

Regulatory Reforms Call for Reduced Reliance on Cost-Type Contracts

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Since the President issued his March 4, 2009 Memorandum on Government Contracting, which identified time-and-material (T&M) and cost-reimbursement contracts as "high-risk" contract vehicles, various reform initiatives have been proposed, including encouraging more use of fixed-price contracts and limiting use of T&M and cost-reimbursement contracts. Recently, the Federal Acquisition Regulation (FAR) Councils and the Department of Defense (DoD) have proposed additional FAR and Defense Acquisition Regulations System (DFARS) changes to implement these reforms.

On March 2, 2011, DoD issued a proposed rule to encourage increased use of fixed-price (firm-target) incentive contracts. 76 Fed. Reg. 11410 (March 2, 2011). This proposed rule follows on the recommendations made by the DoD Undersecretary for Acquisition, Technology and Logistics (USD (AT&L)), in memoranda issued September 10, 2010, and November 3, 2010, regarding "better buying practices." See Fall 2010 issue of *GCIU* "Gates and Carter Fire Shot Across the Bow of DoD Acquisition System; Issue a 23-point Acquisition Reform Memorandum." Under the proposed rule, contracting officers are instructed to "give particular consideration to the use of fixed-price incentive (firm-target) contracts, especially for acquisitions involving development to production" and to pay "particular attention" to share lines and ceiling prices. Consistent with USD (AT&L) recommendations, the "default arrangement" for these fixed-price incentive contracts is a 50-50 share line between the Government and contractor, with a 120 percent price ceiling.

Following on the heels of DoD's proposed rule, on March 16, 2011, the FAR Councils issued an interim rule providing guidance on the use and management of cost-reimbursement contracts. See 76 Fed. Reg.

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14543 (March 16, 2011). The interim rule amends the FAR as follows:

- FAR 16.103 now includes specific documentation requirements when a contract other than a fixed-price contract is selected. In particular, the contract file must include an explanation for why the contract type selected must be used to meet the agency's needs and the additional risks and burdens to the Government associated with the selected contract type. In addressing risks and burdens to the Government, the agency should discuss how it identified the risks, the nature of the additional risks, and how the agency will manage and mitigate the risks and the resources necessary to plan for, award and administer the contract type selected. At a minimum, the contract file should include an analysis of why the use of something other than a firm-fixed price contract was selected, a discussion of the facts and circumstances and reasoning that support the contract type selection, an assessment of the Government resources necessary to plan for, award and administer the contract type selected, a discussion of actions to minimize the use of cost-type contracts on future acquisitions for the same requirement and to transition to firm fixed-price contracts, and a discussion of why a level-of-effort, price redetermination, or fee provision was included. FAR Part 7 is also amended to reflect the additional documentation and acquisition planning requirements for cost-type contracts.
- Recognizing that "assigning adequate and proper resources to support the solicitation, award and administration" of cost-type contracts can be "challenging" and expressing "great concern that a lack of involvement in contract oversight by program offices is primarily present in other than firm-fixed-price contracts," the FAR Councils amended FAR 7.104 and 16.301-3 to require designation of at least one contracting officer representative or contracting officer technical representative prior to award of a cost-type contract. FAR 1.602-2, 1.604 and 7.104 are also amended to implement this requirement.
- If the entire contract cannot be firm fixed-priced, acquisition planners and contracting officers are instructed under FAR 7.105(b)(5)(iv) and 16.104(e) to consider whether certain requirements or CLINs can be awarded on a fixed-price basis.
- FAR 16.301-2, which describes when cost-type contracts are suitable, is expanded to instruct against selection of a cost-reimbursement contract unless (1) the agency cannot define its requirements sufficiently to allow for a fixed-price type contract and (2) uncertainties in contract performance do not permit costs to be estimated with sufficient accuracy to use a fixed-price contract. Similarly, FAR 16.301-3 is amended to permit a cost-reimbursement contract only when the requirements of amended FAR 16.104 have been met; a written acquisition plan has been prepared and approved at least one level above the contracting officer, the contractor's accounting system is adequate for determining costs applicable to the contract; and the Government has adequate resources to award and administer the contract.
- Regarding the adequacy of contractor accounting systems, the Councils amended FAR 42.302 to require a determination of the adequacy of the contractor's accounting system and provide that the accounting system should be adequate during the entire period of contract performance.

These recent FAR amendments and proposed DFARS rules substantially increase the hurdles for agencies to award cost-type contracts and further incentivize agencies to pursue fixed-price contract vehicles. A predictable result will be a further increase in fixed-price contracting-whether appropriate for the task at hand or risky, based on performance uncertainties-as a result of agency reluctance to jump through the documentation and administrative "hoops" necessary to award a cost-type contract. In addition, contractors operating under cost-type contracts can expect that agencies will be looking for ways to move future performance to fixed-price CLINs or vehicles and will be closely monitoring throughout contract performance DCAA findings in regards to the adequacy of accounting systems.