

# Government Contracts Blog

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## Working Like a Highway Road Crew -- Government Finally Amends SF 1443 to Eliminate References to "Paid Cost Rule," a Mere *Seven Years* After the Fact

In November 2002, the FAR Councils eliminated the so-called "paid cost" rule from the FAR, which had previously prevented federal prime contractors other than small businesses from recognizing incurred subcontractor costs for purposes of progress billing until "payment by cash, check, or other form of actual payment" had *actually* been made. *See* 67 Federal Register 70520 (Nov. 22, 2002). The Government form used to request progress payments, the Standard Form (SF) 1443, Request for Progress Payments, implemented the paid cost rule by requiring large contractors to identify "paid costs eligible under progress payments clause" (Line 9) and "incurred costs eligible under progress payments clause" (Line 10). *See* FAR 53.301-1443 (2008) (last updated in October 1982). Bizarrely, however, when the paid cost rule was eliminated in 2002, the SF 1443 was **not** updated to remove these two lines. Now -- a mere six years and eight months since the elimination of the paid cost rule -- the FAR Councils have *finally* issued a revised SF 1443, removing Lines 9 and 10 and thereby eliminating the last vestiges of the long-defunct rule. *See* 74 Federal Register 28430 (Jun. 15, 2009).

The FAR Councils' reasons for delaying removal of these two lines are, and likely will forever remain, a mystery. Surely, however, the FAR Councils could reasonably have foreseen that significant delay in updating the form would be confusing, disruptive, and costly for both contractors and Government personnel. The Councils' delay of almost seven years is bewildering, especially in light of the fact that the elimination of the paid cost rule was part of a major effort commencing in 2000 in which the FAR Councils sought to revise the contract financing provisions "to make them easier to understand and to minimize the burdens imposed on contractors and contracting officers." 65 Federal Register 16276 (Mar. 27, 2000).

### **The Demise of the Paid Cost Rule**

FAR Subpart 32.5 and FAR 52.232-16 allow the Government to make financing payments to a contractor based on the contractor's costs incurred to date. While the FAR generally prefers performance-based financing payments (based on a pre-defined performance schedule and achieving certain milestones) (as outlined in FAR Subpart 32.10 and FAR 52.232-32), making progress payments to contractors based on their costs continues to be an important financing tool for the Government.

Beginning in the mid-1990s, the Government undertook a number of initiatives to revise and simplify the policies and procedures relating to federal procurement. One revision was the elimination of the paid cost rule. Historically, the paid cost rule required prime contractors to "front" payments to subcontractors before they could submit a progress payment request for the subcontractor's bills. However, beginning in 2000 the FAR was amended to eliminate (in part) the rule. *See* 65 Federal Register 16276 (Mar. 27, 2000) (revising the paid cost rule by creating exceptions, while still leaving the principle in other sections of the FAR); 65 Federal Register 56454 (Sep. 18, 2000) (removing the paid cost rule with regard to time & materials and labor hour contracts). In 2002, the FAR Councils finally amended the applicable contract clause, FAR 52.232-16, Progress Payments. This change allowed all contractors (both large and small) to invoice the Government for unpaid amounts determined to be due and payable to subcontractors, as long as the contractor ordinarily pays the amount within 30 days of the submission of the contractor's payment request to the Government. *See* 67 Federal Register 70520 (Nov. 22, 2002). Notably, however, SF 1443, the form by which progress payments are requested, was *not* amended in 2002, with Lines 9 and 10 of SF 1443 continuing to request information as to "paid costs eligible under Progress Payment clause" and "incurred costs eligible under Progress Payment clause." The elimination of the rule in 2002 had the instantaneous effect of rendering the information requested on Line 9 completely and obviously irrelevant -- yet SF 1443 remained unchanged, like a fossil frozen in time.

### **Government Sanctioned "Fudging" In Completing the Old SF 1443**

For Department of Defense contracts, the Defense Contract Audit Agency (DCAA) is charged with: (1) verifying the amounts included on a SF 1443 to the contractor's accounting records; (2) evaluating the propriety of the progress payment request in accordance with the provisions of the contract; and (3) determining whether undue financial risk to the Government will result if the request is granted. *See* DCAA Contract Audit Manual (DCAM) § 14-203(a) (2008). Perhaps ironically for an agency that insists on contractor compliance with numerous counterproductive and sometimes nonexistent rules, DCAA recognized in 2003 the irrelevance of the information on Lines 9 and 10, advising its auditors that "large contractors should not complete [Line 9] and should follow the same instructions to complete SF 1443 as provided for small contractors. All contractors should complete [Line] 10." DCAM § 14-205(d) (2003). While DCAA's internal guidance ignored a glaring irregularity to achieve the overall regulatory purpose behind the form, the fact remains that large contractors have long been required to **certify** their SF 1443s, which have been outdated and inaccurate for the past seven years. We have previously observed as to this exact issue that "a form that is outdated and requires contractors to ignore the form's own instructions has no place in the Federal system. For such a form to require certification is an outrage."

The failure to update the form was also necessarily costly. The cost to Government and industry alike over the past several years in addressing the problems with the SF 1443 has been significant, as demonstrated by the DCAA audit guidance instructing contractors and auditors (essentially) "to fudge the numbers." We would like to see the procedures implementing the Paperwork Reduction Act (44 U.S.C. § 3501 *et seq.*) used for once to develop an honest estimate of the time and labor associated with completing and modifying the old, inaccurate SF 1443 --

only this time, the Government can report on the cost of the delay in implementing these new and extraordinarily simple changes to SF 1443.

### **The New, Updated Form SF 1443**

Recognizing the inadequacy of the old SF 1443 the Department of Defense eventually requested comments in 2004 – yes, it took them two years to get around to this, but let’s not carp, OK? – on “what improvements could be made to the form,” hoping to simplify the form and hoping to improve consistency with the revised Progress Payments clause. *See* 69 Federal Register 67899 (Nov. 22, 2004). But, recognizing a problem and taking prompt action to resolve it are two different things; in this case, the FAR Councils waited *four more years* until April 2008 to publish a proposed rule amending SF 1443 and proposing the deletion of Lines 9 and 10. *See* 73 Federal Register 19035 (Apr. 8, 2008). It was not until June 2009 that the FAR Councils ultimately issued the final amendment. *See* 74 Federal Register 28430 (Jun. 15, 2009).

### **Conclusion**

We have discussed the FAR Councils' tendency to delay issuance of regulations in [prior postings](#) and did not set out to do so again in this case. However, the long and tortured course of events leading up to the red-letter day when SF 1443 was finally updated to allow contractors to file straightforward and understandable payment requests seems to confirm that, as to the FAR Councils' mode of operation, such delay is *representative* rather than *anomalous*. We can take some comfort, however, that in this case, after nearly seven years of what must have been intense internal deliberations (Steven Spielberg has reportedly purchased the movie rights), the FAR Councils got it right. Thus it has not always been.

Authored by:

[W. Bruce Shirk](#)  
(202) 741-8426  
[bshirk@sheppardmullin.com](mailto:bshirk@sheppardmullin.com)

and

[David S. Gallacher](#)  
(202) 218-0033  
[dgallacher@sheppardmullin.com](mailto:dgallacher@sheppardmullin.com)