

ALERT

DOD Plans to Adjust Offerors' Prices to Account for Independent Research & Development Efforts

November 7, 2016

WHAT: The Department of Defense followed up on its previous February 2016 Advance Notice of Proposed Rulemaking with a Proposed Rule that would require DOD Contracting Officers to adjust offerors' proposed prices and estimated costs when their proposals rely on the fruits of their Independent Research & Development (IR&D) efforts. The proposed adjustment would be based on the "amount that such future IR&D investments reduce the price of the proposal."

WHEN: DOD issued the Proposed Rule on Friday, November 4, 2016, with Comments due by January 3, 2017. The Proposed Rule does not include a timeframe for implementing the proposed requirement.

WHAT DOES IT MEAN FOR INDUSTRY: Contractors should evaluate how, under the Proposed Rule, their current IR&D efforts and plans could impact their competitiveness in acquisitions requiring this price/cost adjustment. Under the Proposed Rule, contractors developing proposals for covered acquisitions could face significant upward adjustments to their proposed prices or estimated costs if the Government believes they gained a price advantage by using the fruits of their IR&D efforts.

- **Scope:** The Proposed Rule would apply to two types of DOD acquisitions: (1) Major Defense Acquisition Programs (10 U.S.C. § 2430) and (2) Major Information Systems Acquisitions (10 U.S.C. § 2445a). The Proposed Rule provides for adjustment to "the total evaluated **cost or price** of the proposal," signaling that this rule will apply to proposal evaluations for both cost-reimbursement and fixed-price contracts.

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- **DOD's Stated Purpose:** Contractors currently allocate IR&D costs as indirect costs, potentially across the entire business, which can provide contractors a competitive advantage when they rely on the fruits of their IR&D efforts. DOD expressed concern about the fairness of using IR&D to obtain a price advantage in a competition, noting that "[t]his is not the intended purpose of making IR[&]D an allowable cost."
- **Proposed Solicitation Provision:** The Proposed Rule provides a solicitation provision that includes two key requirements. *First*, it requires each offeror to "include documentation in its price proposal to support [its] proposed approach" if the offeror "intends to use IR&D to meet the contract requirements." *Second*, it requires the Contracting Officer to "adjust the Offeror's total evaluated cost or price to include the amount that such future IR&D investments reduce the price of the proposal."