When last we **wrote about** Raytheon's three appeals of Contracting Officer Final Decisions (COFDs) related to concurrent changes in cost accounting practice made at its Space and Airborne Systems (SAS) business unit, we opined that "Raytheon is one of the few big defense contractors that seems to be willing to litigate its positions, when it believes that is positions have merit." While many other large defense contractors seem eager to settle based on an analysis of legal costs likely to be incurred, Raytheon seems to base its decision more on principle. (It's not the only contractor who seems to do this; there are others—and we'll be writing about Exelis soon.)

In that last article (link in the first sentence) we recapped Raytheon's win/lose statistics in the three appeals as follows:

Revision 1 – Government sought $1,176,600. Raytheon will have to pay nothing. Victory for Raytheon SAS.

Revision 5 – Government sought $512,732. Raytheon will have to pay not more than $153,000 (plus interest), which is the portion of the impact applicable to flexibly priced contracts. There will be a trial to adjudicate the application of a 30 percent mark-up factor by DCAA and whether the CFAO should have found the cost impact to be immaterial.

Revision 15 – Government sought $172,363. Raytheon will have to pay not more than $83,800 (plus interest), which is the portion of the impact applicable to flexibly-priced contracts. However, to the extent that the impact applies to pre-2005 contracts, Raytheon will be permitted to offset the impacts, which will reduce that value by roughly one-third. In addition, there will be a trial to adjudicate the application of a 30 percent mark-up factor by DCAA and

whether the CFAO should have found the cost impact to be immaterial.

The parties settled the dispute regarding the Revision 5 changes in August 2015, just a few weeks after they learned about the decision. We don't know what the settlement amount was but, as we noted above, it was going to be significantly less than the government had sought.

Which leaves us with the final set of concurrent changes to cost accounting practices, those disclosed in Revision 15 of SAS' Disclosure Statement, which was litigated as **ASBCA No. 58068**. Judge O'Connell wrote the decision for the Board and it was issued August 9, 2016 (though it was published weeks later). Today's article recaps that decision.

As we summarized **previously** —

There were three (3) individual changes described in Revision 15. Raytheon's GDM cost impact analysis showed that one change 'caused a $251,500 decrease to flexibly-priced contracts and an increase of $195,200 to fixed-price contracts' while the other two changes 'had the opposite effect.' According to Raytheon's calculations, change 2 (communications) 'caused an increase of $47,800 to flexibly-priced contracts and a decrease of $41,600 to fixed-price contracts' whereas change 3 (inventory maintenance) 'caused an increase of $36,000 to flexibly-priced contracts and a decrease of $17,400 to fixed-price contracts.' DCAA recognized that the aggregate or net effect of all the changes, when considered together, was to *decrease* costs to the government in the amount of $304,000. However, because of the then-recent rule changes to FAR 30.606, DCAA maintained that the impacts of the three changes could not be combined. Instead, each had to be considered individually. Using that logic, DCAA calculated a cost increase to the government of $157,080 related to two of the three changes.

Remember, at this point the government had already lost on the impacts related to contracts awarded before the 2005 FAR changes took effect (since Raytheon was allowed to offset the impacts from concurrent changes) and it had already lost on the "double-counting" issue, such that it would only be able to claim the impacts to one contract type (which we assume would be flexibly priced contracts). Left to be adjudicated were two remaining issues: (1) was DCAA allowed to mark-up the contractor's cost impact calculations by 30% to protect the government's interests, and (2) was the Cognizant Federal Agency Official (CFAO) required to consider the materiality of the cost impact before deciding to issue a COFD? The decision

issued by Judge O'Connell answers one of those two questions. (Unfortunately, because the Board's decision was based on other grounds, it never answered the question as to whether or not DCAA was permitted to add an arbitrary amount of additional costs to a contractor's cost impact analysis.)

As Judge O'Connell found, "In her final decision, the contracting officer noted that Raytheon had requested that she determine the changes were immaterial. The contracting officer did not specifically stated in her decision whether the changes were material [in amount], but the parties agree that she determined that the changes were material because they resulted in increased costs to the government." (Internal citations and redactions omitted.)

The debate to be decided by the Board concerned a discrepancy between the contracting officer's affidavit (offered as testimony) and her deposition. She was under oath for both sets of testimony, but they differed in crucial respects. In her affidavit, she testified that "she considered the materiality criteria in 48 C.F.R. § 9903.305 before issuing her final decision but had based her materiality determination solely upon the increased costs to the government." However, in an earlier deposition, the contracting officer "appears to indicate that she focused on the mere fact that there was an increased cost" and did not consider any other criteria. As Judge O'Connell wrote—

… we find that [the contracting officer] determined that the amount at issue was material based solely upon the dollar value, and that she did not properly consider the other factors in section 9903.305. … We conclude from this testimony that her analysis never progressed beyond the dollar amount, because she viewed the recovery of increased costs as necessary to protect the interest of the taxpayers.

Judge O'Connell recited the six factors that should be considered when determining whether costs are material or immaterial. If you are not familiar with them, we suggest you visit the CAS regulations and review them. He noted that FAR 30.602 requires a CFAO to "promptly evaluate a contractor's general dollar magnitude proposal and to conclude the cost impact process with no contract adjustments if he or she determines the cost impact is immaterial." Further (as Judge O'Connell noted), "FAR 30.602(a) provides that in determining materiality, the contracting officer 'shall use the criteria in 48 CFR 9903.305'."

After finding that the CFAO used but one of the six materiality factors to conclude that the cost impact was material, the Judge observed that use of some of the other factors might have led

her to a different conclusion. Judge O'Connell wrote—

While both the original impact amount, $142,800, and even the reduced amount of $56,146 appear to be significant amounts of money, they pale in comparison to the vastness of the relationship between Raytheon and the government. … the cost impact will be an increase of less than 0.005%. … Assuming for the moment that the changes impacted 1,000 contracts, the cost impact was an average of about $142 per contract … Further, because this amount was spread over four years, the impact may have been as low as $36 per contract, per year.

In other words, the cost impact was obviously immaterial to any reasonable person.

Because the contracting officer failed to consider the six materiality criteria as required by FAR 30.602, the ASBCA found that "the contracting officer abused her discretion." Further, "Because the government has failed to demonstrate that this error was harmless, the government cannot recover [any of] the cost increase." The appeal was sustained.

Another victory for Raytheon.

It should be noted that Raytheon was represented by the firm of Arnold & Porter in its appeals. (At one point, years ago, we had a small role as well.) Paul Pompeo, lead counsel, penned his own view of the decision **here** .

In addition to our observations, he noted the following—

One of the CAS materiality rule's factors, § 9903.305(e), states that a contracting officer assessing materiality must consider whether cumulative impacts "[t]end to offset one another." Although the ASBCA did not analyze this provision, the facts show that the overall decrease in cost to the Government on one change in cost accounting practice more than offset the total increased costs of the two other changes in cost accounting practice that were made to the CAS Disclosure Statement. An offset under these facts would have left an impact of zero, presumably another basis for the contracting officer to have found the cost immaterial and end the cost impact process. This is particularly important in light of a prior decision in this series of

cases where the ASBCA held that the prohibition in FAR 30.606(g)(3)(ii)(A) of offsetting cost impacts showing increased costs to the Government against cost impacts for other cost accounting practice changes showing decreased costs to the Government was valid. *Raytheon Co., Space & Airborne Sys.*, ASBCA Nos. 57801 *et al.*, 15-1 BCA ¶ 36,024. Moreover, the ASBCA's final decision, which sustained the appeal in Raytheon's favor based entirely on the issue of materiality rendered that portion of the 2015 decision on the question of the validity of FAR 30.606(g)(3)(ii)(A) unnecessary to the decision—hence; under the law of the Federal Circuit, it is nothing more than dicta, and non-precedential. *See, e.g., National American Ins. Co. v. U.S.*, 498 F.3d 1301, 1305 (Fed. Cir. 2007) (defining dicta).

In other words, he believes that this decision may have reopened the door to offset individual impacts from concurrent changes to cost accounting practice, despite the 2005 FAR revisions. If he is correct, that would be a stupendous outcome.