

Contract Changes In Today's Contracting Environment

“Getting What Is Contractually Yours”

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PBMares Difference

- Established accounting and business-consulting firm with over 40 years of experience
- Nine offices throughout VA and MD
- Industry specialties include Government Contracting, Construction, Hospitality, Health Care, Financial Institutions, Not-for-Profit, Municipal Governments
- Strategic financial advisor attending to your different needs: assurance, tax, consulting, third part administration and wealth management.



PBMares Gov Con Team

- Experienced professionals knowledgeable about complex rules and regulations, such as FAR and CAS
- DCAA support
- Cyber security
- DFARS business systems
- Mergers and acquisitions and unique tax strategies
- Industry association involvement to stay ahead of the latest changes affecting government contractors
- Serving contractors in the aerospace, defense, manufacturing, technology, and construction industries



GovConConsulting2013

Helping Make the Pieces Fit

- Over 50 years providing Government contract consulting services in industry, public accounting and as an independent contractor
- Provide a proactive and realistic approach to compliance with Government contracting procurement regulations.



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Helping Make the Pieces Fit

- Specializing in assisting both emerging and established Government contractors in:
 - Development and implementation of compliant business systems,
 - Establishing indirect cost allocation and recovery maximization processes,
 - Preparation and negotiation of Requests for Equitable Adjustments and Termination Settlement Proposals,
 - Preparation of Incurred Cost Proposals,
 - Resolution of DCAA compliance issues.



What Are We Going to Discuss?

- Current Contracting Environment and It's Potential Impact
- What is a Request for Equitable Adjustment (REA)
- Contractor Responsibilities
- Types of Contracts Impacted
- Formal and Constructive Changes
- Excusable and Compensable Delays
- Costs to be Considered in Preparing an REA
- Certification Requirements



Current Environment!

- Sequestration
- Continuing Resolutions
- Decreased Budgets
- Increased Demands
- Changing Priorities
- Delayed Funding

**WITHIN EVERY
PROBLEM IS
AN
OPPORTUNITY.
DON'T
GIVE UP!**



What Does This Mean to the Contractor?

- Fewer contracts issued / more competition / more disputes
 - Sharpen pencils
 - Only propose what is requested
- Slower release of RFP's / slower award of contracts
- Delayed release of funds
 - Do **NOT** work at risk!



What Does This Mean to the Contractor?

- Need to be aware of contract requirements
 - Do **NOT** perform work without contractual authorization
 - Confirm authority of government representative requesting additional work
- Reduced government contracting knowledge



What Does This Mean to the Contractor?

- More frequent funding of incrementally-funded contracts
 - Government response to budget restrictions
 - Requires continual monitoring of funding needs
 - Exceed notification requirements of the Limitation of Costs / Limitation of Funding
 - **Stop work** if funding is not provided in a timely manner



What Does This Mean to the Contractor?

- Use of “Option to Extend Services” (Extension Clause) vs. exercising the “Option to Extend Term of Contract” (Option Clause)
 - Extension clause used for short-term extensions
 - Bid protest delays
 - Funding availability delays
 - Avoids negotiation of increased escalation
 - Extension clause avoids making long-term commitment
 - Communicate inappropriate use to the Contracting Officer



**“Gentlemen, we have run out of money.
Now we have to start thinking.”**

Winston Churchill, ca. 1941



What Should the Contractor Do?

Be Vigilant! Be Proactive!



Important to Recognize Changed Conditions

- Important to identify change conditions early
 - Requests for Equitable Adjustment (30 days)
 - Not always reasonable or practical
 - Courts have been more lenient
- Responsibility of all contractor personnel
 - Need to understand what the contract requires and what they are doing
 - Employee training and awareness is essential
- Immediately establish charge numbers and segregate costs
- Document all communications



Change Proposal Preparation Process

- Establish a change proposal team
 - Same process as preparing, submitting and negotiating a proposal prepared in response to an RFP
- Deserves the assignment of qualified personnel to ensure maximum cost recovery
- Requires top management support and a full-time team leader
- Need to establish priority parameters and anticipated completion date



What Needs to Be Proven!

- A need for an adjustment (**HARM**)
- The connection of HARM to the contract (**ENTITLEMENT**)
- The value of the HARM incurred (**QUANTUM/SUM CERTAIN**)

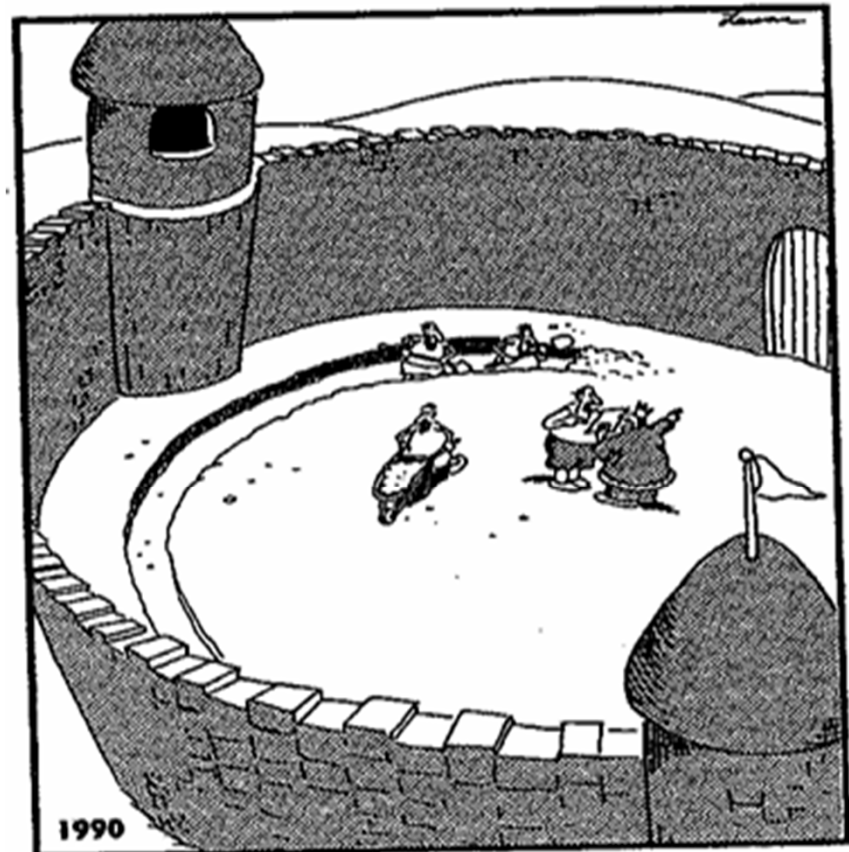


Think Outside the Box! Be Creative!



What Is an Equitable Adjustment?

- Government right to make changes
- Contractor right to an adjustment in contract price and/or schedule due to the change
- FAR does not explain their computation
 - Interpretations left largely to the courts



Suddenly, a heated exchange took place between the king and the moat contractor.

What It Is and What It Is Not!



- **IS** a non-competitive pricing action – subject to the Truth In Negotiation Act (\$750,000)
- **IS NOT** a vehicle to increase profits or reduce losses for reasons unrelated to the change

What Is the Concept?

- Determining the cost impact of a change or a multiple changes on a contractor
- Corrective measure used to keep the contractor “whole”



What Is the Concept?

- Difference between the:
 - **Planned cost of contract performance – not the proposed cost of performance – without** the change or changes, and
 - **Actual or projected cost of performance with the change or changes**
- Planned cost of contract performance may be less than that negotiated
 - Need to be able to prove the planned cost of performance



What Establishes the Right to an REA?

Verify the existence of the FAR changes clauses in your contracts.

- 42.212-10 Suspension of Work
- 52.212-13 Stop Work Order
- 52.212-14 SWO – Facilities
- 52.212-15 Gov't Delay of Work
- 52.236-2 Differing Site Cond.
- 52.243-1 Changes – FFP
- 52.243-2 Changes – CR
- 52.243-3 Changes – T&M/LH
- 52.243-4 Changes
- 52.243-5 Changes & Chg. Cond.
- Allow for adjustment to price and/or fee



What Are the Advantages of an REA?

- Improve profits by recovering costs not originally covered by the contract
- Increase competitiveness by allowing you to only propose what is requested
- Avoid the perception of contract mismanagement for cost overruns and performance delays



How Are Contracts Impacted?

- **Award-fee and Cost-type Contracts**

- You have an award-fee or cost-type contract with negotiated target costs, base fees and award fees based on established performance parameters
- Performance period is delayed and extended
 - Increasing costs incurred
 - Impacting the established performance parameters
- Increased costs incurred are paid but the negotiated base fee remains fixed
- No relief in parameters for earning award fees
- Extension of the contract performance fees impacts allocation of resources and performance of other contracts



How Are Contracts Impacted?

- **GSA Schedule Contracts**

- You are awarded a GSA schedule contract based on hourly rates discounted at the request of the Government due to the level of effort required
 - Sporadic utilization of your people causes the loss of expected efficiencies
 - Delays reduce the overall level of effort anticipated not supporting the discounts provided
 - Personnel had to be released or reassigned and rehiring and retraining expenses are incurred
 - Performance delays do not allow recovery of indirect costs included in the GSA schedule rates creating unabsorbed/mis-allocated overhead



How Are Contracts Impacted?

- **Time and Material and Labor Hour Contracts**
 - You are awarded a T&M/Labor Hour contract based on negotiated hourly rates
 - Sporadic utilization of you people cause the loss of planned efficiencies
 - Planned personnel were not available when needed due to delays and those with more (or less) qualifications had to be used
 - Personnel had to be released or reassigned to do delays and rehiring and retraining expenses are incurred
 - Performance delays do not allow recovery of the indirect costs included in the negotiated rates creating unabsorbed/mis-allocated overhead



How Are Contracts Impacted?

- **Fixed-Price Contracts**

- You are awarded a firm fixed-price contract to be performed at a given time for a known period and to established specifications
 - Start of the contract is delayed creating idle facilities and capacity and un-utilized personnel
 - Government furnished information is not provided when anticipated delaying contract performance and creating a loss of indirect expense absorption
 - Quality control requirements are increased causing delays and increased costs



How Are Contracts Impacted?

- A Stop Work Order is issued causing idle capacity, facilities and personnel
- Changed requirements made work already performed obsolete and requiring significant additional work
- Period of contract performance is extended with no ability to earn additional profits



Types of Changes

- **Express or formal changes**

- Directed by the CO
- Bilateral change including an agreed to price
 - Unilateral change issued prior to agreement on price
- Contractor must execute the change if within the scope of the contract

- **Constructive changes**

- Government does not know or refuses to admit to the change
- Up to the contractor to recognize the change and determine its impact
- Government needs to be convinced of the existence of the change and its value
- Almost always priced after the change has occurred



Common Causes of Constructive Changes

- Differing interpretation of contract requirements
- Acts of over inspection/ performance monitoring
- Defective specifications
- Failure to disclose superior knowledge
- Acceleration of contract performance
- Failure to cooperate
- Late exercise of an option after the contractually indicated expiration date
- Untimely notice to proceed
- Lack of access
- Differing site conditions
- Late or un-usable GFP/GFI



REA Conditions for Consideration

- Sporadic utilization of personnel causes the loss of planned efficiencies
- Reduced contract level anticipated did not support the discounts provided
- Personnel had to be released or reassigned and rehiring and retraining expenses are incurred
- Planned personnel were not available when needed due to delays and those with more or less qualifications had to be used



REA Conditions for Consideration

- Performance delays do not allow recovery of indirect costs included in the negotiated indirect rates creating unabsorbed overhead
- Start of the contract is delayed immediately upon award.
- Changes absorbed in a cost-type contract are paid but the base fee remained fixed
- No relief is given in the parameters for earning the award fees



REA Conditions for Consideration

- Required Government furnished information is not provided on-time delaying performance
- Quality controls are increased causing delays and increased costs
- A Stop Work Order is issued
- Requirements are modified making work already performed obsolete and requiring significant rework
- Changes were granted in the performance period but not in the contracts fixed-price.



Contract Changes Lead to Delays!



Changes = Delays

Delays = *Time*

Time = \$\$\$\$

Delays in Contract Performance

- **Excusable Delays**

- Does **NOT** allow for recovery of the cost of the delay
- Does allow for an extension or adjustment to contractual delivery dates
- Eliminates compensatory damages

- **Compensable Delays**

- Allows for the recovery of costs associated with the delay
- Allows for an extension or adjustment to contractual delivery dates



What Are Excusable Delays?

- Labor strikes
- Weather
- Sovereign acts of the government
 - War
 - Shutdowns?
- Subcontractor or supplier delays
- Unforeseeable unavailability of materials
- Floods
- Fire
- Epidemic
- Embargo
- Acts of God
- Financial difficulties caused by the Government



What Are Compensable Delays?

- Not issuing the Notice to Proceed within a reasonable time
- Not making the workplace available or allowing access to the worksite
- Not providing support personnel required
- Government interference with contractor's work
- Failure of the Government to cooperate in a timely manner
- Government delay in providing contractually established funding
- Unreasonable delay in inspection/approval of work
- Unreasonable delay in issuing change orders



Recovery of the Cost of Delay

- Entitled to recovery of the delay cost when the delay is unreasonable in duration
 - Contractor responsible for establishing unreasonableness of delay
 - Contractor ability to mitigate the delay can impact the determination of unreasonableness
- Entitled to recover entire delay if it is the fault of the Government
- No recovery of delay costs if there are concurrent delays on the part of the contractor



Recovery of the Cost of Delay

- Costs of requested acceleration **whether successful or not**
- Recover cost of delay from the time expected to complete **even if that date is earlier than stated in the contract**



Direct Cost Adjustments

- Direct Labor
 - Hourly rates – increased cost
 - Classification availability – changed cost
 - Loss of efficiencies – more hours
- Direct material
 - Escalation – increased cost
 - Loss of efficiencies – more material
 - Change in vendors – certification costs



Reclassification of Indirect Costs

- “Fair Compensation Principle” at FAR 49.201(a) allows reclassification of costs from indirect to direct
- Reclassified costs must be incurred specifically as a result of the change
- Avoid “double counting” by removing from indirect rate pools
- Use of business judgment – not strict accounting principles apply
- Need for reclassification results from inability to recover costs through overhead application – not planned
- DCAA will oppose reclassification – stand firm



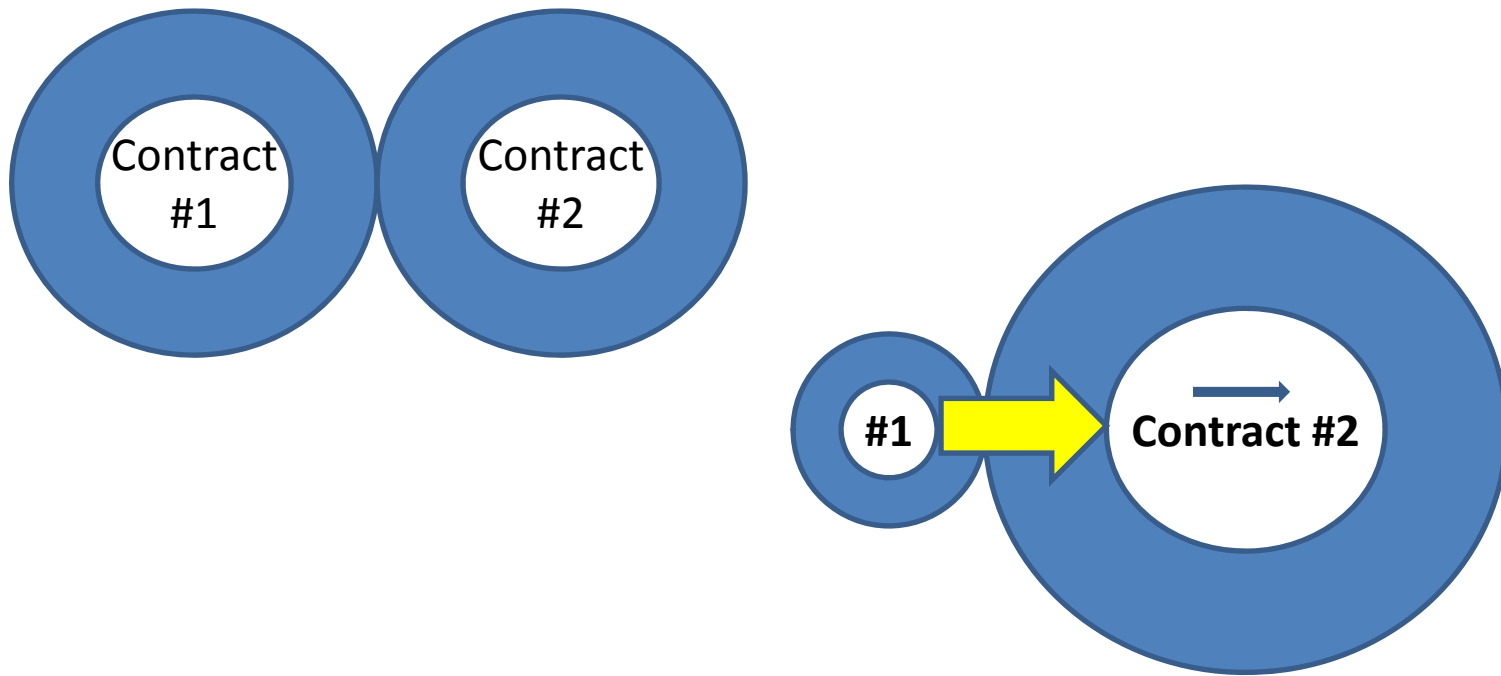
Unabsorbed/Misallocated Overhead

- A request to recoup overhead costs allocated, by default, to other contracts
- **Eichleay Calculation** – approximate determination of daily indirect expenses multiplied by the number of days of delay
 - Only acceptable means of calculation
 - Requires proof of compensable delay
 - Must have been on “standby” waiting for resumption of work
 - Must have been unable to take on additional/replacement work



Unabsorbed/Misallocated Overhead

Contracts As Negotiated/Planned



Resulting Contracts Actual Due To Change



Extended Program Support

- Time-oriented “core” support function
 - Program management
 - Project management
- Extension of contract period requires retention of the “core” support function
- Lower level of effort but unable to reassign



Idle or Excess Facilities and Capacity

- Idle facilities – completely unused and excess
 - Necessary to meet fluctuations in workload
 - Necessary when acquired
 - Must try to eliminate if possible and practical
 - Government will normally absorb for one year
- Idle Capacity – partially/temporarily unused facilities
 - Cost of doing business – recoverable
- Costs include maintenance, repair, taxes, insurance and depreciation



Personnel Costs

- Severance costs – recoverable
 - Required by law
 - Required by an employee=employer agreement
 - Paid under an established policy or implied practice
- Costs of rehiring terminated employees – recoverable
- Costs of retraining released or reassigned employees - recoverable



Material/Equipment Storage Costs

- Cost of space utilized
 - Internal costs of square footage (construction, utilities, maintenance, etc.)
 - External cost of renting or leasing space
- Additional security
- Effects of shelf life
- Re-inspection during storage and when removed
- Stocking and re-stocking
- Inventory control costs



Settlement Expenses

- Administrative and consulting costs incurred internally or through outside resources
 - Generally includes accounting, legal, clerical, management and similar costs
 - Internal costs must be removed from any indirect rate pools to eliminate duplicate recovery
 - Not a normal contract required cost so can be segregated and recovered as a direct cost



Settlement Expenses

- Recoverable both under REA and Termination situations
- Once the Contracting Officer makes their decision on REA proposal settlement costs incurred are not recoverable – **DO A GOOD JOB THE FIRST TIME!**



Profit Considerations

- Contract changes can impact the ability to recover anticipated profits
- Added efforts should be rewarded with additional profit
- Additional risk may demand additional profits
- Certain changes clauses allow for changes in price and profit
- Need to justify the level of profit requested
- No profit recovery on settlement expenses



Certification Requirements

- FAR 52.233-1, Disputes
 - Applies to all claims exceeding \$100,000
 - DCAA will not audit without certification
 - Certifies “claim” is made in good faith, amounts accurately reflects government liability and that signer is duly authorized to sign.



Certification Requirements

- DFARS 252.243-7002, Requests for Equitable Adjustment
 - Required for all Requests for Equitable Adjustment that exceed the simplified acquisition threshold of \$150,000
 - Does not apply to routine contract payments or adjustments under incentive provisions
 - Certifies “request” are made in good faith and not in dispute



Questions and Answers

Please use your Questions
pane to submit your questions.



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