3/10-15, 41-42, 45, 47, 51, 55-56).

11. By letter dated 4 June 1993, LASC officially notified the cognizant Administrative Contracting Officer (ACO), in this case the Division Administrative Contracting Officer (DACO) of the then Defense Logistics Agency, later the Defense Contract Management Agency (DCMA), that LASC would be making changes to its cost accounting practices, that are together commonly referred to by the parties as the Mid-Year 1993 Accounting Changes (Mid-Year Changes, changed practices or new practices) (R4, tab 39). The DACO had previously been apprised of the ongoing OCACR process and eventual recommendations of the government's ORT, including the Mid-Year Changes (tr. 1/213-14, 2/30-31, 3/25). The Mid-Year Changes reclassified the following types of personnel costs (that had previously been charged indirectly) as direct costs of the cost objective (contract/program) with which they could be specifically identified: program management, master scheduling, industrial engineering and engineering administration (R4, tab 50 at G-00316). The 4 June 1993 letter also sought to amend LASC's CAS disclosure statement to reflect the changed practices. The letter requested a waiver of the 60-day requirement for implementation of the new practices and permission to make the changes effective 28 June 1993. (R4, tab 39) The DACO waived the 60-day notification period permitting the changes to be effective as requested. The DACO was aware that LASC intended to incorporate the changed practices in its F-22 rephase proposal. (Tr. 1/206-07)

12. On 22 June 1993, LASC furnished to the DACO the "General Order of Magnitude Cost and Rate Impact Study Reflecting Mid Year 1993 Accounting Changes" (the General Magnitude Study) as required by paragraph (a) of the Administration of CAS clause, FAR 52.230-4, and FAR 30.602-3(a). The General Magnitude Study displayed the estimated cost shifts between LASC's various programs. (R4, tab 41) At the time of its submission, LASC's business base was predominantly oriented toward production of C-130 aircraft under fixed-price contracts (tr. 2/137-38, 163, 199-202). The General Magnitude Study listed the F-22 contract (pending the conclusion of the rephase repricing negotiations) and estimated that the direct charging of the costs involved in the Mid-Year Changes (offset to an extent by no longer charging the costs indirectly) would result in an increase of costs to the F-22 program of $10,055,000 during the period from mid-1993 through 1997, while decreasing the costs allocable to the fixed-price C-130 contracts an estimated $11,748,000 over that period (R4, tab 41 at G-00204).

13. The Air Force was also apprised of the new practices in early June 1993. In its 2 July 1993 update to its proposal for the rephrased F-22 contract, appellant officially disclosed to the Air Force that it was implementing the Mid-Year Changes as of 28 June and anticipated that recalculated forward pricing rates incorporating the changed practices would be available by 20 July 1993. (R4, tab 43 at G-00210-11)

14. On 19 July 1993, LASC submitted to the DACO proposed forward pricing rates, including both direct labor and indirect rates. The rates reflected the estimated impact of the Mid-Year Changes and recently-concluded union negotiations that significantly reduced labor rates. (R4, tab 46)

15. In its rephrase proposal update of 29 July 1993, with copy furnished to the DACO, LASC again fully disclosed the changed practices and provided the Air Force negotiating team with the new forward pricing rates reflecting the Mid-Year Changes and new union agreement, as follows:

> The last adjustment is for new LASC rate information, including accounting system changes. After the 07-02-93 LASC Update was provided, LASC published new rate information. These new rates incorporate the recent union agreement and the accounting change which now charges Program Management, Master Scheduling, Industrial Engineering, and Engineering Administration direct versus indirect.
>
> LASC has estimated the impact of these changes to the Revised EMD Program and calculated a net ($8,435,437) impact. This net impact is comprised of a decrease of ($79,613,799) and an increase of $71,193,246. The decrease results primarily from lower direct labor rates and overhead rates. Direct labor rates decreased in all categories as a result of the union agreement and other forecast projections. Engineering Overhead, Factory Overhead and G & A have decreased as a result of the movement of indirect costs to direct costs. The fiscal year impact of the decrease is as follows:

FY 1992	18
FY 1993	(3,167,825)
FY 1994	(9,272,966)
FY 1995	(14,682,245)
FY 1996	(17,181,101)
FY 1997	(13,850,103)
FY 1998	(11,849,795)
FY 1999	(5,570,702)
FY 2000	(3,539,856)
FY 2001	(499,224)
TOTAL	($79,613,799)

The increased amounts for the new direct costs were estimated based on the new forward pricing rates for the new categories and estimated headcount requirements.

Program management headcount was estimated at seven (7) people from July 1993 through the end of the EMD program. Total Program Management cost is estimated at $12,954,501.

Master Scheduling headcount was estimated at approximately 31.5 people from July 1993 decreasing to 29 people in 1997, 19 people in 1988, 12 people in 1999, 5 people in 2000 and 0.2 people in 2001. Total Master Scheduling cost is estimated at $32,638,592.

Engineering Program Control headcount was estimated at approximately 6.3 people from July 1993 through 1995, 5.4 people in 1996, 5 people in 1997, 3.3. people in 1998, 2 people in 1999, and 1 person in 2000. Total Engineering Program Control cost is estimated at $6,562,069.

Engineering Support Staff headcount was estimated at approximately 4.5 people from July 1993 through 1996, 4 people in 1997, 2.7 people in 1998, 1.7 people in 1999, and .7 people in 2000. Total Engineering Support Staff cost is estimated at $5,159,579.

Industrial Engineering headcount was estimated at 12.5 people from July 1993 through the end of the year, 15 people in 1994 through 1996, 11.5 people in 1997, 7.7 people in

1998, 4.7 people in 1999, and 2 people in 2000. Total industrial Engineering cost is estimated at $13,878,505.

The fiscal year impact of the increase is as follows:

FY 1993	2,914,185
FY 1994	11,603,433
FY 1995	12,036,526
FY 1996	13,106,913
FY 1997	12,316,020
FY 1998	9,288,473
FY 1999	6,124,715
FY 2000	3,119, 634
FY 2001	683,347
TOTAL	$71,193,246

For this update, it has been assumed that the total impact is an Other Cost Change. This amount is not in any of the proposal details previously submitted on 07-02-93 or in the Team update details. This amount is provided at the bottomline only (in the same way Post Flight Data Processing was in the 04-23-93 submittal).

As the Post Flight Data Processing estimate has been updated and included in the proposal detail for the update, the following information is not longer necessary.

(R4, tab 47 at G-00276-77)

16. The 29 July 1993 update reflected appellant's estimate that the increased cost and base fee attributable to the rephase was $915,875,468 (*id.* at G-00279-80).

17. The changed practices were adequately described and considered by the DACO to be CAS-compliant. In a letter of 10 August 1993, the DACO requested that LASC, within 60 days, submit a "detailed cost impact study" (CIS) for the Mid-Year Changes as required for voluntary changes by paragraph (b) of the Administration of CAS clause and FAR 30.602-3(b). (R4, tab 48; tr. 1/239-40)

18. On 23 September 1993, the DACO provided the Air Force PCO with "Interim Forward Pricing Rate Recommendations" for the period 1993-1997 for use in the F-22 rephase negotiations. No forward pricing rate agreement for LASC was then in effect. The interim rates acknowledged, considered, and incorporated the new practices. The

DACO indicated that the potential reduced volume of overall work for the F-22 would not be known until mid-October 1993 and this factor (along with others) resulted in the DACO's recommendation of lower rates than LASC had proposed in its 29 July 1993 updated proposal for all years except 1997. (R4, tab 54 at G-00337-40; tr. 3/244)

19. On 24 September 1993, LASC requested a 60-day extension to submit its CIS for the Mid-Year Changes. The DACO approved the extension on 27 September 1993 making the date for submission 10 December 1993. (R4, tab 55)

20. From the time that the new practices were incorporated into its proposal for the rephrased F-22 contract in late July through the completion of negotiations in late October 1993, LASC and the Air Force negotiation team thoroughly discussed and negotiated the estimated impacts of the Mid-Year Changes. The estimated increased direct labor hours that shifted from indirect accounts as a result of the changed practices were identified and justified by appellant and understood and verified by the Air Force. New direct-charged personnel were disclosed by name and their hours specifically itemized. Estimated travel expenses for these employees were also identified. By the end of negotiations, there was no disagreement between LASC and the Air Force about the accuracy of the estimated direct labor hours or direct labor rates attributable to the employees. The effects of the changed practices were fully integrated and factored into the rephased F-22 contract price. (Tr. 3/104, 110-17, 120, 123-24, 126-28, 130-137, 141-45, 148; app. supp. R4, tab 45 at 11, 23-31, tab 47 at 2, 5, 7-15, 21-26)

21. Each of the IPTs called for in the RFP letter included technical representatives of LASC and the government. The IPTs collaborated in evaluating the changes in cost and total cost of all of the "base" cost elements associated with their items of work (including labor hours, travel and material costs) to which indirect cost rates would be applied. The rephase negotiation process comprehensively reexamined and reevaluated all of the work items to be performed down to the IPT level, not just the "incremental" or discrete additive/deductive items specifically mentioned in the RFP letter. (Tr. 3/65, 73, 75-76, 79-82, 148, 176-83) There is no persuasive evidence that the evaluation of "base" hours by the IPTs distinguished "changed" (additive/deductive technical items) work from the originally specified work.

22. By letter of 2 November 1993, LASC confirmed completion of negotiations and attached its Certificate of Current Cost or Pricing Data certifying that the data was accurate, current and complete as of 22 October 1993. The agreed upon increase between LASC and the PCO in the price of the contract including base fee was $721,676,603. (R4, tab 58)

23. LASC and the Air Force PCO executed contract Modification No. P00098 (Mod. 98), dated 15 November 1993, definitizing Mod. 59. Mod. 98 decreased the

contract price (estimated in Mod. 59) in the amount of $326,523,397. (R4, tab 60) The Price Negotiation Memorandum (PNM) accompanying Mod. 98 and bearing the same date indicates that the Air Force elected to use the DACO-approved indirect rates resulting in minor differences in the parties' rate calculations and a "bottom line agreement" on the final estimated cost (R4, tab 59 at G-00364, -00371, -00374; tr. 1/83-86, 90, 158, 169-70, 173-74, 185-87). The PNM notes, "The IPT process resulted in the agreement of all discrete items and issues prior to the completion of fact-finding. The end result is that the process resulted in an excellent technical rebaselining of the program and one that meets the fiscal year funding limitations that caused the rephrase." (R4, tab 59 at G-00364)

24. LASC submitted its CIS for the Mid-Year Changes to the DACO on 10 December 1993. The CIS indicated that there was an overall decrease of $1,978,000 to government CAS-covered contracts. The F-22 contract was identified but excluded from the study because LASC considered that the impacts were already reflected in the negotiations and "repricing" of the rephased contract. (R4, tab 61) Following receipt of the CIS, the DACO transmitted the study to the Defense Contract Audit Agency (DCAA) for audit (tr. 2/6).

25. On 28 September 1998, DCAA issued its audit report on LASC's CIS, concluding that the net result of the Mid-Year Changes was to increase total costs to the government in the estimated amount of $20,622,025, including an estimated increase of $18,622, 000 on the F-22 contract through FY 2000. DCAA maintained that the CAS clauses protected the government from paying increased costs resulting from the voluntary changed practices. (R4, tab 2; tr. 2/69-70, 92-107, 132-33) DCAA considered that the rephasing of the F-22 contract was a contract modification and not a new contract and thus the contract was required to be included in the CIS. (R4, tab 2 at 3) The DACO forwarded the audit report to LASC's successor Lockheed Martin Aeronautical Systems (LMAS) on 2 December 1998 and requested its response (R4, tab 2, cover letter).

26. LMAS responded on 30 March 1999 asserting its position that the cost impacts of the changed practices were fully disclosed and incorporated into the repriced and rephased F-22 contract (R4, tab 6).

27. The DACO asked DCAA to review LMAC's position on 4 April 1999 and DCAA, in turn, on 21 April 1999, asked the Air Force questions regarding the impact of the Mid-Year Changes and the rephase negotiations (R4, tab 64; app. supp. R4, tab 63; tr. 2/167-69). The Air Force responded in a memorandum to DCAA of 18 May 1999, which stated in part:

> 1. The intent of CCP0015, rephrase 1, was to reprice the entire F-22 EMD contract to reflect the current total cost of

the contract. The rephrase included five sections or buckets, each associated with different cost impacts. Two of the buckets would be associated with your questions, they were bucket one which included all actual impacts through November 1992, and bucket two which included all cost growth from December 1992 to the end of the contract. The cost growth included the use of current rates and factors, and bucket two included the impact of the 1993 midyear accounting change. As part of the negotiations, the contractor disclosed the accounting changes and their impact to the F-22 program. The AFNT [Air Force Negotiation Team] worked with the contractor, the DCAA and the DCM[A] to understand the impacts and develop a Government position. . . . It was our intent to incorporate the impact of the accounting changes, as they impacted the F-22, in our negotiations, and we believe we did so. However, it was never our intent, or in our authority, to review or account for the accounting change impacts across the entire LMAS business base. We were limited to addressing the accounting change impacts to the F-22 EMD contract.

Your letter contained four additional questions. The answers are as follows:

The contractor did identify the new rates and how they impacted the current F-22 EMD contract.

The contractor did identify the direct hours and how they impacted the current F-22 EMD contract.

The net impact of the changes were not separately priced, but they were explained and understood by the AFNT. Do [sic] to the nature of the change, the AFNT found it necessary to spend a great deal of time working the issue with the contractor, DCAA and DCMC, including obtaining a unique set of rates to be used for the rephase only, from the DCMC.

The AFNT can not provide a definite yes or no to your final question. We were aware that the changes were of a voluntary nature, and we knew their impact to the F-22 EMD contract, however, we did not look into the impact across the

> LMAS business base. As such, the AFNT would not have known if the voluntary changes had resulted in increased costs to the Government in total. Further, it was never our intent to make an assessment, as our review and authority was limited to the F-22 program.
>
> 2. In summary, it was our intent to make the F-22 contract current for all changes in rates, factors and cost impacts at the time of negotiations. This included the impact of the 1993 midyear accounting change. However, the negotiations were for the F-22 program only and never addressed any other Government contracts with LMAS or the impact of the accounting change impacts on the total LMAS Government business base.

(R4, tab 65)

28. The parties continued to discuss cost impact issues associated with the Mid-Year Changes as well as other subsequent changed accounting practices implemented by appellant for approximately two years. On 3 April 2001, the DACO sent appellant a letter asserting that appellant was indebted to the government in the amount of $37.8 million for these changes citing FAR 30.602-3. (R4, tab 10)

29. Appellant responded in early May 2001 with a letter and white paper that reargued its position that the 1993 changed practices were fully disclosed and used in the cost estimating process by the contracting parties to reprice the rephased contract. Therefore, the F-22 contract was not an "affected contract" subject to inclusion in the detailed CIS. (R4, tab 11)

30. In an audit report of 31 October 2001, DCAA reached the same conclusion that it had in its previous audit, *i.e.*, that no "new contract" resulted from the rephrasing and pricing of the modification of the contract. With reference to FAR 30.602-3(a)(2), DCAA further stated that the voluntary change was "not desirable, and, further, is grossly detrimental [to the government] since the amount of money affecting the contract is substantial." (R4, tab 13 at 3) (Emphasis in original)

31. By final decision dated 4 March 2002, the DACO asserted a claim against appellant for $32 million pursuant to FAR 30.602-3 related to the Mid-Year Changes here in dispute, as well as other later cost accounting practice changes made in 1994 through 1996. With respect to the 1993 changed practices, the DACO maintained that the F-22 contract was an "affected contract" because the rephase negotiations pertained merely to a modification of that contract and did not constitute a new contract. (R4, tab

14) According to the DACO, the negotiations associated with the rephase were simply "an exercise in estimating" until final costs were determined (*id.* at 5-6). In addition, the DACO stated, "The Air Force negotiators did not have the authority or desire to determine in advance, or agree to, final overhead rates, or negotiate CAS required adjustments to contracts arising from voluntary accounting changes, whose negotiation and settlement is a DACO function" (*id.* at 6). The DACO also has determined that the Mid-Year Changes were not desirable and were detrimental to the government in that they resulted in increased costs (tr. 2/199-200). There is no documentation in the record providing any further rationale for the latter DACO determination.

32. Appellant timely appealed the final decision on 29 May 2002 (R4, tab 16). On 2 April 2002, appellant paid the government $17,300,000 to cover adjustments associated with the cost impacts of all of the post-1993 changes in cost accounting practice, leaving approximately $14.7 million in dispute. However, the precise dollar cost shifts associated with including or excluding the F-22 contract from the CIS are uncertain. (R4, tab 15; tr. 2/211) The parties have requested that we decide only entitlement, leaving determination of the precise amount to negotiation on remand.

DECISION

The government argues that the F-22 contract was an "affected contract" within the meaning of the CAS provisions and regulations establishing requirements for a CIS. As an "affected contract," the government maintains that the impacts of the voluntary changed practices on that contract were required to be included in appellant's CIS. According to the government, if the impacts of the new practices on that contract had been included, the CIS would have shown that costs to the government would have increased by approximately $14.7 million as a consequence of the changed practices. The government now claims that it is entitled to a commensurate price adjustment. In addition, the government alleges that the DACO had sole authority to make determinations regarding the cost impact of changed practices and that actions by the Air Force PCO that encroached on cost impact determinations were unauthorized. Finally, the government argues that the voluntary changed practices were not "desirable" within the meaning of FAR 30.602-3(c).

Appellant contends, *inter alia,* that no "increased costs" were paid by the government as a result of the changed practices because the contract was completely repriced during the rephase negotiations. Appellant notes that the new practices were disclosed, and knowingly used by both the DACO and PCO in developing the estimated cost of the F-22 contract as rephased. As a result, appellant asserts that the contract was not an "affected contract," was not required to be included in appellant's detailed CIS, and was not otherwise subject to a price adjustment as a consequence of the changed practices. Appellant argues that the PCO had authority to negotiate the rephase

modifications (Mods. 59 and 98) and did not infringe on the DACO's authority. Appellant also contends that the changed practices were instituted following the extensive ORACA review by the government of LASC's accounting practices. According to appellant, not only were the new practices considered desirable from the perspective of the government's ORT, the government actively pressured LASC to make the changes.

We agree with the government's contention that the primary issue in this appeal is whether the F-22 contract was an "affected contract." We disagree, however, with the government's conclusion that the contract should be so classified.

Following a summarization of pertinent contract and regulatory provisions in effect at the time of the dispute, we discuss the meaning of the term "affected contract" and apply it to the specific facts and circumstances of this case. We then address the government's contentions regarding the respective authority of the DACO and PCO.

Contract and Regulatory Requirements

The contract's CAS clause, FAR 52.230-2, requires the contractor to disclose its cost accounting practices and follow the disclosed practices consistently in accumulating and reporting costs in performance of the contract. If its cost accounting practices change, the contractor must amend its CAS disclosure statement to reflect the changed practices and apply the changed practices prospectively. In addition, the clause requires that, "If the contract price or cost allowance . . . is affected by such [changed practices], adjustment shall be made [in the present case] in accordance with subparagraph (a)(4) . . . of this clause." Subparagraph (a)(4)(ii) requires, in the case of non-required and non-agreed [voluntary] changes, that the contractor "[n]egotiate with the Contracting Officer [CO][2] to determine the terms and conditions under which a change may be made . . . provided that no agreement may be made under this provision that will increase costs paid by the United States." The CAS clause further incorporates into the contract by reference the provisions of 48 C.F.R. Part 9903.

With respect to voluntary changed practices of the type involved in this appeal, subparagraph (a) of the Administration of CAS clause, formerly at FAR 52.230-4, requires that the contractor initially submit to the cognizant CO a description of the change, its impact on CAS contracts and a "general dollar magnitude cost impact analysis of the change which displays the potential shift of costs between CAS-covered contracts by contract type . . . and other contractor business activity." This submission must be

[2] For purposes of administration of the CAS clauses and regulations cited herein, the CO, ACO and DACO are used interchangeably.

made not less than 60 days prior to the effective date of the proposed change unless otherwise agreed.

FAR 30.602-3(b) provides that, "The cognizant ACO shall review the [voluntary] accounting change concurrently for adequacy and compliance [with CAS]." Within 60 days (or as mutually agreed) following the "determination of the adequacy and compliance of a change," subparagraph (b) of the Administration of CAS clause requires the contractor to submit a "cost impact proposal in the form and manner specified by the cognizant [CO]."

Expanding on the latter requirement, FAR 30.602-3(b) requires the ACO to request "a cost impact proposal identifying all [CAS-covered contracts and subcontracts] and the contractor to submit a "cost impact proposal . . . in sufficient detail to allow evaluation and negotiation of the cost impact upon each affected CAS-covered contract and subcontract" (emphasis added).

Upon receipt of the detailed cost impact proposal/study, FAR 30.602-3(c) states that, "With the assistance of the auditor, the ACO shall promptly analyze . . . [and] determine whether or not the proposed change will result in increased costs being paid by the Government. The ACO shall consider all of the contractor's affected CAS-covered contracts and subcontracts" (emphasis added).

Subparagraph (c) of the Administration of CAS clause requires the contractor to "[a]gree to appropriate contract and subcontract amendments to reflect adjustments established in accordance with [subparagraph (a)(4) of the CAS clause]."

FAR 30.602-3(d) states in pertinent part, "if the parties fail to agree concerning the cost impact, the cognizant ACO, with the assistance of the auditor, shall estimate the cost impact" and ultimately "issue[] a unilateral determination" under the Disputes clause.

FAR 30.602-3(c) provides an exception to the prohibition in paragraph (a)(4)(ii) of the CAS clause against payment of increased costs by the government resulting from voluntary changes. It states that, "Increased costs resulting from a voluntary change may be allowed only if the ACO determines that the change is desirable and not detrimental to the Government."

"Affected Contract" Generally

In this appeal, there is no dispute that appellant's revised allocation procedures constituted voluntary changes in its cost accounting practice. Nor is there any dispute that the changed practices were properly disclosed and complied with CAS. Instead the

issues concern whether the F-22 contract was an "affected contract"[3] within the meaning of the above CAS provisions and regulations and thus subject to a possible price adjustment. *See McDonnell Douglas Corp*., ASBCA No. 44637, 95-2 BCA ¶ 27,858 at 138,911 (in determining government entitlement to price adjustment, all of contractor's "affected CAS-covered contracts" must be considered to determine whether the voluntary changed practice "will result in increased costs being paid").

Neither party proposes that resort to a broad dictionary definition is appropriate to aid in the interpretation of the critical term "affected contract[s]." Nor does either contend that the words have a "plain meaning" that should be invoked without regard to the business/accounting, statutory and regulatory context of the detailed cost impact proposal/study process. The contentions of both parties have relied considerably on their respective views of the CAS statutory and regulatory intent and the contracting parties' understanding and usage of the term within that narrow context.

There are few details in the applicable CAS provisions and regulations regarding the scope of the cost impact proposal/study process for voluntary changes generally and, prior to 2005, no express definition of the critical term "affected contract."

In 2005, a definition of "affected contract" was added to the FAR in two places—to the list of definitions in FAR 30.001 and to subparagraph (a) of the previously revised Administration of CAS clause, previously redesignated as FAR 52.230-6. As relevant to this dispute, that definition states that an "affected CAS-covered contract" is one for which the contractor "[u]sed one accounting practice to estimate costs and a changed cost accounting practice to accumulate and report costs under the contract." *A fortiori*, contracts for which the contractor used the changed practice to *both estimate and accumulate costs* are not "affected contracts" under the 2005 definition and would not be included within the cost impact proposal/study required by FAR 30.602-3(b) or otherwise subject to adjustment as a consequence of the changed practice under the CAS clause.

There is nothing to suggest that the term had a different meaning or that the cost impact proposal/study process had a different scope under the CAS provisions and regulations in effect at the time of the events in dispute in this case. Nor does the government contend that the term "affected contract" as expressly defined in 2005 had a different meaning in 1993. The 2005 definition makes explicit what we consider implicit in the CAS provisions and regulations summarized above. It advances the policy and purpose underlying the CAS provisions and regulations then in effect. In the latter

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[3] Our discussion and interpretation of the term "affected contract[s]" in this opinion pertain solely to definition and meaning of the term in the context of the cost impact proposal process, without prejudice to possible alternative meanings in different statutory, contractual or regulatory contexts.

respect, the definition protects the government from payment of increased costs resulting from voluntary changes and promotes causation requirements inherent in analyzing the cost impact of changed practices. The definition also complements, and is a corollary to, CAS consistency requirements.

The CAS provisions in effect in 1993 (as well as 2005) implement language in the statutes that created and reconstituted the CAS Board (CASB), both of which focus on whether any "increased costs" were *caused* by the changed practice. Under the 1998 statute, a price adjustment is required only if "any increased costs are paid . . . by reason of a [changed practice]" (emphasis added). 41 U.S.C. § 422(h)(1)(B).[4] The regulations also underscore that there must be a causative relationship between the changed accounting practice and any "increased costs." For example, causation is emphasized in 48 C.F.R. Subpart 9903.306 which sets forth a CASB Interpretation describing considerations "in determining amounts of increased costs." Subparagraph (a) of the Interpretation states in part that, "Increased costs shall be deemed to have resulted whenever the cost paid by the Government results from a change in a contractor's cost accounting practices . . . and such cost is higher than it would have been had the practices not been changed" (emphasis added). Similarly, 48 C.F.R. Subpart 9903.306(c) states in part, "The statutory requirement underlying this interpretation is that the United States not pay increased costs, including a profit enlarged beyond that in the contemplation of the parties to the contract when the contract costs, price, or profit is negotiated" (emphasis added).

We consider that these CAS statutory and regulatory provisions envision that, to the extent that changed practices were knowingly used by both parties in estimating contract costs, any resulting increases are reflected in the negotiated contract price and within the parties' contemplation. For the accounting practice to cause increased (or decreased) costs, there must be a difference between the estimating practice and the accumulating/reporting practice. If the contract is estimated/priced in the same way it is costed, the parties have negotiated a bargained-for price that is not subject to the adjustment at issue here.

Finally, the 2005 definition of "affected CAS-covered contract" complements, and is a corollary to, the requirements of CAS 401, CONSISTENCY IN ESTIMATING, ACCUMULATING AND REPORTING COSTS, in effect in both 1993 and 2005. *See* 48 C.F.R. Subpart 9904.401. CAS 401 requires the consistent application of disclosed practices in

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[4] Of course, the cost shifts attributable to the changed practice may, at the individual contract level, decrease or increase costs payable by the government under one or more "affected contracts." The changed practice may also cause an overall cost increase or decrease in the aggregate among the universe of "affected contracts" to be included in the cost impact analysis. *See* 48 C.F.R. Subpart 9903.306(e).

estimating, accumulating and reporting costs. The 2005 definition extends and implements CAS 401 consistency concepts in the context of the cost impact proposal/study process. To the extent that a changed practice precludes compliance with consistency requirements, the government is protected from paying "increased costs" because they will be identified during the cost impact proposal process. On the other hand, in situations where the changed practice is disclosed and used in cost estimation and negotiation of a contract price, the accumulation and reporting of costs in accordance with the same changed practice does not violate these CAS consistency requirements.

The Rephased F-22 Contract

Had the rephase negotiations not occurred, the parties do not dispute that the F-22 contract would be an "affected CAS-covered contract" for inclusion in the appellant's detailed cost impact proposal/study. In the government's view, the rephase negotiations involved merely a contract modification and were either irrelevant on the issue of whether the F-22 contract was an "affected contract" or were not sufficiently material to change the status of the contract and remove it from the cost impact proposal process. To address these contentions, examination of the substance of the rephase negotiations is required.

The government maintains that appellant and the Air Force understood that they were negotiating a contract change proposal and did not price the equivalent of a new contract. The government emphasizes that the approximate $722 million increase to the F-22 contract price was only a "fraction" of the contract's $9.55 billion price as awarded. (Gov't br. at 60) The government contends that the contract was not completely repriced (gov't br. at 65-70). It also generally minimizes the materiality of the repricing effort by emphasizing that the scope of the contract as rephased was not revised and that the rephasing was not a "cardinal" change and simply "moved [the schedule] to the right" by 11 months (gov't br. at 60-64).

The government contentions are based on superficial, mostly irrelevant generalizations relating to the intent, scope and technical revisions of the rephase modifications and negotiations that miss the point. They do not convincingly and substantively address the critical issues inherent in the definition of "affected contract," *i.e.*, what accounting practices were used in estimating the price of the F-22 contract as rephased. The essential questions are whether the negotiating parties (LASC and the Air Force) knowingly repriced the contract using the changed practices rather than the practices used in pricing the original contract and whether the scope of that repricing effort was sufficiently comprehensive to justify a conclusion that the impact of the changed practices were fully incorporated in the contract price as rephased.

First, we agree with appellant that the negotiations associated with the pricing of the rephase modifications were unusually comprehensive. The Air Force as well as appellant described the scope of this effort as a "repricing" of the F-22 contract. The negotiations were budget-driven and the scope of the rephase repricing efforts was not coextensive with the scope of the incremental rephase technical changes. The parties were attempting to accurately determine the cost of the entire program and "rebaseline" the contract to insure compliance with budgetary constraints.

More important, however, than the general scope of the estimating and repricing effort is the role the changed practices in dispute played in that effort. The critical issue is whether the cost impacts of the changed practices were fully integrated into the pricing structure for the entire contract as rephased or solely the discrete technical revisions to the work.

In that regard, our findings detail that not only were the changed practices fully disclosed, but also that the DACO incorporated their effects in forward pricing rates provided to the Air Force for express use in the rephase negotiations. The parties conducted extensive cost-specific negotiations regarding the increased number of hours, personnel and associated costs that would be charged directly as a consequence of the changed practices. We have found that the effects of the changed practices were fully integrated and factored into the price of the entire contract as rephased.

The government diminishes the significance of the comprehensiveness of the repricing negotiations by stating that appellant will eventually be paid all of its allowable costs during the final rate/actual cost determination process. It maintains that the rephase negotiations were merely an "exercise in estimating."

While it is true that costs agreed to during negotiations are "estimated," there are detailed rules and regulations concerning how those estimates are derived and how costs will be accumulated, reported, allocated to contracts, and ultimately paid. What is not "estimated" is the accounting methodology and treatment of the types of costs in question. Here as a result of the Mid-Year Changes, certain indirect personnel costs were treated as direct costs. The agreed "estimated" hours and rates for the persons removed from the indirect cost pools may vary during the course of performance, but regardless of the estimated amount the resultant costs must be charged directly pursuant to the revised practices. The numbers may differ at the time of actual cost determination from the time of their estimation, but how the arithmetic is performed remains consistent. Moreover, appellant must consistently use that accounting methodology in negotiating, pricing and costing other contracts. The government's contentions fail to consider these consistency requirements as they apply not only to the F22 contract but also to appellant's universe of contracts.

We conclude that the F-22 contract was not an "affected CAS-covered contract." Therefore, it was not required to be included in the CIS analysis of the cost shifts resulting from the new practices.

DACO/PCO Authority and Relationship

The government emphasizes that the DLA DACO was (at that time) the point of contact for CAS and solely responsible for CAS administration under FAR 30.601, including the calculation of impacts and adjustments associated with voluntary cost accounting practice changes (gov't br. at 72). The government contends that the Air Force PCO did not agree to pay any "increased costs" and had no implied authority to pay the "impact" resulting from the rephasing because that authority was delegated to the DACO (gov't br. at 70-77).

The government's contentions concerning the respective authorities of the DACO and PCO again beg the real question in dispute, *i.e.*, was the F-22 contract an "affected contract." The Air Force may not disregard CAS administration requirements. However, the general requirement for submission of the CIS does not control what specific "affected contracts" must be included in that proposal/study for possible adjustment. The DACO is charged with determining the cost impact of changed practices on "affected contracts." That role does not give the DACO authority to determine that a contract must be so classified when the evidence is to the contrary.

The classification of a contract as an "affected contract" is not an authority issue. It is a factual issue for determination in each case. Here, the DACO: waived time limitations for implementation of the new practices sanctioning their use in the F-22 rephase negotiations; extended the date for completion of the detailed cost impact proposal/study until after conclusion of the negotiations; and, developed interim forward pricing rates for Air Force use in the negotiations that incorporated the effects of the new practices. Whether the DACO realized it at the time, the above actions and the integration of the new practices into the rephrased contract price effectively removed the F-22 contract from any requirement to include it in the detailed CIS. We conclude that CAS administration requirements do not supersede or permit restructuring of the results of the parties' arms length price negotiations conducted by the Air Force with full knowledge and integration of the changed practices. The PCO had authority to negotiate the rephrased contract price. *Cf. Teledyne Continental Motors (General Products Div.)*, ASBCA No. 22571, 85-3 BCA ¶ 18,472 (appellant changed its pension accounting practices after issuance of a letter contract but prior to its definitization; PCO had authority to negotiate and definitize price using the newly disclosed and changed practices even though the practices differed from those in its CAS disclosure statement in effect on the date of the contract).

Quantum and Desirability of Changed Practices

In this appeal, we are to decide entitlement only. In that respect, we have concluded that the F-22 contact need not be included in the detailed cost impact proposal/study and is not subject to a price adjustment as a consequence of the Mid-Year Changes. The effect of this conclusion on the amount of increased costs to the government, if any, resulting from the changed practices is uncertain as we have found. That quantum determination is remanded to the parties for negotiation.

If material increased costs resulted from the changed practices, the CO shall further consider the question of whether the voluntary changes are "desirable and not detrimental to the interests of the Government" within the meaning of FAR 30.602-3(c) and document the rationale supporting the determination. In that regard, an increase in costs alone is not a sufficient basis for determining that the changed practices are not desirable. *See PACCAR Inc.*, ASBCA No. 27978, 89-2 BCA ¶ 21,696 at 109,080; Dept. of Defense CAS Steering Guidance W.G. 79-23; 48 C.F.R. Subpart 9903.201-6(c)(2)**.** In assessing desirability, we consider that relevant factors may include not only the magnitude of any increased costs but also: the extent of active government involvement in, and support for, the decision to institute the changed practices; the degree to which the changed practices increased the accuracy and precision of the cost measurement, assignment, and/or allocation process; the degree to which the changed practices increased the visibility, manageability and/or controllability of the costs in question; and, any other short or long term benefits to the government.

CONCLUSION

The appeal is sustained and remanded to the parties for negotiation of quantum in accordance with this decision.

Dated: 27 June 2007

ROBERT T. PEACOCK
Administrative Judge
Armed Services Board
of Contract Appeals

(Signatures continued)

I concur

MARK N. STEMPLER
Administrative Judge
Acting Chairman
Armed Services Board
of Contract Appeals

I concur

CAROL N. PARK-CONROY
Administrative Judge
Acting Vice Chairman
Armed Services Board
of Contract Appeals

I certify that the foregoing is a true copy of the Opinion and Decision of the Armed Services Board of Contract Appeals in ASBCA No. 53822, Appeal of Lockheed Martin Corporation, rendered in conformance with the Board's Charter.

Dated:

CATHERINE A. STANTON
Recorder, Armed Services
Board of Contract Appeals

APPENDIX

The clauses and regulations applicable to this dispute are, in pertinent part, as follows:

FAR 52.230-2, COST ACCOUNTING STANDARDS (AUG 1992)

> (a) Unless the contract is exempt from 48 CFR, Subparts 9903.201-1 and 9903.201-2, the provisions of 48 CFR, Part 9903 are incorporated herein by reference and the Contractor, in connection with this contract, shall—
>
> (1) (CAS-covered Contracts Only) By submission of a Disclosure Statement, disclose in writing the Contractor's cost accounting practices as required by 48 CFR, Subpart 9903.202-1 through 9903.202-5, including methods of distinguishing direct costs from indirect costs and the basis used for allocating indirect costs. The practices disclosed for this contract shall be the same as the practices currently disclosed and applied on all other contracts and subcontracts being performed by the Contractor and which contain a Cost Accounting Standards (CAS) clause. . . .
>
> (2) Follow consistently the Contractor's cost accounting practices in accumulating and reporting contract performance cost data concerning this contract. If any change in cost accounting practices is made for the purposes of any contract or subcontract subject to CAS requirements, the change must be applied prospectively to this contract and the Disclosure Statement must be amended accordingly. If the contract price or cost allowance of this contract is affected by such changes, adjustment shall be made in accordance with subparagraph (a)(4) or (a)(5) of this clause, as appropriate.
>
> (3) Comply with all CAS, including any modifications and interpretations indicated thereto contained in 48 CFR, Part 9904 (Appendix B, FAR loose-leaf edition), in effect on the date of award of this contract or, if the Contractor has submitted cost or pricing data, on the date of final agreement on price as shown on the Contractor's signed certificate of current cost or pricing data. The Contractor shall also comply with any CAS (or modifications to CAS) which hereafter

become applicable to a contract or subcontract of the Contractor. Such compliance shall be required prospectively from the date of applicability to such contract or subcontract.

(4)(i) Agree to an equitable adjustment as provided in the Changes clause of this contract if the contract cost is affected by a change which, pursuant to subparagraph (a)(3) of this clause, the Contractor is required to make to the Contractor's established cost accounting practices.

(ii) Negotiate with the Contracting Officer to determine the terms and conditions under which a change may be made to a cost accounting practice, other than a change made under other provisions of subparagraph (a)(4) of this clause; provided that no agreement may be made under this provision that will increase costs paid by the United States.

(iii) When the parties agree to a change to a cost accounting practice, other than a change under subdivision (a)(4)(i) of this clause, negotiate an equitable adjustment as provided in the Changes clause of this contract.

(5) Agree to an adjustment of the contract price or cost allowance, as appropriate, if the Contractor or a subcontractor fails to comply with an applicable Cost Accounting Standard, or to follow any cost accounting practice consistently and such failure results in any increased costs paid by the United States. Such adjustment shall provide for recovery of the increased costs to the United States, together with interest thereon computed at the annual rate established under section 6621 of the Internal Revenue Code of 1986 (26 U.S.C. 6621) for such period, from the time the payment by the United States was made to the time the adjustment is effected. In no case shall the Government recover costs greater than the increased cost to the Government, in the aggregate, on the relevant contracts subject to the price adjustment, unless the Contractor made a change in its cost accounting practices of which it was aware or should have been aware at the time of price negotiations and which it failed to disclose to the Government.

(b) If the parties fail to agree whether the Contractor or a subcontractor has complied with an applicable CAS in 48 CFR part 9904 or a CAS rule or regulation in 48 CFR part 9903 and as to any cost adjustment demanded by the United States, such failure to agree will constitute a dispute under the Contract Disputes Act (41 U.S.C. 601).

FAR 52.230-4, ADMINISTRATION OF COST ACCOUNTING STANDARDS (SEP 1987)

For the purpose of administering the Cost Accounting Standards (CAS) requirements under this contract, the Contractor shall take the steps outlined in paragraphs (a) through (f) of this clause:

(a) Submit to the cognizant Contracting Officer a description of any accounting change, the potential impact of the change on contracts containing a CAS clause, and if not obviously immaterial, a general dollar magnitude cost impact analysis of the change which displays the potential shift of costs between CAS-covered contracts by contract type (i.e., firm-fixed-price, incentive, cost-plus-fixed-fee, etc.) and other contractor business activity. . . .

(1) For any change in cost accounting practices required to comply with a new CAS in accordance with subparagraph (a)(3) and subdivision (a)(4)(i) of the CAS clause, within 60 days (or such other date as may be mutually agreed to) after award of a contract requiring this change.

(2) For any change in cost accounting practices proposed in accordance with subdivision (a)(4)(ii) or (a)(4)(iii) of the CAS clause or with subparagraph (a)(3) of the Disclosure and Consistency of Cost Accounting Practices clause, not less than 60 days (or such other date as may be mutually agreed to) before the effective date of the proposed change.

(3) For any failure to comply with an applicable CAS or to follow a disclosed practice as contemplated by subparagraph (a)(5) of the CAS clause or by subparagraph

(a)(4) of the Disclosure and Consistency of Cost Accounting Practices clause, within 60 days (or such other date as may be mutually agreed to) after the date of agreement of noncompliance by the Contractor.

(b) Submit a cost impact proposal in the form and manner specified by the cognizant Contracting Officer within 60 days (or such other date as may be mutually agreed to) after the date of determination of the adequacy and compliance of a change submitted pursuant to paragraph (a) of this clause. If the cost impact proposal is not submitted within the specified time, or any extension granted by the cognizant Contracting Officer, an amount not to exceed 10 percent of each payment made after that date may be withheld until such time as a proposal has been provided in the form and manner specified by the cognizant Contracting Officer.

(c) Agree to appropriate contract and subcontract amendments to reflect adjustments established in accordance with subparagraphs (a)(4) and (a)(5) of the CAS clause or with subparagraphs (a)(3) or (a)(4) of the CAS Disclosure and Consistency of Cost Accounting Practices clause.

48 C.F.R. 9903.306, INTERPRETATIONS

In determining amounts of increased costs in the clauses at 9903.201-4(a), Cost Accounting Standards, 9903.201-4(c), Disclosure and Consistency of Cost Accounting Practices, and 9903.201-4(d), Consistency in Cost Accounting, the following considerations apply:

(a) Increased costs shall be deemed to have resulted whenever the cost paid by the Government results from a change in a contractor's cost accounting practices or from failure to comply with applicable Cost Accounting Standards, and such cost is higher than it would have been had the practices not been changed or applicable Cost Accounting Standards complied with.

. . . .

(c) The statutory requirement underlying this interpretation is that the United States not pay increased costs, including a profit enlarged beyond that in the contemplation of the parties to the contract when the contract costs, price, or profit is negotiated, by reason of a contractor's failure to use applicable Cost Accounting Standards, or to follow consistently its cost accounting practices. In making price adjustments under the Cost Accounting Standards clause at 9903.201-4(a) in fixed price or cost reimbursement incentive contracts, or contracts providing for prospective or retroactive price redetermination, the Federal agency shall apply this requirement appropriately in the circumstances.

. . . .

(e) An adjustment to the contract price or of cost allowances pursuant to the Cost Accounting Standards clause at 9903.201-4(a) may not be required when a change in cost accounting practices or a failure to follow Standards or cost accounting practices is estimated to result in increased costs being paid under a particular contract by the United States. This circumstance may arise when a contractor is performing two or more covered contracts, and the change or failure affects all such contracts. The change or failure may increase the cost paid under one or more of the contracts, while decreasing the cost paid under one or more of the contracts. In such case, the Government will not require price adjustment for any increased costs paid by the United States, so long as the cost decreases under one or more contracts are at least equal to the increased cost under the other affected contracts, provided that the contractor and the affected contracting officers agree on the method by which the price adjustments are to be made for all affected contracts. In this situation, the contracting agencies would, of course, require an adjustment of the contract price or cost allowances, as appropriate, to the extent that the increases under certain contracts were not offset by the decreases under the remaining contracts.

(f) Whether cost impact is recognized by modifying a single contract, several but not all contracts, or all contracts, or any other suitable technique, is a contract administration matter. The Cost Accounting Standards rules do not in any way restrict the capacity of the parties to select the method by which the cost impact attributable to a change in cost accounting practice is recognized.

FAR 30.601, RESPONSIBILITY

(a) The cognizant ACO shall perform CAS administration for all contracts in a business unit notwithstanding retention of other administration functions by the contracting officer.

FAR 30.602, CHANGES TO DISCLOSED OR ESTABLISHED COST ACCOUNTING PRACTICES

Adjustments to contracts for CAS noncompliance, new standards, or voluntary changes are required only if the amounts involved are material. . . .

FAR 30.602-3, VOLUNTARY CHANGES

(a) The contract price may be adjusted for voluntary changes to a contractor's Disclosure Statement or cost accounting practices. The contractor must first notify the cognizant ACO by submission, not less than 60 days (or such other date as may be mutually agreed to) before proposed implementation, of a description of the accounting change and the general dollar magnitude of the change (including the sum of all increases and the sum of all decreases) for all CAS-covered contracts and subcontracts.

(b) The cognizant ACO shall review the accounting change concurrently for adequacy and compliance (see 30.202-7). If the change meets both tests, the ACO shall so notify the contractor and request that the contractor submit a cost impact proposal identifying all contracts and subcontracts containing the clause at 52.230-3, Cost Accounting Standards, and the clause at 52.230-2, Disclosure and Consistency of Cost Accounting Practices. The cost

impact proposal shall be in sufficient detail to allow evaluation and negotiation of the cost impact upon each affected CAS-covered contract and subcontract.

(c) With the assistance of the auditor, the ACO shall promptly analyze the cost impact proposal to determine whether or not the proposed change will result in increased costs being paid by the Government. The ACO shall consider all of the contractor's affected CAS-covered contracts and subcontracts, but any cost changes to higher-tier subcontracts or contracts of other contractors over and above the cost of the subcontract adjustment shall not be considered. Increased costs resulting from a voluntary change may be allowed only if the ACO determines that the change is desirable and not detrimental to the Government. The ACO shall then follow the procedures in 30.602-1(e).

(d) If the contractor fails to submit a cost impact proposal in the form and time specified or if the parties fail to agree concerning the cost impact, the cognizant ACO, with the assistance of the auditor, shall estimate the cost impact on contracts and subcontracts containing a CAS clause and shall then request the contractor to agree to the cost or price adjustment. The ACO may withhold an amount not to exceed 10 percent of each subsequent payment request related to the contractor's CAS-covered prime contracts, which contain the appropriate withholding provisions, until the proposal has been furnished by the contractor. The contractor shall also be advised that, in the event no agreement on the cost or price adjustment is reached within 20 days, action may be taken in accordance with the clause at 52.233-1, Disputes. If the ACO issues a unilateral determination under the Disputes clause, the ACO shall consider appropriate action to protect the Government's interests under Subpart 32.6.

FAR 30.001, DEFINITIONS [Rev'd March 2005]

As used in this part—

Affected CAS-covered contract or subcontract means a contract or subcontract subject to Cost Accounting Standards

(CAS) rules and regulations for which a contractor or subcontractor—

(1) Used one cost accounting practice to estimate costs and a changed cost accounting practice to accumulate and report costs under the contract or subcontract; or

(2) Used a noncompliant practice for purposes of estimating or accumulating and reporting costs under the contract or subcontract.

FAR 52.230-6, ADMINISTRATION OF COST ACCOUNTING STANDARDS (APR 2005)

For the purpose of administering the Cost Accounting Standards (CAS) requirements under this contract, the Contractor shall take the steps outlined in paragraphs (b) through (i) and (k) through (n) of this clause:

(a) *Definitions*. As used in this clause—

Affected CAS-covered contract or subcontract means a contract or subcontract subject to CAS rules and regulations for which a Contractor or subcontractor—

(1) Used one cost accounting practice to estimate costs and a changed cost accounting practice to accumulate and report costs under the contract or subcontract; or

(2) Used a noncompliant practice for purposes of estimating or accumulating and reporting costs under the contract or subcontract.