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DEFECTIVE PRICING:
A VERY SHORT COURSE

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I. INTRODUCTION

The Truth in Negotiations Act ("TINA"), 10 U.S.C. § 2306a, is a disclosure statute. It requires contractors in certain circumstances to disclose to the government accurate, current, and complete "cost or pricing data" relevant to costs or prices proposed by the contractor. Its purpose is to level the negotiations playing field by ensuring that government negotiators have access to the same pricing information as the contractor's negotiators. TINA does ***not*** require the contractor to change its price. The theory is, however, that, with complete information, the government can negotiate the price down.

Accordingly, a good rule of thumb to follow to avoid trouble is that if you think that any information within the company might allow the government to negotiate a lower price, then the information almost certainly is cost or pricing data that must be disclosed.

The regulations implementing TINA are found in FAR Subpart 15.4. "Cost or pricing data" is defined in FAR 2.101, which is reproduced in Section II.C, below.

II. APPLICABILITY

A. Thresholds

TINA requires contractors to submit cost or pricing data in the following circumstances:

- Before the award of a prime contract awarded on the basis of other than sealed bid procedures and expected to exceed $700,000;

- Before the pricing of a contract modification expected to exceed $700,000;
- Before the award of a subcontract at any tier expected to exceed $700,000, if the prime or higher-tier subcontractors have furnished data;
- Before pricing a subcontract modification to such a subcontract expected to exceed $700,000.

B. Exemptions

Disclosure of cost or pricing data is not required:

- When the price is based on adequate competition. This exemption is based on the assumption that price competition will ensure the reasonableness of the price the government pays. Adequate price competition exists if:

  (1) The government solicits offers;

  (2) Two or more responsible offerors that can satisfy the government's requirements submit priced offers responsive to the solicitation's express requirements.

- When the item or service being acquired is a commercial item or service.

- When the price is set by law or regulation.

- In an "exceptional case" when the head of the agency determines that the Act's requirements may be waived.

- When modifying a contract or subcontract for a commercial item if the modification does not change the item from a commercial item to a noncommercial item.

  Caution: Contracts funded by DOD, NASA, or the Coast Guard require the submission of cost or pricing data for modifications to a commercial item contract if the total cost of the modifications exceeds the greater of $500,000 or 5% of the total contract price.

C. Definition of "Cost or Pricing Data"

The Act defines "cost or pricing data" as "all facts that, as of the date of agreement on the price of a contract (or the price of a contract modification), a prudent buyer or seller would reasonably expect to affect price negotiations

significantly. Such term does not include information that is judgmental, but does include the factual information from which a judgment was derived." Factual information is discrete, quantifiable information that can be verified.

The regulatory definition of FAR 2.101 is:

> "Cost or pricing data" (10 U.S.C. 2306a(h)(1) and 41 U.S.C. 254b) means all facts that, as of the date of price agreement or, if applicable, an earlier date agreed upon between the parties that is as close as practicable to the date of agreement on price, prudent buyers and sellers would reasonably expect to affect price negotiations significantly. Cost or pricing data are data requiring certification in accordance with 15.406-2. Cost or pricing data are factual, not judgmental; and are verifiable. While they do not indicate the accuracy of the prospective contractor's judgment about estimated future costs or projections, they do include the data forming the basis for that judgment. Cost or pricing data are more than historical accounting data; they are all the facts that can be reasonably expected to contribute to the soundness of estimates of future costs and to the validity of determinations of costs already incurred. They also include such factors as —
>
> (1) Vendor quotations;
>
> (2) Nonrecurring costs;
>
> (3) Information on changes in production methods and in production or purchasing volume;
>
> (4) Data supporting projections of business prospects and objectives and related operations costs;
>
> (5) Unit-cost trends such as those associated with labor efficiency;
>
> (6) Make-or-buy decisions;
>
> (7) Estimated resources to attain business goals; and
>
> (8) Information on management decisions that could have a significant bearing on costs.

1. "All Facts"

The term "cost or pricing data" has almost always been broadly construed. It has included not only a contractor's historical costs, but also in some instances:

- judgments
- projections
- estimates

either as facts in and of themselves or with respect to their factual content. *E.g.*, *Aerojet-General Corp.*, ASBCA No. 12264, 69-1 BCA ¶ 7664, *aff'd on reconsideration*, 70-1 BCA ¶ 8140 (internal engineering estimates – or, at least their factual content – showing vendor quote overstated are cost or pricing data); *Grumman Aerospace Corporation*, ASBCA No. 27476, 86-3 BCA ¶ 19,091 (draft narrative portion of prime contractor's report analyzing subcontractor quote deemed cost or pricing data, despite elements of judgment in the narrative, because the narrative added meaning to the prime's numerical assessment, which had been disclosed); *Texas Instruments, Inc.*, ASBCA No. 23678, 87-3 BCA ¶ 20,195 (computer generated report containing selected production run costs held to be cost or pricing data, notwithstanding the fact that selection of runs was judgmental, the averaged results were estimates, and judgments were, therefore, mixed with facts, *i.e.*, the actual cost data). In other words, the existence of an estimate is a fact as is each bit of verifiable information upon which the estimate was based.

2. "As of the Date of Price Agreement"

All facts "as of the date of price agreement" have been construed to mean the "shake-hands" date. Thus, all facts existing as of the shake-hands date must be disclosed, but new facts occurring after the shake-hand date need not be disclosed, although prudence dictates in some cases that they should be. More on that point shortly.

A significant difficulty for contractors arises in complying with this "currency" requirement. Typically, there are two "lag times" that create problems: (1) the time between the collection or last formal submittal of data and the shake-hands date and (2) the time between the receipt or creation of data within the contractor's organization and the communication of that data to the contractor's negotiator(s).

With respect to the first lag time – between collection or last formal submittal of data and the shake-hands date – although the regulations recognize that the currency of the data need only "be as close as practicable to the date of agreement on price" and that the parties may agree upon a currency cutoff date other than the price agreement date, the regulations and the required certificate of current cost or pricing

data effectively do not permit ***any*** lag time. Thus a contractor should vigilantly review outstanding proposals prior to an agreement to determine if changes or additions exist, such as new supplier quotations or projections and new or revised estimates or studies by relevant departments (*e.g.*, estimated overhead rates or labor improvement projections). This practice, known as a "sweep," is addressed in Section II.D.2, below. Absent wartime circumstances, there is generally no exculpatory excuse for the submission of defective data, even when there is very little time to prepare the proposal. *Compare Central Navigation and Trading Co., S.A.*, ASBCA No. 23946, 82-2 BCA ¶ 16,074 (response required within two weekend days in a war zone a valid excuse) *with Baldwin Electronics, Inc.*, ASBCA No. 19683, 76-2 BCA ¶ 12,199 (one month no excuse, particularly because contractors may decline to respond to government requests if time is insufficient).

With respect to the second period – between the creation of the data and its communication to a contractor's negotiator(s) – the Courts and Boards have not permitted ***any*** lag time. For example, in *Sylvania Electric Products, Inc. v. United States*, 202 Ct. Cl. 16, 23, 479 F.2d 1342, 1347 (1973), the Court stated:

> Plaintiff specifically argues . . . that the information was not "reasonably available." Plaintiff admits that the new information regarding the Rack Hardware was known to a branch of plaintiff-corporation approximately one week before the negotiating sessions, but that it takes "approximately thirty to thirty seven days" for this information to make its way to the firm's negotiators. ***This position we find untenable, even ludicrous. A simple telephone call could have obviated the situation***. [Emphasis added.]

The "no lag time allowed" holding of *Sylvania* is not, however, without contrary example. The Board in *Boeing Co.*, ASBCA No. 20875, 85-3 BCA ¶ 18,351, held that a three to four week period necessary to process data on labor hours and rates by a subcontractor using its normal accounting system (which did not segregate raw data by contract) made the data not reasonably available for disclosure purposes on a contract by contract basis, at least in the context of an urgent procurement. A prime contractor's lack of knowledge or possession of a subcontractor's cost or pricing data does not excuse the prime contractor's obligation to disclose accurate, current, and complete cost or pricing data for the subcontractor. *McDonnell Aircraft Co.*, ASBCA No. 44504, 03-1 BCA ¶ 32,154.

3. "That Prudent Buyers and Sellers . . . ."

In considering whether any particular piece of data should be disclosed, a contractor should not only determine whether the data have been relied on by the company in pricing but also: (1) whether it might in fact eventually become relevant to contract performance and (2) whether it might reasonably be used in pricing by others, despite the contractor's decision not to do so. In making this determination, it is prudent to err on the side of overdisclosure rather than underdisclosure.

Remember, your negotiators (or estimators) may have rejected the data or have been completely unaware of it, but those facts have no influence on whether the information is cost or pricing data. If data fits the definition, it must be disclosed. Moreover, do not be fooled by the phrase "affect price negotiations significantly," because the word "significantly" has been judicially written out of the law.

Understandably, contractors have argued that data which has only a *de minimus* effect on the price of a contract need not be disclosed. Almost uniformly, the Boards and the Courts have rejected this argument. Indeed, the Court of Claims expressly rejected this "*de minimus*" argument by holding that any data is significant, and thus must be disclosed, if it would have ***any*** effect on price. *Sylvania Electric Products, Inc. v. United States*, 202 Ct. Cl. 16, 479 F.2d 1342 (1973). *Accord Kaiser Aerospace & Electronics Corp.*, ASBCA No. 32098, 90-1 BCA ¶ 22,489, *aff'd on reconsid.*, 90-2 BCA ¶ 22,695 (failure to disclose current labor rates entitled the government to a price adjustment even though the nondisclosure had an impact of only $5,527 on total price of $2.7 million); *American Boesch Arma Corp.*, ASBCA No. 10305, 65-2 BCA ¶ 5280, *corrected decision issued*, 66-2 BCA ¶ 5747 (data affecting price by $20,000 on a contract with a target price of $15 million – less than 2/10 of one percent – held to be significant and thus requiring disclosure).

D. Submission of Pricing Data

- Submitting a proposal gives the contracting officer or authorized representative the right to examine records that formed the basis for pricing the proposal.
- The requirement for submitting cost or pricing data is met if the contractor either has submitted or identified in writing all cost or pricing data reasonably available at the time the parties agree to price.
    - When in doubt, disclose.
- A contractor must do more than merely submit (or make available) voluminous files and expect the government to locate the data pertinent to negotiation. The disclosure must be

meaningful. The contractor must identify data by answering these questions:

- What is it?
- Where is it?
- How was it used? and
- What does it represent?

- Significance: If the significance of certain data is not readily apparent, the contractor must explain its significance to the government.
- Once again, the contractor's duty to provide data is not limited to personal knowledge of the negotiators. Data anywhere within the organization are considered readily available.
- Government Knowledge: Failure to disclose cost or pricing data does not create liability for defective pricing if the government official authorized to receive the data has ***actual*** knowledge of the specific data. Constructive knowledge is not a defense.
- The contractor has an obligation to update the submission and disclose data that are in existence as of the date of the price agreement.

1. Practical Guidelines for Data Submission

- Always err on the side of pointing out data. Err on the side of inclusion.
- Draw a "road map" for the Contracting Officer or auditor; let them understand what it is you are disclosing. Ambiguity will only hurt the company.
- Make sure the government personnel with whom you negotiate are properly authorized representatives of the cognizant Contracting Officer or the prime contractor. Make all disclosure directly to or by "cc" to the Contracting Officer.
- Keep records of all data disclosed to government personnel after the original submission. Note when it was disclosed, and to whom it was disclosed.

- Maintain an index of all cost or pricing data and information accompanying or identified in the proposal, and a supplemental index of any revisions of such data up to the time of price agreement. Exempt these records from your records destruction policy.

2. A Checklist

- Furthermore, to ensure compliance it may be useful to create a checklist of all potential sources of cost or pricing data, the types of data used in the proposal, and the date each type of data was updated. An example of a checklist is attached.

E. Sweeps

Similarly, to ensure data currency, a "sweep," after the date of price agreement, looking for data existing but unknown to the negotiators as of the date of price agreement, may be required. The government is aware of this practice. The Defense Contract Audit Agency's ("DCAA's") Audit Manual states, for example:

> 14-120.4 Defective Pricing "Sweeps"
>
> a. A defective pricing sweep is a process whereby a contractor reviews its records to determine if more current cost or pricing data exist and need to be disclosed to the government. The sweep usually occurs after price agreement and the contractor submits this additional data to the government with its executed Certificate of Current Cost or Pricing Data. The additional data reflect cost or pricing data that were reasonably available at the time of price agreement but not submitted or disclosed before price agreement. As a result of FASA, FAR now allows a date other than the date of price agreement on price for certification (see 14-104.3). This and the encouragement to the contracting officer to use cutoff dates, where practicable, should reduce the need for sweeps.
>
> b. Sweep data appear defective in that the cost or pricing data were not submitted or disclosed to the government before the price agreement. However, if the government receives cost or pricing data with the certificate before the contract award, the contracting

officer has the opportunity to adjust the contract price for such data. In addition, procurement policy issued by the DoD in June 1989 (see 14-111c) requires contracting officers to reflect such data in the PNM and the extent to which they relied on it in establishing the contract price.

III. CERTIFICATION

A. TINA requires the contractor to certify that, to the best of its knowledge and belief, the cost or pricing data submitted are accurate, complete and current as of the date of agreement on price. The absence of a certificate does not eliminate defective pricing liability.

B. The date of agreement on price is the final day on which there is agreement. Thus, if there is a two-month negotiation, data submitted on day one must be updated as of day 60. Furthermore, the courts assume that if data are in existence anywhere within the company, they are available and should therefore be given to the government before final agreement on price.

C. The certificate must be submitted once (and only once) for each procurement; however, primes reasonably may seek a warranty of subcontractor data more than once. Usually the certificate should be submitted as soon as practicable after the agreement on price – that is, the shake-hands date.

Certificate of Current Cost or Pricing Data

This is to certify that, to the best of my knowledge and belief, the cost or pricing data (as defined in section 2.101 of the Federal Acquisition Regulation (FAR) and required under FAR subsection 15.403-4) submitted, either actually or by specific identification in writing, to the Contracting Officer or to the Contracting Officer's representative in support of _____* are accurate, complete, and current as of _____**. This certification includes the cost or pricing data supporting any advance agreements and forward pricing rate agreements between the offeror and the Government that are part of the proposal.

Firm _____

Signature _____

Name _____

Title _____

Date of execution*** _____

* Identify the proposal, request for price adjustment, or other submission involved, giving the appropriate identifying number (e.g., RFP No.).

**Insert the day, month, and year when price negotiations were concluded and price agreement was reached or, if applicable, an earlier date agreed upon between the parties that is as close as practicable to the date of agreement on price.

*** Insert the day, month, and year of signing, which should be as close as practicable to the date when the price negotiations were concluded and the contract price was agreed to.

IV. PROTECTING PRICING DATA FROM DISCLOSURE

A. Pursuant to FOIA Exemption 4, the government is not obliged to disclose information consisting of trade secrets and commercial or financial information obtained from a person, which is privileged and confidential. If the contractor considers the information to be confidential or privileged, each page of the proposal containing the information should be marked with a legend to that effect.

B. Information is considered confidential if disclosure would impair the government's ability to obtain necessary information in the future and would cause substantial harm to the competitive position of the person from whom the information was obtained.

- Line item price information is considered to be confidential commercial or financial information.

C. The FAR prohibits the release of a contractor's cost breakdown, profit, overhead rates, trade secrets, manufacturing processes and techniques, or other confidential business information. FAR § 15.503(b)(1)(v); § 15.506(e).

V. DEFECTIVE PRICING LIABILITY

A. TINA authorizes the contracting officer *unilaterally* to adjust the contract price to exclude any significant amount by which the price was increased because the contractor or a subcontractor submitted defective

data. TINA was amended in 1986 to provide for interest on overpayments and double damages for knowingly false data.

B. The prime contractor is absolutely liable for the defective data of its subcontractors, and it is required to get that data from all non-exempt actual subcontractors and certain prospective subcontractors. Subcontracts often contain indemnification clauses holding the prime contractor harmless in the event of a price reduction based on defective subcontractor cost or pricing data.

VI. CIVIL AND CRIMINAL LIABILITY

The difference between civil liability for defective pricing and criminal liability for defective pricing is the intent of the contractor. The inadvertent submission of defective data may result in a contract price reduction. An intentional or knowing submission of defective data subjects the contractor to a wide variety of civil and criminal penalties including substantial fines, imprisonment of individuals, and suspension and debarment of the company. The government regards the following actions as evidence of fraudulent intent:

- Falsification or alteration of data;
- Failure to update data even though the contractor knows that costs or prices have decreased; and
- Failure to make complete disclosure of known data to responsible government personnel.