In a recent article on the DOD Inspector General's semiannual report to Congress, we noticed that the DOD IG reported on the status of "significant post-award contract audits". (See Appendix E of the DOD IG report, linked at the end of **this article** .) According to the IG's report, as of September 30, 2009 there were 1,617 open audits that covered $5.06 billion dollars worth of DCAA-questioned costs. Of that total, 153 were in litigation and 1,085 were considered "overage"—i.e., not dispositioned by the cognizant Contracting Officer within 6 months of receipt. The amount of questioned costs associated with the overage contract post-award audit reports was $2.66 billion.

This matters because Contracting Officer delays in dispositioning audit findings can lead to a forfeiture of amounts to which the government would have otherwise been entitled in a court of law, as a very recent case at the Armed Services Board of Contract Appeals (ASBCA) demonstrates.

McDonnell Douglas Services, Inc. (MDS) vs. United States (ASBCA No. 56568, 12/02/2009)

involved a "post-award" (aka "defective pricing") DCAA audit finding related to MDS' subcontractor's proposed costs under its contract with the Royal Saudi Air Force for Foreign Military Sales (FMS) Technical Support Program (TSP) services in support of the Saudi F-15 fleet. (Note we have written about the FMS program, in general, **here**.) MDS was awarded a letter contract effective May 1, 1997 and that contract was definitized in early October, 1997. Pursuant to the Truth-in-Negotiations Act and its contract clauses (52.215-22 and 52.215-24), MDS certified that its cost or pricing data was current, accurate, and complete as of October 2, 1997.

MDS's subcontractor, Alsalam Aircraft Company (Alsalam) submitted its proposal to MDS on or about October 8, 1996. As the court noted, "Prior to award, Alsalam had submitted numerous documents to the Defense Contract Audit Agency (DCAA) containing or transmitting cost and pricing data. DCAA reviewed the documents and data and issued pre-award audit reports on 16 December 1996 and 16 April 1997." Alsalam certified that its cost or pricing data were current, accurate, and complete as of April 25, 1997, and it began performance on May 1, 1997. (These dates are important to the case, trust us.)

Less than a year after starting contract performance (February 10, 1998), DCAA's European Branch Office (DCAA EBO) initiated a "post-award" audit to evaluate whether Alsalam had complied with the disclosure requirements related to its subcontract pricing. On July 31, 1998 (five months later), the DCAA EBO issued a "preliminary Audit Report" in which it alleged that Alsalam had overstated both its site overhead and TSP program overhead costs because (1) Alsalam failed to include forecasts for future contract direct labor dollars in its proposed site overhead allocation base, and (2) Alsalam had failed to exclude unallocable amortization costs from its TSP overhead pool. (With respect to the latter finding, it seems that Alsalam had included an amount for amortization of "pre-operating costs" in its TSP overhead pool.) The DCAA recommended a downward price adjustment of $3.12 million.

Subsequently (May 3, 2000), DCAA revised its report and recommended a downward adjustment of $2.9 million. The revised audit report did not change any of the findings; it simply changed the resulting impact of the findings. Alsalam disputed the preliminary findings in a September 2, 2000 response. DCAA EBO issued its final audit report to DCAA's Boeing St. Louis Resident Office on March 22, 2001. In the final report, DCAA EBO recommended a downward price adjustment of $1.67 million—but, again, the underlying findings did not change significantly. The final report noted "coordination" between DCAA and the cognizant Air Force Contracting Officer at Warner Robins Air Logistics Center.

Just to recap the timing, DCAA initiated its audit of Alsalam in February, 1998 and issued its final audit report on March 22, 2001—more than three years after starting its audit work. But that delay wasn't really a problem; the problem was how long it took the St. Louis DCAA auditorso do anything with the DCAA EBO audit report.

It took an additional 14 months (until May 14, 2002), for the local DCAA St. Louis auditors to send a letter to the Boeing Company (who had acquired MDS during the time period) seeking "comments before we issue our final audit report" which recommended a prime contract price adjustment of $2.025 million (an amount that included MDS overhead and profit applied to Alsalam's questioned costs). In that letter, DCAA St. Louis reiterated the basis for the recommended price adjustment, which again had not changed from the original DCAA EBO findings. The final Audit Report was issued to the cognizant Warner Robins Contracting Officer by DCAA St. Louis on June 17, 2002—nearly 52 months after DCAA EBO initiated its audit work. But that delay wasn't the problem; the problem was how long it took the cognizant Contracting Officer to do anything with the DCAA St. Louis audit report.

It took nearly another *six years* for the cognizant Contracting Officer to issue a final decision on the matter. (In the meantime, there had been a change in Contracting Officer assignment to the contract.) As the judge noted—

The CO cited DCAA's Audit Report No. 3421-2002H42097001, the incorporated subcontractor Audit Report No. 2191-1998S42000315, and the same three bases for price adjustment asserted therein. He decided that MDS and Alsalam had failed to submit accurate, complete and current cost and pricing data as required by TINA and implementing contract provisions, thereby increasing the contract price by $2,024,877. He reduced the contract price by that amount and asserted that the Air Force was entitled to a refund in that amount, plus interest.

The Contracting Officer's final decision was issued on June 3, 2008 (and was confirmed on June 17, 2008). MDS appealed the decision to the ASBCA roughly three months later. Before the court was the question as to whether the Government's claim for a price reduction was time-barred by the six-year statute of limitations found in the Contract Disputes Act (CDA), 41 U.S.C. § 605(a). A similar provision is also found in the FAR, at 33.206 (Initiation of a claim).

The CDA language is as follows—

Each claim by a contractor against the government relating to a contract and each claim by the government against a contractor relating to a contract shall be submitted within 6 years after the accrual of the claim. The preceding sentence does not apply to a claim by the government against a contractor that is based on a claim by the contractor involving fraud.

As the court noted, the CDA does not define the phrase "accrual of a claim"—and that was the critical issue. If the claim accrued when the DCAA St. Louis office issued its final audit report (June 17, 2002) then the government's claim was just inside the six-year limit and would be valid. The government argued that was the date on which it knew of its damages in a "sum certain". On the other hand, if the claim accrued on March 21, 2001 (when the DCAA EBO issued its report and "coordinated" the findings and issues with the cognizant contracting officer), then the government's claim would be outside the six-year limit and would be rejected.

To answer the question, the court looked at the definitions section of FAR Part 33, at 33.201. The court found the definition it had been looking for, which read—

Accrual of a claim occurs on the date when all events, which fix the alleged liability of either the Government or the contractor and permit assertion of the claim, were known or should have been known. For liability to be fixed, some injury must have occurred. However, monetary damages need not have been incurred.

The court recited that the government had the burden of proving a claim for defective pricing damages—"In a defective pricing claim the government is required to prove that: (1) the information in dispute is 'cost or pricing data' under TINA; (2) the cost or pricing data was not meaningfully disclosed; and (3) the government relied to its detriment upon the inaccurate, noncurrent or incomplete data presented by the contractor."

The court adjudged that—

Here, we do not need to determine a precise date on which the government was on notice of, was aware of, or should have been aware of, its potential defective pricing claim against the prime contractor, because the undisputed and uncontrovertible facts demonstrate that the government had established the basis for its defective pricing claim against the prime contractor well before, and definitely no later than, 14 May 2002, more than six years before the COs' June 2008 decisions issued. Furthermore, in connection with its motion, appellant has not disputed the government's contention that the alleged defective pricing increased the contract price. This occurred as of contract definitization, with the logical consequence that the government incurred increased costs when contract performance began and, again, definitely no later than 14 May 2002.

The government's claim was determined to be time-barred and thus "it is not viable and cannot be considered." With a bit of finality, the court concluded as follows—

Because the government's defective pricing claim upon which the COs' decisions were based is time-barred and not cognizable under the CDA, the COs' decisions asserting the claim were not valid. If there is no valid CDA claim, any purported CO's decision on the matter is a nullity and we do not have jurisdiction to entertain an appeal from the purported decision.

The case is provided **here** .

DOD Instruction 7640.02 ("Policy for Follow-up on Contract Audit Reports") requires that "Findings and recommendations contained in contract audit reports shall be resolved and dispositioned in a timely manner which is consistent with legal statutes, regulations, and DoD policy." The DoDI requires, as a matter of policy, that the Director, DCAA must "Issue timely audit reports and provide timely and complete responses to contracting officers or review officials who request clarification or information supporting the audit findings and recommendations." Moreover, the DOD contracting officers are required to "resolve reportable audit reports within 6 months of report issuance." The Instruction provides for a Contract Audit Follow-Up (CAFU) database and periodic status reports. Obviously, one of the purposes of such a system is to prevent such a delay in resolution that a claim asserted by the government is time-barred, as happened in the MDS case before the ASBCA.

So as one ponders why it would take DCAA more than four years to notify the prime contractor of its recommended price adjustment related to a subcontractor's defective pricing, and why it would take the DOD contracting officer(s) another six years to officially issue a final decision demanding the price adjustment (plus interest), one might also wonder if the audit reports had been entered into the CAFU database, as DOD policy required. And if the DOD Instruction had been followed, would that have accelerated the process and lead to a successful government claim?

Perhaps that is merely idle speculation. But when we read from the DOD IG report that there are more than 1,000 "overage":post-award audit reports awaiting disposition, we can't help but asking how many of those are in a situation that is similar to the MDS case discussed here. And perhaps more worrisome is the question regarding how many audit reports aren't even in the CAFU database, leaving them invisible and uncounted in the DOD IG report?