

## Contract Administration

# Activity 44: Defective Pricing

*Procedures for identifying and addressing contractor defective cost or pricing data and offsets.*

**Related Flow Charts:** [Flow Chart 44](#)

**Related Courses:** [CLC 056](#), [CLC 058](#)

Tasks	FAR Reference(s)	Additional Information
1. Identify factors that suggest cost or pricing data may be defective.	Defense Contract Audit Agency Contract Audit Manual (DCAM) 14-117 Possible Defective Pricing Indicators.	<p>Indicators of defective cost or pricing data may be uncovered during day-to-day operations or during reviews of contractor operations (e.g., technical reviews for negotiating other related contracts, purchasing system reviews, or contract performance reviews). Examples of situations that may raise your concern about possible defective pricing include:</p> <ul style="list-style-type: none"><li>• Incurred costs (either generally or in a particular category) seem to be running significantly less than projected.</li><li>• Operations included in the contractor's proposal are not actually performed in completing the contract.</li><li>• Direct cost items included in the proposal appear to be priced higher than they should be based on information available to the contractor (and not disclosed to the Government) at the time of contract price agreement.</li><li>• Data presented during later negotiations with the same company provide information that is significantly different from that presented in earlier negotiations.</li><li>• Data collected during market research for a subsequent contract are inconsistent with the certified data.</li><li>• Defective pricing is identified on related contracts.</li><li>• Operating budget plans (e.g., indirect cost budgets)</li></ul>

Tasks	FAR Reference(s)	Additional Information
		<p>contain data that are different from the data in the contract proposal.</p> <ul style="list-style-type: none"> <li>• Labor-mix estimates do not include data on the actual labor mix on the same or similar contracts.</li> <li>• Review of other proposals indicates that the value of the contractor's inventory was erroneously computed or the latest valuation was not reflected in the contractor's proposal.</li> <li>• Estimating system reviews reveal deficiencies in procedures for identifying and submitting cost or pricing data.</li> <li>• Contractor pricing personnel or negotiators informally state that they failed to follow contractor internal pricing policy or estimating and/or purchasing manual instructions.</li> <li>• Technical review of contract performance indicates that quantity estimates were erroneous because the contractor did not use current product drawings or failed to read drawings correctly.</li> <li>• Purchasing reviews indicate that the contractor did not submit available evaluations of vendor quotations or failed to reveal changes in its evaluations.</li> <li>• Purchasing reviews indicate that purchase order cancellations were not disclosed to the Government.</li> <li>• Later technical evaluations indicate that the contractor did not disclose projected increases in business volume that would affect current and projected overhead and general and administrative expense rates.</li> <li>• Contract performance reviews indicate that the contractor duplicated cost estimates for the same task.</li> <li>• The make-or-buy plan submitted with the proposal is significantly different than the plan being used in contract performance.</li> </ul>

Tasks	FAR Reference(s)	Additional Information
<p>2. Discuss concerns about possible defective pricing with the contractor and the auditor.</p>	<p>FAR 15.407-1(d) Defective certified cost or pricing data.</p>	<ul style="list-style-type: none"> <li>• New or revised production processes which will be used in contract performance were not disclosed.</li> </ul> <p>After contract award, investigate whenever you suspect that the data provided by the contractor or subcontractor were not accurate, complete, and current as of the close of negotiations or (if applicable) on another agreed-upon date.</p> <p>To ensure that you understand the situation, you may wish to contact the contractor to discuss your suspicions before contacting the cognizant auditor. During your discussions:</p> <ul style="list-style-type: none"> <li>• Describe the data that you suspect are defective.</li> <li>• Unless it would jeopardize the Government's position, describe the reasons that you suspect that the data are defective.</li> <li>• Obtain the contractor's position on whether the cost or pricing data were accurate, complete, and current.</li> </ul> <p>Document your suspicions and the results of your discussions with the contractor. Place a copy in the affected contract file(s).</p> <p>If you are not satisfied with the contractor's position, you may wish to informally contact the cognizant auditor before requesting a defective pricing audit. A situation that appears suspicious may, in fact, result from using acceptable accounting and estimating practices.</p>

Tasks	FAR Reference(s)	Additional Information
<p>3. Consider the significance of the possible defective pricing.</p>	<p>FAR 15.407-1(c) Defective certified cost or pricing data.</p> <p>FAR 52.215-10, Price Reduction for Defective Certified Cost or Pricing Data.</p> <p>FAR 52.215-11 Price Reduction for Defective Certified Cost or Pricing Data—Modifications.</p> <p>DCAM 4-304-3 Postaward Audits of Certified Cost or Pricing Data for Possible Defective Pricing.</p>	<p>The FAR defective pricing clauses provide that the Government is entitled to remedies if a contract price was increased by any “significant amount” because the contractor provided cost or pricing data that were not accurate, complete, and current. However, it does not define what amount is significant.</p> <p>One Board of Contract Appeals found that the Government was entitled to a reduction of \$5,000 even though that amount was only two-tenths of one percent of the contract price. The decision pointed out that the language of the Truth in Negotiations Act does not vest in a contractor the right to keep amounts obtained through supplying defective pricing data on the grounds that the amount so obtained was insignificant in relation to the overall contract price.</p> <p>However, substantial resources are required to identify, pursue, and settle defective pricing allegations. Accordingly, you should consider the materiality of alleged defective pricing before you decide to pursue the allegation.</p> <p>There is no universal Government policy on materiality, but DCAA provides one useful guideline. In DCAA potential price adjustments of less than five percent of contract price or \$50,000, whichever is less, are normally considered immaterial and not pursued unless:</p> <ul style="list-style-type: none"> <li>• A contractor's deficient estimating practices have resulted in recurring defective pricing; or</li> <li>• The potential price adjustment is due to a system deficiency, which affects all contracts priced during the period.</li> </ul>

Tasks	FAR Reference(s)	Additional Information
<p>4. If you still suspect that the contract price significantly increased because of defective cost or pricing data, request an audit to evaluate the accuracy, completeness, and currency of the cost or pricing data submitted by the contractor through the close of negotiations.</p>	<p>FAR 15.407-1(c) Defective certified cost or pricing data. DCAM 4.304.3 Postaward Audits of Certified Cost or Pricing Data for Possible Defective Pricing.</p>	<p>Provide the following information in the request:</p> <ul style="list-style-type: none"> <li>• Identify the data that you suspect are defective.</li> <li>• Describe, in detail, your reasons for suspecting that the data are defective.</li> <li>• Provide the auditor a copy of: <ul style="list-style-type: none"> <li>○ The price negotiation memorandum (PNM) if one was not previously provided.</li> <li>○ The final proposal index of cost or pricing data provided by the contractor.</li> <li>○ Any cost or pricing data provided to the contracting officer to support the contractor's pricing proposal, but not previously provided to the auditor.</li> </ul> </li> </ul> <p>If the auditor needs any additional information or support to complete the audit, provide it in a timely manner.</p>
<p>5. Prepare a defective pricing memorandum documenting the determination and any corrective action taken as a result.</p>	<p>FAR 15.407-1(d) Defective certified cost or pricing data. FAR 33.211 Contracting officer's decision [disputes and appeals].</p>	<p>The pricing memorandum must include the following:</p> <ul style="list-style-type: none"> <li>• The contracting officer's determination as to whether or not the submitted data were accurate, complete, and current as of the date certified and whether or not the Government relied on the data; and</li> <li>• The results of any contractual action taken.</li> </ul>
<p>6. Distribute the memorandum.</p>	<p>FAR 15.407-1(d) Defective cost or certified pricing data.</p>	<p>Distribute the defective pricing memorandum as follows:</p> <ul style="list-style-type: none"> <li>• Send one copy to the cognizant auditor.</li> <li>• If the contract has been assigned for administration, send one copy to the administrative contracting officer (ACO).</li> <li>• Provide a copy of the memorandum or other notice of the determination to the contractor.</li> </ul> <p>Distribute other contractual documents as required by FAR and agency procedures.</p>

Tasks	FAR Reference(s)	Additional Information
<p>7a. If the amount due the Government exceeds the amount remaining on the contract, issue a demand letter.</p>	<p>FAR 15.407-1(b)(1) Defective cost or certified pricing data [demand letter].</p>	<p>Ensure that the contract modification and any demand letter include the following information:</p> <ul style="list-style-type: none"> <li>• The repayment amount.</li> <li>• The penalty amount (if any).</li> <li>• The interest amount through a specified date.</li> <li>• A statement that interest will continue to accrue until the date repayment is made.</li> </ul>
<p>7b. If the cost or pricing data was understated, consider an offset.</p>	<p>FAR 15.407-1(b) Defective certified cost or pricing data.</p>	<p>The amount of the offset may equal, but not exceed, the amount of the Government’s claim for overstated cost or pricing data arising out of the same pricing action.</p> <p>An offset must be allowed only in an amount supported by the facts and if the contractor:</p> <ul style="list-style-type: none"> <li>• Certifies to the contracting officer that, to the best of the contractor’s knowledge and belief, the contractor is entitled to the offset in the amount requested; and</li> <li>• Proves that the certified cost or pricing data were available before the “as of” date specified on the Certificate of Current Cost or Pricing Data but were not submitted. Such offsets need not be in the same cost groupings (e.g., material, direct labor, or indirect costs).</li> </ul> <p>An offset must not be allowed if:</p> <ul style="list-style-type: none"> <li>• The understated data were known by the contractor to be understated before the “as of” date specified on the Certificate of Current Cost or Pricing Data; or</li> <li>• The Government proves that the facts demonstrate that the price would not have increased in the amount to be offset even if the available data had been submitted before the “as of” date specified on the Certificate of Current Cost or Pricing Data.</li> </ul>

Tasks	FAR Reference(s)	Additional Information
<p>8. Conduct settlement discussions with the contractor to reach a bilateral agreement.</p>	<p>FAR 15.407-1(d) Defective certified cost or pricing data.  FAR 33.210 Contracting officer's authority [disputes and appeals].</p>	<p>If the contracting officer believes it would benefit discussions, the cognizant auditor may be invited to participate.</p> <p>In attempting to reach settlement do not—</p> <ul style="list-style-type: none"> <li>• Make an agreement that precludes further defective pricing audit reviews on the same or other contracts.</li> <li>• Make an agreement that is contingent upon settling defective pricing found in other contracts.</li> <li>• Accept contractual goods or services on the same or other contracts as compensation for, or disposition of, a defective pricing case.</li> <li>• Credit the amount of defective pricing in negotiating a concurrent or subsequent contract, including a follow-on contract.</li> <li>• Adjust only one contract for defective pricing when the same defective pricing was cited on multiple contracts with the same contractor.</li> </ul> <p>Settle, compromise, pay, or otherwise adjust any claim involving fraud, or any claim or dispute for penalties or forfeitures prescribed by statute or regulation that another Federal agency is specifically authorized to administer, settle, or determine.</p>
<p>9a. If a settlement is reached, modify the contract to reflect the defective pricing settlement.</p>	<p>FAR 15.407-1(b)(1) Defective cost or certified pricing data.</p>	<p>If the contract price is reduced as a result of the alleged defective pricing, document the price reduction in a contract modification.</p>
<p>9b. If a settlement is not reached, issue a final decision in accordance with Contract Disputes statute.</p>	<p>FAR 15.407-1(d) Defective certified cost or pricing data.  FAR 33.211 Contracting officer's decision [disputes and appeals].</p>	<p>See Activity 49: Resolving Disputes for further discussion.</p>

Tasks	FAR Reference(s)	Additional Information
<p>10. Upon issuing a final determination that the contractor submitted defective cost or pricing data, ensure that information relating to the determination is reported in the Federal Awardee Performance and Integrity Information System (FAPIIS) module of CPARS.</p>	<p>FAR 15.407-1(d) Defective certified cost or pricing data.  FAR 42.1503(h) Other contractor performance information [procedures].</p>	<p>Agencies must ensure information is accurately reported in FAPIIS module of CPARS within three calendar days after the contracting officer issues a final determination that a contractor has submitted defective cost or pricing data.</p>