

Financial Forum 2023 Selected Cost Principles – Compensation, Travel, Legal, and Related Costs

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Agenda

- Cost Allowability & Reasonableness
 - Overview
- Compensation
- Travel Costs
- Legal Costs
- Best Practices

Cost Allowability & Reasonableness

Cost Allowability Overview

- Allowable costs are limited to those defined under FAR Part 31 and refers to whether the Government will pay for a particular cost incurred in connection with a government contract.
- FAR 31.201-2:
 - (a) A cost is allowable only when the cost complies with all of the following requirements:
 - (1) Reasonableness.
 - (2) Allocability.
 - (3) Cost Accounting Standards (CAS).
 - (4) Contract terms and conditions.
 - (5) FAR Part 31 Cost Principles.
- Cost allowability applies to cost type contracts and pricing of fixed-price contracts when negotiated based on cost

Cost Reasonableness Overview

- FAR 31.201-3(a): “A cost is reasonable if, in its nature and amount, it does not exceed that which would be incurred by a prudent person in the conduct of competitive business.”
- Reasonableness considerations – is the type of cost:
 - Generally recognized as ordinary and necessary for the conduct of the contractor's business or contract performance?
 - Compatible with
 - Generally accepted sound business practices;
 - Arm's-length bargaining; and
 - Federal and state laws and regulations?
 - Consistent with the contractor's responsibilities to the government, other customers, business owners, employees, and the public?
 - A significant deviation from the contractor's established practices?

Cost Reasonableness Overview (cont.)

- The government evaluation of contractor cost reasonableness:
 - Courts are permitted to evaluate not only the process, but also employee decisions made implementing the process
 - DCAA and contracting officers may attempt to substitute their *post hoc* judgment for that of the contractor
 - Increases need to fully explain both reasonableness determinations and the context in which the determinations were made

KBR cases - Kellogg Brown & Root Servs., Inc. v. United States, 728 F.3d 1348 (Fed. Cir. 2013); Kellogg Brown & Root Servs., Inc. v. United States, 742 F.3d 967, (Fed. Cir. 2014), cert. denied, 135 S. Ct. 167 (Oct. 6, 2014)

Compensation for Personal Services

Employee Compensation

- FAR 31.205-6, Compensation for Personal Services
 - General Criteria:
 - Must be for work performed by the employee in the current year
 - Must be reasonable for the work performed
 - Must be based upon and conform to the terms and conditions of the contractor's established compensation plan or practice (consistent application)
 - No presumption of allowability when the contractor introduces major revisions of existing compensation plans or new plans, and prior to implementation (or within a reasonable period after it), the contractor has not provided the ACO an opportunity to review the allowability of the changes.

Travel Costs

Regulations Related to Travel Cost Allowability

- FAR 31.205-46, Travel Costs
- FAR 47.4, Fly America Act
- Related to travel costs:
 - General Rules on Allowability
 - FAR 31.205-6, Compensation
 - FAR 31.205-13, Morale, health, and welfare
 - FAR 31.205-14, Entertainment Costs
 - FAR 31.205-34, Recruitment Costs
 - FAR 31.205-35, Relocation Costs
 - FAR 31.205-43, Trade, Business, Technical, and Professional Activity Costs
 - FAR 31.205-51, Alcohol Costs

FAR 31.205-46, Travel Costs

- Costs incurred for official company business are allowable, subject to the limitations set forth in FAR 31.205-46.
- Costs must be documented:
 - Date and place (city, town or other similar designation) of the expenses;
 - Purpose of the trip;
 - Name of the person on the trip and that person's title or relationship to the contractor
- The cost of transportation must be a “reasonable charge” based on:
 - Mileage rates;
 - Actual costs incurred; or
 - A combination of the two

Airfare Costs

- Airfare costs in excess of the lowest priced airfare available to the contractor during normal business hours are unallowable.
- Exceptions:
 - Accommodations require circuitous routing
 - Unreasonable hours
 - Excessively prolonged travel
 - Increased costs that would offset transportation savings
 - Inadequate for traveler physical or medical needs
 - Incompatible with mission requirements
- Any exceptions must be documented and justified.

Business Class Travel

- There is no general threshold for when business class travel is allowable.
- Contractor must be able to show that the economy rates are unreasonable using a relevant exception.

Fly America Act

- FAR 27.4, Air Transportation by U.S. – Flag Carriers, implements the Fly America Act.
- The Fly America Act requires that contractors use U.S.-flag air carriers for U.S. Government financed international air travel and transportation, if available.
- U.S.-flag air carrier is considered “available” even if a foreign-flag carrier:
 - Provides a lower cost for a comparable service;
 - Is preferred by or more convenient for the agency or traveler; or
 - May be paid in excess foreign currency.

Fly America Act (cont'd)

- Exceptions:
 - Open-Skies Agreements
 - EU (not UK) – allows onward travel
 - Japan
 - Australia
 - Switzerland
 - US airline code-shares (US ticket on foreign metal)
 - Extends travel by 24 hours
 - No US non-stop / direct flight and:
 - requires more than 2 aircraft changes outside US
 - four hour stop-over, or
 - increases travel time by more than 6 hours
 - Flight time from origin to destination is less than three hours and using a U.S. flag carrier doubles the flight time

Contractor-Owned, -Leased, or –Chartered Aircraft

- As a general rule, travel costs via contractor -owned, -leased, or – chartered) in excess of standard commercial airfare costs are unallowable.
- Costs of travel include the costs of lease, charter, operation (including personnel), maintenance, depreciation, insurance, and other related costs
- Higher costs for travel by private aircraft may be allowable if:
 - Travel by such aircraft is specifically required by the contract
 - Higher costs are approved by the contracting officer.
 - When an advanced agreement has been reached
 - When commercial travel would require circuitous routing, travel during unreasonable hours, or excessively prolonged travel
 - Contractor must maintain and make available manifest/logs for all flights
 - Date, time, and points of departure;
 - Destination, date, and time of arrival
 - Name of each passenger and relationship to the contractor;
 - Authorization for the trip; and
 - Purpose of trip

Lodging, Meals, and Incidental Expenses

- A “reasonable charge” is calculated based on:
 - Per diem
 - Actual expenses; or
 - Combination of the two
- Only considered reasonable and allowable if charges “do not exceed on a daily basis the maximum per diem rates in effect at the time of travel” set forth in:
 - Federal Travel Regulation: Contiguous United States
 - Joint Travel Regulation, Volume 2 Appendix A (DoD) : Alaska, Hawai`i, outlying areas of U.S.
 - Standardized Regulations, Section 925: All other areas

Per Diem Rates

- Maximum per diem rates are a combination of lodging plus meals and incidental expenses
 - Contractors “are subject to only one ceiling, a total of lodging plus meals and incidental expenses.” DCAA, *Selected Areas of Cost Guidebook*, Ch. 72-1.3.
- When using the maximum daily per diem rates, DCAA presumes “that the costs are reasonable and allowable and detailed receipts or other documentation are not required to support claims by employees.” *Id.*
- Maximum per diem rates would not constitute a reasonable daily charge:
 - When no lodging costs are incurred; and/or
 - On partial travel days
- Contractors need to make appropriate downward adjustments to result in a reasonable charge

Actual Costs

- Actual costs in excess of per diems are allowed in “special or unusual situations.”
 - Actual costs may exceed per diem rates but cannot exceed the higher amounts authorized for federal civilian employees
 - Written justification
 - Approved by an officer of the contractor
 - JTR/FTR specifies circumstances for approval of actual expense
- Documentation requirements:
 - Track contractor policies
 - Receipt required for expenses over \$75
 - Retain required approvals
- All unallowable costs must be separately identified and excluded from billings, claims, and proposals

Related Cost Principles – Examples

- Alcohol (FAR 31.205-51) – shows up often with meals during travel
- Compensation (FAR 31.205-6) – hazard pay and bonuses
- Morale (FAR 31.205-13) - Recreation costs, food services at temporary sites
- Entertainment (FAR 31.205-14) – hotel movies, cable/internet in long term housing, certain meals or events
- Trade, business, technical, and professional activity costs (FAR 31.205-43) – travel for trade shows / conferences

Legal Costs

FAR 31.205-33, Professional and consultant service costs

- “Professional and consultant services”
 - Services rendered by persons who are members of a particular profession or possess a special skill and who are not officers or employees of the contractor
- Allowable when reasonable in relation to the services and when not contingent upon recovery of the costs from the government
- Some factors for allowability:
 - Nature and scope of the service rendered in relation to the service required
 - Necessity of contracting service (considering contractor’s capability)
 - Past pattern of acquiring services and costs
 - Impact of government contracts on the contractor’s business
 - Whether the services can be performed more economically by employment rather than by contracting
- Examples include legal, economic, financial, or technical consultants

FAR 31.205-47, Costs related to legal and other proceedings

- FAR 31.205-47 addresses costs of legal and other proceedings
 - Identifies specific unallowable legal proceedings
 - Costs of legal matters or proceedings generally allowable if not specifically made unallowable
 - Must be reasonable
 - Must comply with FAR 31.205-33
- Costs of actions for fraud and/or violation of law/regulation against contractor unallowable per FAR 31.205-47
 - Costs unallowable if result in:
 - Criminal conviction, finding of liability involving fraud, civil/administrative penalty, suspension or debarment, or termination of a contract for violation of law or regulation
 - Settled and could have resulted in one of the above outcomes
 - “Proceeding” must be brought by
 - Federal, state, local, or foreign government; or
 - A third-party in the name of the United States under the False Claims Act, 31 U.S.C. 3729–3733 (*qui tam*)
 - “Proceeding” includes an investigation

FAR 31.205-47, Costs related to legal and other proceedings (cont.)

- Costs of other types of non-fraud related proceedings unallowable per FAR 31.205-47
 - Connected with organization, reorganization, mergers and acquisitions
 - Defense of anti-trust suits
 - Patent infringement litigation unless provided for in contract
 - Bid protest costs
 - May recover if costs of defending protest are incurred pursuant to a written request from a CO
 - Defense or prosecution of suits between contractors, concerning:
 - Teaming agreement
 - Joint venture
 - Similar arrangements of shared interest
 - Except if required by contract or approved by CO

Best Practices

Best Practices

- Established policies/practices in accordance with cost principles
 - A key element of demonstrating cost reasonableness is establishing, maintaining, and consistently applying policies/procedures
 - Internal approvals and audits integrated into processes to ensure that documentation of business decisions is complete
 - Documentation requirements
 - Travel Policies
 - Frequent flier miles policy
- Reinforce Processes with Training
 - Regular training should occur on all policies/procedures
 - Document and retain records of attendance
- Advance Agreements

Thank you

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