# Understanding Economic Price Adjustment in Department of Defense Contracts

When I first started working with Department of Defense contracts, I remember sitting through a briefing where a senior contracting officer described how a supplier had to absorb a 15 percent cost increase on a five-year fixed-price agreement. The room went quiet. Everyone knew that kind of loss could put a small business under. That was my first real lesson in why the economic price adjustment clause exists. It is not a loophole or a giveaway. It is a practical tool that keeps long-term contracts viable when the economy moves in ways no one can predict.

## Why Economic Price Adjustment Matters in DoD Contracts

DoD contracts often span several years. A lot can change in that time. The price of steel jumps because of trade policy. Fuel costs spike due to geopolitical instability. Labor rates rise when the civilian sector competes for the same skilled workers. Without a mechanism to account for those shifts, contractors face a choice: eat the loss or cut corners. Neither outcome serves the government's interest. The economic price adjustment clause provides a structured way to adjust the contract price based on verifiable changes in specific cost indexes. It keeps the contract fair and the supply chain stable.

I have seen this play out in real time. One contractor I advised was supplying specialized electronics for a communications system. The contract was written in 2020, but by 2022 the cost of semiconductor components had doubled. The original price was no longer sustainable. Because the contract included an economic price adjustment provision tied to the Producer Price Index for electronic components, the contractor could request an adjustment without renegotiating the entire agreement. That saved months of administrative work and kept the production line running.

## How Economic Price Adjustment Works

The core idea is straightforward. Instead of locking in a single price for the life of the contract, you tie part or all of the price to an independent index. The Defense Contract Management Agency and individual contracting officers specify which index to use, how often adjustments can occur, and whether they apply to the whole contract or only to certain cost elements. Common indexes include the Employment Cost Index for labor, the Producer Price Index for materials, and the Consumer Price Index for general inflation.

There are two main types of economic price adjustment clauses used in DoD contracts. The first is the standard clause found in the Federal Acquisition Regulation, often referred to as the

FAR 52.216-4. This clause allows for upward or downward adjustments based on a single index. The second type is a tailored clause, which the contracting officer and the contractor negotiate to fit a specific situation. Tailored clauses might use a combination of indexes or set a cap on how much the price can change in a given year.

Both types require careful documentation. The contractor must show that the cost increase is real, that it matches the index movement, and that it applies to the specific items or services covered by the contract. A sloppy submission will get rejected, and a rejected adjustment can mean the difference between profit and loss on a multiyear program.

## Common Pitfalls and How to Avoid Them

One mistake I see often is contractors waiting too long to request an adjustment. The clause usually sets a specific window, like 30 or 60 days after the cost change occurs. If you miss that window, you forfeit the adjustment for that period. Another issue is using the wrong index. I worked with a company that tried to use the Consumer Price Index to justify a labor cost increase. The contracting officer pointed out that their contract specified the Employment Cost Index, which was much lower that quarter. The contractor had to eat the difference.

Documentation is another weak spot. You need more than a spreadsheet. You need invoices, supplier quotes, and a clear narrative that connects the index movement to your actual costs. The government auditor will want to see that the price increase is not due to inefficiency or poor management. If you cannot show that your costs went up because of market forces, not because you switched to a more expensive supplier for convenience, the adjustment will not hold.

Finally, do not assume that an economic price adjustment clause protects you from all risks. It does not. If your contract does not include one, or if the clause is written narrowly, you may have no recourse when costs spike. That is why I always advise contractors to negotiate for these clauses early, during the proposal phase, when the government is still deciding on terms. Once the contract is signed, it is much harder to add protection.

## SpendLogic and Compliance Solutions

Managing economic price adjustments across multiple contracts can become a data-heavy task. You have to track dozens of indexes, monitor submission deadlines, and keep a clean audit trail. That is where compliance software like SpendLogic comes into play. It helps contractors automate the monitoring of price adjustment triggers, generate the required documentation, and maintain a clear record for government auditors. But no tool replaces the need for a solid understanding of the rules. SpendLogic works best when you already know what you are looking for.

## Practical Steps for Contractors

If you are new to working with economic price adjustment clauses, here are a few things to keep in mind:

- Read your contract clause carefully. Know which index is used, how often adjustments are allowed, and what documentation is required.
- Set up a tracking system for the relevant indexes. Many are published monthly by the Bureau of Labor Statistics. If you wait until you need the data, you will be scrambling.
- Build a cost baseline early. When the contract starts, document your actual costs for labor, materials, and overhead. That baseline becomes the reference point for any future adjustment.
- Submit adjustment requests promptly. Note the deadline and work backward from it. Late submissions are almost always rejected.
- Keep an audit-ready file. Include the index data, your cost breakdown, and a clear explanation of the cause and effect. If the government ever questions the adjustment, you want to be able to hand over a complete package.

These steps sound simple, but I have seen many contractors skip them and then wonder why their adjustment request was denied. The government does not grant economic price adjustments as a favor. It grants them because the contract says it will, and only if the contractor follows the rules.

## The Bigger Picture

Economic price adjustment is not just about protecting profit margins. It is about maintaining a healthy defense industrial base. When contractors know that their long-term contracts have a safety valve for cost increases, they are more willing to bid on multiyear programs. They invest in capacity, hire skilled workers, and build the supply chains that the military relies on. Without that stability, the risk premium becomes too high, and fewer companies compete for DoD work. That ultimately hurts readiness.

I have seen the difference a well-written clause can make. On one program, the contractor had a robust economic price adjustment mechanism that covered both labor and materials. When inflation hit in 2021 and 2022, they were able to adjust prices smoothly, and the program stayed on schedule. On another program, the clause was so narrow that it only covered raw material costs. The contractor had to absorb a 12 percent increase in labor costs because the contract did not account for wage inflation. That contractor is now reluctant to bid on similar work.

If you are involved in DoD contracting, take the time to understand how economic price adjustment works in your specific contracts. It can be the difference between a program that runs smoothly and one that becomes a financial drain. And if you are negotiating a new contract, push for a clause that reflects the real cost drivers in your business. The government wants you to succeed, but it will not read your mind. You have to ask for what you need.