

ALERT

# Indirect Cost and Profit Recovery for Increased Wages

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The Civilian Board of Contract Appeals last month issued an important decision permitting broad recovery under the contract Changes clause for a construction contractor performing a contract subject to the Davis-Bacon Act. In *W.G. Yates & Sons Construction Co.*, CBCA 1495, Dec. 21, 2010, the Board found that a construction contractor was entitled to an equitable adjustment for higher labor costs, including applicable indirect rates and profit, when the General Services Administration (GSA) modified a contract to retroactively impose a higher Davis-Bacon Act wage determination that should have been incorporated when a construction portion of the contract was awarded. The decision confirms a contractor's entitlement to indirect costs and profit when higher wage determinations are imposed under the authority of a contract's Changes clause, instead of the Davis-Bacon Act's Price Adjustment clause (or similar clause), which otherwise limits adjustment only to a contractor's actual increase in wage and fringe benefits costs but does not permit recovery of indirect costs or profit.

In *Yates*, the GSA awarded the construction portion of a contract following an initial design phase, in August 2005. The firm fixed-price contract included the standard FAR clauses implementing the Davis-Bacon Act, and incorporated a Department of Labor (DOL) wage determination dated August 2004. However, DOL had issued a revised wage determination in July 2005-six weeks prior to the August 2005 option exercise-which GSA was required to include in the option pursuant to FAR 22.404-12(a), but GSA failed to do so. In February 2006, a GSA audit revealed that the higher wage determination should have been included, and the contracting officer subsequently issued a modification incorporating the revised wage determination

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in the contract and instructing the contractor to pay the higher wage rates to employees both prospectively and retroactive to the August 2005 contract award. The contracting officer cited the FAR Changes clause (FAR 52.243-1) and the General Services Acquisition Regulation (GSAR) Equitable Adjustment clause as the basis for the modification.

Shortly thereafter, the contractor submitted a proposal seeking an equitable adjustment due to the higher wage costs and included the contractor's actual increased wage costs, plus an allowance for overhead and profit, for the entire contract performance period. Citing the Davis-Bacon Act's Price Adjustment clause, FAR 52.222-32 (which was not even incorporated into the contract), and FAR 22.404-12, the contracting officer rejected the request for overhead and profit. The contracting officer also refused to compensate the contractor for any adjustment based on the actual number of labor hours the contractor incurred performing the contract, insisting that any adjustment be based instead only on the number of labor hours that were assumed in the contractor's initial bid (adjusted for any formal change orders on the project).

The Board determined that:

- Because the wage revision was incorporated under the auspice of the Changes clause it did not trigger the limitations of the Price Adjustment clause that might prevent recovery of overhead and profit (if, in this case, read into the contract under the *Christian* doctrine);
- The appropriate basis for any adjustment was the wage increase applicable to the actual number of hours that the contractor incurred under the contract, rather than wage increases on only the proposed number of hours; and
- Because the award of the construction phase of the contract was a stand-alone contract award (as opposed to the exercise of an option), any limitations on recovery found in FAR 22.404-12 or the Price Adjustment clause would not apply.

This decision reinforces the guidance initially provided in *Prof'l. Servs. Unified, Inc.*, ASBCA No. 45799, Dec. 14, 1993, 94-1 BCA 26,580 and extends its rationale to the Davis-Bacon Act. In *Professional Services*, the Armed Services Board held that an increased wage determination incorporated after the fact through a modification under the Changes clause entitled the contractor to an adjustment including applicable indirect costs and reasonable profit. In that case, a Service Contract Act (SCA) wage determination revision was retroactively incorporated into a contract, after the contract had been solicited and awarded using an outdated wage determination.

Finally, this decision should be of interest not just to construction contractors, but also to contractors performing under SCA covered contracts because the SCA regulations use similar clauses and contracting officers likely will seek to apply similar principles when faced with Price Adjustment clause or failure to incorporate situations. Given the broad measure of recovery available when contracting officers fail to incorporate wage determinations legally required to be included in construction or services contracts, contractors alike need to be aware of their rights when facing retroactive revisions to an applicable wage determination.