Many people believe that, when they receive a cost-type contract, they will be reimbursed for all costs incurred on that contract. That belief is wrong. First, the government customer will only reimburse the contractor for allowable costs (as defined at FAR 31.201-2). Costs that are not allowable will not be reimbursed. Second, there are a couple of contract clauses that impose a ceiling on the amount of costs that may be reimbursed, even if those costs are allowable. Those contract clauses are 52.232-20 (Limitation of Cost) and 52.232-22 (Limitation of Funds). The Limitation of Funds clause applies when the contract is being incrementally funded and the Limitation of Cost clause applies when the contract has been fully funded.

In order to have an adequate accounting system for government contracts, a company must show that it can comply with those contract clauses. Accordingly, it is very important that you understand those clauses and comply with them to the letter.

It's difficult to define the clauses with much specificity, because the contracting officer can tailor them for the individual contract. Suffice it to say that the clauses require the contractor to track its costs (and earned fee) against the amount funded to date (or against the total contract's estimated cost and fee), and report to the contracting officer before it has incurred a specified percentage of those values. Typically, the contractor must report 60 days before incurring 75 percent of the values, but that's not a given.

Right away it's clear that the contractor must be managing its costs and projecting its future expenditures, because if you wait until after you've passed the reporting values then you are already in noncompliance with the clause requirements. It's a difficult challenge, but one that must be met in order to have an adequate accounting system and receive cost-type contracts.

The challenge is even more daunting when one has received an ID/IQ contract with multiple task/delivery orders, each with its own ceiling values. The challenge is even more daunting than *that* when one thinks the ceiling values are associated with the ID/IQ contract *instead of* the individual task/delivery orders, but then one is informed by a court that the belief was wrong. Let's look at the recent Court of Federal Claims
decision
in the appeal of Interimage, Inc.

Interimage is a small woman-owned IT business, qualified under the 8(a) program to receive

special set-aside awards. In 2005, the Naval Criminal Investigative Service (NCIS) awarded Interimage a cost-plus-fixed-fee (CPFF) contract. The contract contained included eleven individual delivery orders.

Interimage performed the work satisfactorily and then submitted a (single) final invoice in the amount of $990,000, which "represented the difference between the amount paid and the amount InterImage claimed it was owed for both costs and fee." The problem was that NCIS lacked sufficient funding to pay the full amount of the final invoice. Interimage submitted a certified claim in the amount of $695.6K (the amount not paid). The contracting officer agreed but Interimage was unable to obtain payment. Interimage "was told that funding would need to come from other appropriations because the funds to pay InterImage had been de-obligated."

Subsequently, the Navy asserted that it did not owe Interimage anything more, because "the Navy had determined that InterImage was seeking payment for both costs and fee above various delivery order ceiling limitations."

Thus, the dispute centered on whether the contract established the limitation of cost/funds values, or whether it was each delivery order that did so. From the decision—

InterImage argues that it is undisputed that the amounts claimed for costs are within the base contract ceiling, as amended, and that the contract, and not the individual delivery orders, is controlling with regard to the contract ceiling limitation. InterImage also argues that the government's objections to InterImage's claim for its fee must be rejected on the ground that the government can only change the fixed fee through an equitable adjustment, which was not done. InterImage further argues that the amount InterImage has claimed for the fixed fee is justified based on the total hours of work performed under the contract as a whole.

… the government argues that the individual delivery orders and not the base contract set ceilings for costs and that InterImage is seeking payments above the ceilings set in the delivery orders in contravention of the limitation of cost and funds clauses in the Federal Acquisition Regulations ('FAR') and incorporated into the contract and delivery orders. With regard to the fixed fee, the government argues that InterImage's fixed fee also must be adjusted under the terms of the contract because the delivery orders provide limitations inclusive of fee and because InterImage did not perform the required hours under certain delivery orders and is thus not entitled to the amount of fixed fee now claimed.

Judge Firestone denied Interimage's motion for summary judgment, finding that there were issues of fact that needed to be adjudicated. In the meantime, she also found that the task/delivery orders established individual values that should be used in lieu of the overall contract values.

One of the problems was how DCAA had audited the contract and documented values in the Cumulative Allowable Cost Worksheet (CACWS). The DCMA Closeout Specialist stated "'[p]art of the issue appears to be DCAA's audit did not limit the direct and indirect cost to the contract ceiling and funding limitations for each [delivery order] on The Schedule of Cumulative Allowable Cost by Contract.'" He also stated that he believed the DCAA's schedule of cumulative allowable cost was incorrect in that the worksheet should have included entries for contract ceilings for each delivery order …."

"DCAA stated that although DCAA had 'potentially made an 'error' on the [cumulative allowable cost worksheet] . . . we all agree that the [cumulative allowable cost worksheet] is only a guideline for the Contracting Officer and the actual contract terms and ceiling limitations hold the ultimate authority.'"

(Contractors who have disputes with DCAA regarding the CACWS should memorize that quote, above, and use it as necessary.)

Long story short: DCAA and the contracting officer were willing to use the values at the overall contract level when establishing how much more Interimage should have been paid, but the more that Interimage complained about the lack of payment, the less willing the government was to see things the contractor's way. Eventually the CO was switched out and a new DCAA auditor was assigned, and suddenly Interimage owed the government $434,000 instead of the government owing Interimage $700,000! (Interesting to note that the new DCAA auditor was unable to locate the working papers of the previous auditor.)

Perhaps the parties will settle this dispute, now that Judge Firestone has made her ruling. Regardless, this is a good lesson on the importance of understanding contract terms (as well as individual task/delivery order terms) and making sure one is complying with them. Among the various contract terms for which compliance is required, the Limitation of Cost and Limitation of Funds stand out as being some of the most important.