

# Prince, Ramish and Johnson in The Government Contractor: The Most Important Cost And Pricing Cases Of 2025—Part 2

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To read Part 1 [click here](#).

This article, presented in two parts, discusses noteworthy decisions from the past year regarding cost and pricing issues. The second installment reviews cases addressing entitlement to fee under a cost-plus-fixed-fee, level-of-effort contract (*Peraton*) and calculation of allowable lease costs following sale and leaseback of a depreciable asset (*Parsons*), and discusses statutory and regulatory developments affecting cost and pricing, including the National Defense Authorization Act for Fiscal Year 2026.

***Peraton, Inc., ASBCA 62853, 25-1 BCA ¶ 38,856***—The board’s decision in *Peraton* considered and rejected the argument that, at least under the circumstances presented, the contractor was entitled to the full fixed fee under a cost-plus-fixed-fee effort regardless of whether it provided the full level of effort upon which that fixed fee was calculated.

*Peraton* held a cost-plus-fixed-fee, level-of-effort (CPFF-LOE) task order to provide technical systems engineering support services for the Navy, issued under an indefinite-delivery, indefinite-quantity contract. *Peraton* argued that it was entitled to the full fixed fee, notwithstanding that the Government had not required all budgeted hours. The board rejected that argument and, in a decision issued simultaneously in an appeal brought by *Vectrus Systems Corp.* under a successor contract, determined that the cases involved identical legal issues and reached the same conclusion. See *Vectrus Sys. Corp., ASBCA 62685, 25-1 BCA ¶ 38,859*.

The IDIQ contract permitted the agency to award “term” type cost-plus-fixed-fee orders. As the contract defined it, that meant:

The term form [of task order] describes the scope of work in general terms and obligates the contractor to devote a specified level of effort for a stated period of time. Under this form [of task order], if the performance is considered satisfactory by the Government, the fixed fee is payable at the expiration of the agreed-upon period and upon contractor certification that the level of effort specified in the order has been expended in performing the contract work.

The contract also included a special clause, SEA 5252.216-9122, LEVEL OF EFFORT (DEC 2000), which required the contractor to provide a specified total level of effort of total man-hours of direct labor for each order as identified in the task order proposal. If the contractor envisioned exceeding the allocated hours for the task order, then it was required to notify the contracting officer and propose an “acceleration plan,” for continuing work through the remaining contract term. The contract also permitted the Government to accelerate the contract work and require the contractor to consume all available hours before the end date. If the work required fewer hours than budgeted, the contract permitted the CO to either reduce the fee proportionally based on the ratio of hours expended to hours budgeted, or to require the contractor to perform work until the budgeted hours were entirely expended.

The task order solicitation purported to describe a CPFF LOE requirement. The Navy provided estimated direct labor hours for each year, requiring an offeror to propose a total fixed fee that it would then include in an hourly rate, which would include fee per labor hour calculated by dividing the proposed fixed fee by the total estimated labor hours. The hourly rate would be used for billing and payment. However, the solicitation expressly stated that the estimated hours were not a guarantee.

The Navy awarded Peraton the task order in accordance with the methodology for fee and payment addressed in the solicitation, reiterating that the total hours were estimates of the Navy’s needs. Navy personnel testified that the estimates were intended to be a maximum, or a ceiling. The task order’s contract line item structure stated the total fixed fee for each performance period and specified a fee per direct labor hour. Fee was payable at the “per hour rate,” with “any balance of fixed fee” to be paid to the contractor, and any “overpayment of fixed fee” to be repaid by the contractor.

During performance, the Navy’s actual requirements for each performance year were consistently lower than estimated. The Navy ordered hours based on potential job needs for eligible customer groups within the agency, requesting that Peraton provide rough order of magnitude (ROM) pricing and level of effort estimates for the internal customer to review and approve if appropriate. Beginning in 2017, during the final planned year of performance, Peraton began providing ROM estimates using a recalculated hourly profit rate based on Peraton’s estimate of the overall labor hour requirements for the year, rather than the Navy’s initial hour estimates that formed the basis of the task order fee rates.

The Navy first learned of the adjusted fee rate when Peraton’s subcontractor under the task order, Vectrus, requested a meeting to discuss correcting the fee. The Navy then demanded that Peraton resubmit ROMs using only the contractual hourly rates. Ultimately, Peraton complied, and the fee it was paid for each performance period was only approximately two-thirds of the original total fixed fee amount it proposed. Peraton then submitted a certified claim for approximately \$2 million, which the CO denied. The appeal to the board followed.

Peraton argued that the Navy was obligated to renegotiate the fixed fee and that its failure to do so breached the contract. It based its position on a provision in the task order providing that, if “for any reason” the CO adjusts the task order amount of the estimated total hours, then “such adjustments shall be made by task order modification.” Peraton contended that any change to the estimated hours therefore required the CO to modify the contract.

The board rejected Peraton’s interpretation because it viewed the clause at issue as providing only what happens when the hours increase, not decrease. The very next sentence of the clause addressed the adjustment that would be made to fee for additional estimated hours. The clause

was silent regarding downward adjustment. Although Peraton urged that the plain language refers to both upward and downward adjustment, the board applied the long-established rule that contracts are interpreted as a whole. The IDIQ contract included a provision addressing when actual needs are less than estimated and provided for a downward adjustment of the fixed fee. Read together, the contract already provided that when hours required were fewer than estimated, fixed fee would be reduced proportionally.

The board continued by reinforcing that the hour estimates were not guarantees, but only estimates, and that there was no evidence the Navy had duped the contractor into unfairly low prices or that the estimates were otherwise unreasonable, inadequate, or not presented in good faith. The board also reiterated that the “lump sum” fixed fee was clearly presented as an estimate used to calculate the fee rate—not as a guarantee—and that Peraton understood it that way. The board also reiterated that the so-called “negligent estimate rule” does not apply to IDIQs.

The board observed that its conclusions are consistent with the intent of cost-plus contracts, which shift risk of cost fluctuations to the Government and guarantee reimbursement of allowable costs. The board implied that the Government also benefits by avoiding payment of costs if the contractor’s costs are fewer than estimated, which is certainly accurate. However, the board did not address the distinction between cost and fee in this framework. In any event, *Peraton* suggests that “fixed fee” does not necessarily mean a fixed lump sum but instead can mean “fixed” by reference to actual performance metrics—so long as it does not depend on costs actually incurred.

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***Parsons Gov’t Servs., Inc., ASBCA 62269 et al. , 2025 WL 1217311***—This decision involved an issue of first impression: the proper interpretation of Federal Acquisition Regulation 31.205-36 (Rental costs) applied to a sale and leaseback arrangement after the 2005 revision of the cost principle. Through clear hypotheticals and careful discussion of the related provisions at FAR 31.205-16, the board explained why Parsons’ interpretation of the cost principle, while clever, must fail.

Parsons Government Services Inc. (Parsons) appealed six final decisions. Five final decisions disallowed certain lease costs and unilaterally established final indirect rates for fiscal years (FYs) 2014–2018, and one denied Parsons’ claim requesting the CO find lease costs for FYs 2014–2017 were allowable. Parsons had previously pursued similar appeals for FYs 2011–2013, but the board held the FY 2011 claim was time-barred and Parsons withdrew its claims for FY 2012 and FY 2013.

The core dispute concerned how to calculate allowable lease costs of Parsons’ headquarters building following Parsons’ sale and leaseback of the asset. Parsons constructed the building in Pasadena, California between 1973 and 1974 at a cost of approximately \$19 million, and fully depreciated the building between August 1974 and December 1991. Parsons also made improvements over the years costing approximately \$13.5 million. The Government partially reimbursed Parsons for the depreciation and improvements through payments under Parsons’ Government contracts. In 1991, Parsons and the Government executed an advance agreement pursuant to FAR 31.109 and 31.205-11, permitting Parsons to recover \$754,201 per year through 2011 as a use charge for the building.

In May 2011, Parsons sold the building, along with other facilities on its headquarters campus, to a third party for \$319.9 million, of which \$149.3 million were allocated to the price of the building. The improvements were not fully depreciated at the time of the sale. At the time, the building had a net book value, or undepreciated balance, of \$4.2 million. The difference between the net amount

realized from the sale (\$149.3 million) and the undepreciated balance (\$4.2 million) was \$145.1 million.

The sale of the building triggered FAR 31.205-16, which addresses the “gain” or “loss” attributable to the sale of a tangible asset and provides for the gain or loss to be credited or charged to the Government. Under FAR 31.205-16(c), gain or loss is “the difference between the net amount realized ... and its undepreciated balance.” However, to prevent the Government from receiving a windfall, the cost principle limits the gain recognized “for contract costing purposes” to the difference between the acquisition cost and the undepreciated balance and applies that adjustment only to depreciation costs previously recognized. FAR 31.205-16(c), (d).

Applying FAR 31.205-16—i.e., taking the difference between the net amount realized from the sale and the undepreciated balance on the date Parsons became a lessee (\$145.1 million), and then limiting the recognized gain to the difference between the acquisition cost (\$32.6 million) and the undepreciated balance (\$4.2 million)—yielded a recognized gain of approximately \$28.4 million credited to the Government.

Parsons then leased the building back for a 15-year term and, in 2012, the first full year of the leaseback arrangement, incurred approximately \$14.4 million in lease and related costs. Parsons sought to recover a portion of those costs under FAR 31.205-36 (Rental costs):

[r]ental costs under a sale and leaseback arrangement [are allowable] only up to the amount the contractor would be allowed if the contractor retained title, computed based on the net book value of the asset on the date the contractor becomes a lessee of the property adjusted for any gain or loss recognized in accordance with 31.205-16(b).

FAR 31.205-36(b)(2). FAR 31.205-16(b) provides that, in the case of a sale and leaseback, gains and losses are calculated as “the difference between the net amount realized and the undepreciated balance of the asset on the date the contractor becomes a lessee.”

Initially, Parsons included in its incurred cost proposals through FY 2017 only \$2.17 million, representing the net book value of \$4.2 million adjusted by the \$28.4 million gain to \$32.6 million in total, spread out over the 15-year term of the lease. However, Parsons took a new position in discussions and subsequent letters with the Defense Contract Management Agency. Parsons argued that the “gain” recognized in FAR 31.205-16(b) is not limited, for purposes for FAR 31.205-36(b)(2), by FAR 31.205-16(d). In other words, Parsons should be permitted to recover up to the entire net gain realized and undepreciated balance (\$145.1 million) instead of just the difference between the acquisition cost and the undepreciated balance, i.e., the gain credited to the Government (\$28.4 million). Under this interpretation, Parsons argued \$9.67 million of its annual lease costs were allowable, rather than \$2.17 million. Parsons included this larger amount in its FY 2018 incurred cost proposal. The Government determined the amounts were unallowable. Parsons ultimately filed a certified claim asserting it was entitled to a total increase in corporate allocations of adjusted leaseback costs of \$12,912,324 for FY 2014–2017.

Parsons’ fundamental argument was facially simple and based on the plain language of FAR 31.205-36(b)(2), which addresses the allowability of rental costs incurred by a contractor following a sale and leaseback. FAR 31.205-36(b)(2) provides that rental costs are allowable “only up to the amount the contractor would be allowed if the contractor retained title, computed based on the net book value of the asset on the date the contractor becomes a lessee of the property adjusted for any gain or loss recognized **in accordance with 31.205-16(b)**.” (Emphasis added). FAR 31.205-16(b), in turn, provides in relevant part that “The gain or loss is the difference between the net

amount realized and the undepreciated balance of the asset on the date the contractor becomes a lessee.” FAR 31.205-16(b)(2). While “gain” recognized under FAR 31.205-16 is limited “to the difference between the acquisition cost” and “its undepreciated balance” under FAR 31.205-16(d), FAR 31.205-36(b)(2) explicitly and exclusively references FAR 31.205-16(b). In other words, the gain for purposes of FAR 31.205-16(b), and in turn the rental costs under FAR 31.205-36(b)(2), is not limited by FAR 31.205-16(d), the cap on the gain credited to the Government.

The board carefully set out the related cost principles at FAR 31.205-16, FAR 31.205-11, and FAR 31.205-36, explaining that the Government cannot be charged for cost of using contractor-owned property after the Government has paid the contractor for the full depreciation costs unless the parties agree to a use charge. If the contractor sells the depreciating asset, then FAR 31.205-16 applies, which may result in an adjustment to the depreciation costs for which the Government is responsible: either a credit back in the event of a “gain,” capped at the acquisition cost and the undepreciated balance, or a charge to the Government in the event of a “loss.” FAR 31.205-16(a), (c). As the board explained it, the cost principles would thus allow the Government to recover up to, but never more than, the amount of depreciation for which it paid. The parties agree that they followed this methodology to determine the amount of the gain for which the Government would be credited due to the sale.

Parsons’ argument turned on the addition in 2005 to FAR 31.205-36(b)(2) of the following bolded words to the cost principle: “Rental costs under a sale and leaseback arrangement only up to the amount the contractor would be allowed if the contractor retained title, **computed based on the net book value of the asset on the date the contractor becomes a lessee of the property adjusted for any gain or loss recognized in accordance with 31.205-16(b).**” But the board was troubled by its assessment that the added language, interpreted as Parsons suggested, ignores the first part of the provision: that the costs are allowable “only up to the amount the contractor would be allowed if the contractor retained title.”

The board observed that the sale of property for a gain has two effects on the contractor’s cost recovery: “(1) the contractor is no longer able to recoup the remaining undepreciated balance through depreciation charges, and (2) it must credit to the Government some or all of the depreciation payments it had received to date.” Those effects thus had to be reversed to put the contractor in the position it would have been in had it retained title. The board interpreted the added language in FAR 31.205-36(b)(2) as being composed of two components, net book value and the gain/loss adjustment, corresponding to “the two effects caused by the sale.” Including the net book value in allowable rental costs allows the contractor “to recover an amount equal to the remaining depreciation it would have been able to charge but for the sale” The gain/loss adjustment then must “reverse[] the credit or charge to the government dictated by -16(b) upon an asset sale.”

Turning to applying FAR 31.205-36(b)(2) to the specific case, the board determined that the Government’s reading of the regulation, applying the cap on gains imposed by -16(d), was correct for several reasons.

First, the board stated that the Government’s interpretation was the only reasonable reading in context of the overall regulatory scheme. The primary effect of FAR 31.205-36(b)(2) is to “avoid[] either the contractor or the government being better or worse off than if the sale and leaseback had not occurred.” Under Parsons’ interpretation, it would receive a windfall compared to the situation had it retained title.

Second, the board found the Government’s interpretation to be the only one that gave coherent meaning to the full regulations at issue. FAR 31.205-16(b) is not applied in isolation, but rather, is

applied in conjunction with the upper limit on the gain for which the Government could be credited under FAR 31.205-16(d). Under Parsons' interpretation, gain would mean "one thing for purposes of -16 and something else for purposes of -36(b)(2)," creating an inconsistency disfavored under standard canons of regulatory interpretation.

Third, FAR 31.205-36(b)(2) refers to costs "recognized" in accordance with FAR 31.205-16(b). But FAR 31.205-16(b) does not use the word "recognized," it only uses the word "realized." Those "realized" costs are limited to an amount "recognized" using the limits provided by FAR 31.205-16(d). Without applying FAR 31.205-16(d), there is no defined amount "recognized" under FAR 31.205-16(b) or FAR 31.205-36(b)(2).

Parsons argued that the cost principle as interpreted by the Government was unreasonable because Parsons could have retained title to the building and recovered a larger amount from the Government as a negotiated reasonable use charge pursuant to FAR 31.205-11, which it had done from 1992 through 2011. But Parsons would not have been *entitled* to these amounts; it had only the possibility of negotiating amounts subject to the Government's discretion. Parsons' additional argument, that the interpretation was unreasonable because the contractor could just sell a building, move, and lease a more expensive facility and treat the costs as allowable, was true but irrelevant. The board has no authority to overturn a policy decision reflected in unambiguous regulatory text.

Although unnecessary to its holding, the board reinforced its interpretation by reference to the regulatory history. The Civilian Agency Acquisition Council and the Defense Acquisition Regulations Council (the "Councils") explicitly rejected a commenter's suggestion that the regulation should "permit the contractor to recover the lease payments that result from the sale and leaseback arrangement." 69 Fed. Reg. 29,380, 29,381 (May 21, 2004). The Councils asserted that:

[a]llowable lease costs relating to a sale and leaseback arrangement have long been limited in the cost principles to what the contractor would have received had they retained title. The basic tenet that underlies this provision is that a contractor should not benefit for entering into a sale and leaseback arrangement. The Councils believe this basic tenet continues to be appropriate. It is important to note that a sale and leaseback arrangement is a voluntary financing mechanism entered into by the contractor. The Councils do not believe the contractor should be entitled to recover additional monies simply because of a paper transaction that provides no significant benefit to the Government.

The intent was to ensure only that the contractor would retain the "ability to recoup what would otherwise be considered allowable costs up to the original acquisition cost." 70 Fed. Reg. 33,673, 33,674 (June 8, 2005).

Parsons arguably had the better interpretation of the plain language of FAR 31.205-36(b) in a vacuum. But the board was unwilling to accept an interpretation that was unreasonable in the broader context of the relevant cost principles. The board accordingly determined that rental costs under FAR 31.205-36(b)(2) in the case of a sale and leaseback necessarily are limited to net book value adjusted for the recognized gain provided under FAR 31.205-16(d).

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**Statutory and Regulatory Developments**—Federal Government procurement is changing rapidly, including changes to cost and pricing requirements. The FY 2026 NDAA mandates five significant statutory revisions to cost and pricing rules: (1) nontraditional defense contractors will be exempt

from the cost principles, certified cost or pricing data requirements, and DOD business-systems rules on defense contracts; (2) the thresholds for Cost Accounting Standards coverage will increase substantially; (3) the Truthful Cost or Pricing Data Act threshold will increase markedly as well; (4) the methodology for calculating the cost impact of changes in cost accounting practices will be revised; and (5) the CAS Board's composition and rulemaking process will be amended.

**Nontraditional Defense Contractor Exemptions:** Section 1826 directs DOD to exempt nontraditional defense contractors from the FAR pt. 31 cost principles, certified cost or pricing data requirements, and contractor business systems clauses (accounting, earned value management, cost estimating, material management, property management, and purchasing). These exemptions will apply only to defense contracts, not to civilian agency contracts. The head of contracting activity or delegee is authorized to waive the exemptions, or modify or partially apply them, with a written determination. However, the secretary of defense must notify congressional defense committees within 60 days after a waiver is issued, "including with a discussion of efforts made to adapt the acquisition approach for the product or service with respect to which the [ ] waiver was granted so that such waiver would not be necessary."

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These exemptions will apply to the overwhelming majority of companies in the defense industrial base. 10 USCA § 3014 defines *nontraditional defense contractors* as companies that are not currently performing a contract subject to full coverage under the CAS and that have not performed such a contract in the past year. George Mason's Baroni Center for Government Contracting estimated last year that under the current CAS rules, 92.5 percent of the defense industrial base would qualify as nontraditional defense contractors. 2025 Government Contracting Trends and Performance Index at 1, <https://webdocs.gmu.edu/wp-content/uploads/baroni-center-government-contracting-trends-and-performance-index.pdf>. That figure will only increase as changes in CAS applicability (discussed below) reduce the number of CAS covered contracts (and companies performing them).

**(2) CAS Thresholds:** Section 1806 will sharply reduce the number of CAS-covered contracts by implementing three changes to the coverage rules. First, CAS will apply only to contracts and subcontracts valued at \$35 million or more, replacing the current two-step framework under which CAS can apply to certain contracts valued at \$2.5 million if the contractor is currently performing a \$7.5 million "trigger" contract. Second, the threshold for full CAS coverage will double, increasing from \$50 million to \$100 million. Finally, the rules will be amended to allow CAS exemptions to apply to discrete portions of otherwise covered contracts or subcontracts—that is, portions of contracts would be exempt from CAS if involving commercial products or services, items priced by law or regulation, or fixed-price work awarded with adequate price competition without certified cost or pricing data.

These CAS program reforms appear to have originated in the recommendations of the Section 809 Panel, the most recent “Blue Ribbon” procurement reform effort. In 2018, the Panel recommended increasing the CAS threshold to \$25 million and increasing the threshold for full CAS applicability to \$100 million. Section 809 Panel Recommendation 30, [https://discover.dtic.mil/wp-content/uploads/809-Panel-2019/Volume2/Recommendation\\_30.pdf](https://discover.dtic.mil/wp-content/uploads/809-Panel-2019/Volume2/Recommendation_30.pdf). Similarly, the General Services Administration recommended increasing the CAS coverage threshold for individual contracts to \$35 million as part of legislative proposals submitted to Congress last year during the Revolutionary FAR overhaul initiative. GSA estimated that the change would “provid[e] relief from CAS [for] approximately half of currently covered entities, but retain coverage to over 90 percent of the dollars,” and suggested that it “would substantially reduce a large disincentive for certain contractors to want to work with the government.” <https://www.gsa.gov/policy-regulations/policy/acquisition-policy/legislative-proposals>

**(3) Truthful Cost or Pricing Data Threshold:** Section 1804 increases the threshold for certified cost or pricing data from \$2.5 million (up from \$2 million following an inflation adjustment in late 2025) to \$10 million. This change, which applies to both defense and civilian contracts, together with the new exemption for nontraditional defense contractors on DOD contracts, will substantially reduce the circumstances in which certified cost or pricing data are required.

**(4) CAS Board Changes:** Section 1806 mandates several changes to the composition and operation of the CAS Board. Effective Jan. 1, 2028, Defense Contract Audit Agency personnel (any “individual who is a member of an audit entity of an executive agency”) will be ineligible to serve on the Board. The CAS Board will continue to be chaired by the Office of Federal Procurement Policy (OFPP) Administrator. The statute amends the description of the four other members to provide that they will consist of a representative of DOD and a representative of GSA, each with substantial experience administering CAS-covered contracts; one senior employee or retired senior employee of a Government contractor with comparable private-sector experience; and one private-sector representative of the accounting profession with substantial experience. The statute also permits the Board to appoint up to two nonvoting members “from academia, a nonprofit organization, or a private entity with substantial experience establishing financial accounting and reporting standards in compliance with Generally Accepted Accounting Principles.” This provision appears intended to support the ongoing CAS-GAAP conformance effort. In addition, the statute relocates the CAS Board from OFPP to the Office of Management and Budget and increases the number of senior staff supporting the Board from two to not fewer than four, in addition to the executive secretary. Finally, Section 1806 removes the requirement for the Board to publish an advanced notice of proposed rulemaking in the Federal Register as part of the process of prescribing cost accounting standards and interpretations.

These CAS Board reforms also track recommendations of the Section 809 Panel. The Panel urged that the CAS Board be removed from OFPP, which it characterized as having proven “ineffective at providing oversight for application of CAS to federal government contracts.” It further recommended that “Government auditors and investigators should not be eligible to serve as members of CASB, both to avoid conflicts of interest and because they typically lack the administrative and management experience needed.” The Panel called for increased staff support for the Board as well. Section 809 Panel Recommendation 29, [https://discover.dtic.mil/wp-content/uploads/809-Panel-2019/Volume2/Recommendation\\_29.pdf](https://discover.dtic.mil/wp-content/uploads/809-Panel-2019/Volume2/Recommendation_29.pdf).

**(5) Cost Accounting Practice Change Price Adjustment Methodology:** Section 1806 prescribes revisions to the methodology for calculating contract price adjustments for cost accounting practice changes. This section states that, for changes in cost accounting practices: “(A) costs recovered by the Federal Government shall exclude any contract or subcontract (or any portion of such contract or subcontract) that is firm fixed-price, or that is not price-redeterminable based on costs,” and “(B) for a fiscal year, for any contract or subcontract (or any portion of such contract or subcontract) that is not a firm, fixed-price contract or subcontract the costs recovered by the Federal Government shall not exceed the net increased costs, if any, paid to the contractor or subcontractor for all changes in cost accounting practices implemented within the same fiscal year.”

For years, The Boeing Co. has been litigating claims challenging the FAR 30.606(a)(3)(ii) restrictions on offsetting the cost impacts of unilateral cost accounting practice changes with savings achieved through other changes implemented at the same time as contrary to the CAS statute. See *Boeing Co. v. U.S.*, 119 F.4th 17 (Fed. Cir. 2024); [66 GC ¶ 288](#). Section 1806 may at last resolve this longstanding dispute, at least for new contracts.

**Conclusion**—The 2026 NDAA cost and pricing changes are the most significant we have seen in many years. The exemptions for nontraditional defense contractors from the cost principles and TINA and the increases in the CAS and certified cost or pricing data thresholds will relieve many Government contractors of Government-unique cost and pricing requirements. Going forward, these requirements will primarily apply to large prime contractors, at least on defense contracts. In effect, the new framework will create a two-tiered system: traditional defense contractors will remain subject to cost and pricing obligations, while most others will be exempt, or largely so. That will reduce the compliance burden and risk for nontraditional defense contractors and reduce barriers to entry to the defense market. It may also create an incentive for traditional defense contractors to find ways to route some of their business through nontraditional defense contractor entities.

There are two important caveats to the nontraditional defense contractor exemption from the contract cost principles: (1) the statutory allowability provisions of 10 USCA §§ 3741–3765 will continue to apply independent of FAR pt. 31; and (2) nontraditional contractors will remain subject to the cost principles on civilian agency contracts.

As far as statutory allowability rules, 10 USCA § 3744 (“Specific costs not allowable”) lists 17 enumerated types of costs that are not allowable on covered contracts—defined as contracts exceeding \$500,000 other than fixed-price contracts without cost incentives or contracts for commercial products or services—including entertainment costs, lobbying costs, and costs of alcoholic beverages. Thus, DOD will not be picking up the tab for nontraditional defense contractors’ wine or beer anytime soon. 10 USCA § 3745 (“Required regulations”) then provides that the FAR “shall contain provisions on the allowability of contractor costs” and must “define in detail and in specific terms those costs which are unallowable, in whole or in part, under covered contracts” and, “at a minimum, clarify the cost principles applicable to contractor” for 17 types of costs. Several other statutory provisions likewise prescribe allowability rules or limitations for particular costs, including 10 USCA § 3761 (Restructuring costs), 10 USCA § 3762 (Independent research and development costs: allowable costs), and 10 USCA § 3763 (bid and proposal costs: allowable costs). The DAR Council will need to implement regulations addressing these restrictions, balanced against the requirements of Section 1826.

That nontraditional defense contractors remain subject to the cost principles on civilian agency contracts may create confusion, leaving some contracts governed by FAR pt. 31 and others by pared-back statutory allowability rules. This dichotomy exists in part because the Revolutionary

FAR Overhaul (RFO) initiative made few changes to FAR pt. 31, notwithstanding Executive Order 14275, Restoring Common Sense to Federal Procurement (Apr. 15, 2025), which directed that “the FAR should contain only provisions required by statute or essential to sound procurement, and any FAR provisions that do not advance these objectives should be removed.” The FAR pt. 31 practitioner album explained that “[m]ost definitions and procedures [were] retained to maintain uniformity across the Government.” Now that Congress has mandated that nontraditional defense contractors performing defense contracts be exempt from the cost principles, in Phase 2 of the RFO, the FAR Council should amend FAR pt. 31 to adopt more minimalist, statutory cost principles across the board.

In what might have been the headline development in another year, on Sept. 11, 2025, the CAS Board issued a notice of proposed rulemaking (NPRM) addressing the conformance of CAS 404, 408, 409, and 411 to GAAP, along with a final rule conforming CAS 403 to GAAP for operating revenue and lease accounting. 90 Fed. Reg. 43,994 (Sept. 11, 2025); 90 Fed. Reg. 43,942 (Sept. 11, 2025). In announcing the NPRM, the administration stated that it “intends to significantly accelerate work on additional conformance of CAS to GAAP” as part of its “ongoing efforts to drastically reduce regulatory burdens” and “will streamline the complex maze of rules that govern nearly \$750 billion in annual contract spending by government agencies.”

<https://www.whitehouse.gov/briefings-statements/2025/09/white-house-omb-board-proposes-elimination-of-dozens-of-unnecessary-and-redundant-accounting-requirements-on-federal-contractors/>. The FAR and DAR Councils should likewise keep these objectives in mind as they shape the future of the cost principles.

***This Feature Comment was written for THE GOVERNMENT CONTRACTOR by Richard C. Johnson, Zachary D. Prince, and Daniel H. Ramish. Mr. Prince and Mr. Ramish are Partners and Mr. Johnson is Senior Counsel in the Government Contracts practice at Haynes & Boone, LLP in Tysons, Virginia.***

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