

Multi-Association Consolidated Response to
Questions for Contractors That Sell Commercial Goods
or Services to the Government

1. Does your organization have sales in the commercial market?

Yes

2. Do you know of any commercial practices that can and should be utilized in Government contracts under FAR Part 12 that are not currently being used?

Yes

a. What are the practices?

Some FAR Part 12 contracts do not go far enough to be performance – based.

b. How would the use of such practices improve contracting?

Should reduce overall cost and, in particular, cost of contract administration by the Government.

3. Do you segment your Government and commercial markets when selling commercial goods or services? If so, why?

Yes, we have different business units that sell to the different markets, due to the customers' different buying approaches, and of course the Government's requirements for TINA, CAS, and other items that impose additional burdens not **encountered in the commercial market.**

4. Do you use different pricing methodologies for your Government and commercial markets? If so, why?

Our commercial products are not necessarily priced differently when sold to a government or commercial buyer. However, generally speaking, commercial products are priced based on market demand, whereas items sold to the Government, and priced according to the Government pricing process will more often be cost-based. Commercial pricing also involves many more variables – financing, long-term commitments, providing life cycle support, warranties and guarantees, liabilities, etc.

5. Is there any price-related information that you provide to your commercial customers that you generally do not provide to the Government?

No. We advise all customers of the opportunities for volume discounts, but the Government purchasing office, which places orders only for a specific procurement request by a user, is generally incapable of taking advantage of such discounts.

6. When an item qualifies as a “commercial item” under FAR Part 12 but the Government is the primary buyer, there generally is no efficient “market” establishing prices. How should “commercial” prices be established in this case?

We would disagree with the premise that the presence of a single dominant buyer (the Government) destroys the ability or efficiency of a market to set prices. In any event, most items that qualify as a commercial item under FAR Part 12 are likely sold or offered for sale in the marketplace – so there is a market-established price. Price history may be available. Also, there are likely analogous or similar products or services that could be studied in a market analysis. It appears that most Government buyers are very inexperienced and weak when it comes to doing market analyses – no matter if an item is FAR Part 12 or not – and much too dependent on gaining access to detailed cost history to demonstrate price reasonableness. Several studies by the Defense Science Board and others have noted that the Government should move to price based acquisition. However, the Government culture resists this and Congress also has made it even harder to use FAR Part 12 or to get TINA waivers for non-FAR Part 12 contracts.

7. What price-related information, other than certified cost or pricing data, could be provided to the Government when there is no efficient market establishing prices?

RESPONSE #1 - Depending on the situation, some companies would be willing to help the customer do reasonable market research – including in some cases confidentially providing sales information to customers (provided this is protected against disclosure under FOIA). In addition, companies may be willing to share information on certain cost drivers. Also, it is not all that terribly hard for the Government to determine prevailing wages and cost of labor in any given industry or locale. Where there is competition, even if it’s just two bidders, that also helps set the price. An interesting research project for DAU would be to have two teams each determine the price of a list of items – one team using only cost data; and one team using only price analysis; and then comparing how close each one came to the actual price paid in a procurement.

RESPONSE #2 - There are several issues imbedded in this question. The definition of “information other than cost or pricing data” at FAR 2.101 basically means any data that is not required to be certified under TINA. As a practical matter, this involves two types of data: price data and cost data. Each is discussed below.

Price data. This type of data is used for price analysis purposes to determine the fairness and reasonableness of offered pricing. It is most commonly associated with contracts for commercial items where price is to be based on the prices paid for same or similar services in the commercial marketplace. The rationale is that fairness and reasonableness can be judged on the prices that others were willing to pay, provided that the commercial marketplace consisted of buyers and sellers free

to bargain. This type of data has traditionally also included prices paid for same or similar services in the Government marketplace (e.g., price based on adequate price competition).

Cost data. Two circumstances typically create the need for cost data meeting the definition of “information other than cost or pricing data.” One circumstance is where cost data is required to perform a cost realism analysis on a competitive procurement. An example would be providing labor information for the purpose of assessing understanding of work requirement or ability for attracting experienced workers. The other circumstance would be to determine the fairness and reasonableness of offered pricing where price data was insufficient. An example would be the cost of modifying a commercial item.

As a general rule, for commercial item acquisition, commercial companies are only willing to provide price data. This is because commercial companies do not develop cost data at the contract or item level. Instead, commercial companies generally develop cost data at the product center or profit center level, and the cost data usually do not include general and administrative (G&A) expense allocations. Often the cost data is based on engineering estimates or standard costing methods with costs variances be allocated at an aggregate level. In a sense, this is one reason why Cost Accounting Standards (CAS) was created - that is, the bridge the gap between financial accounting and contract accounting.

While it might be possible to compile cost data based on estimates, studies, and analyses, such cost data would not meet TINA’s standards of being complete, accurate, and current. Also, the cost data would not have had the FAR Part 31 contract cost principles applied. A major concern for private industry is that contracting officers and Government auditors might misinterpret the cost data for being more than it really was. Another major concern is that contracting officers and Government auditors might misconstrue cost and profit relationships of specific products.

8. In your commercial contracts, to what extent and under what circumstances or limitations are time and materials type contracts used (as opposed to fixed price)?

Time and materials type contracts are used frequently for certain types of services where it is not possible to estimate price in advance due to the unusual nature of the task (e.g., testing services; repairs). It is easier for both parties to share the risk of the cost, rather than one or the other to bear most of the risk. As noted above, it should be fairly easy for the Government to ascertain if the labor hour wages are correct in almost any circumstance.

9. In your commercial contracts, under what circumstances are “gain sharing” (or “share-in-savings”) arrangements used?

a. What terms are provided for those contracts?

We have one FAR Part 12 contract, which includes a Shared Savings provision. It provides for sharing up to 50% of the savings over a 6-year period. Proposals are to be submitted and approved by the Government. There has been no activity under this provision due to the uncertainty of annual buys.

b. What limitations are imposed by the buyer for those contracts?

In the case above, the Government must approve the proposal, and can audit the results and negotiate the savings and share.

10. As a seller of commercial items or services:

a. What contract terms and conditions do you use? Are these “standard” for all of your customers, including the Government?

In most instances we have a model contract that includes terms and conditions commonly used in the marketplace appropriate for the goods and services. Yes, these are standard for all customers, including the Government (recognizing that some tailoring is required under laws applicable to Government contracts). In some cases, we execute agreements with major customers on these T&C's in advance, which facilitates subsequent individual orders (similar to the Basic Ordering Agreement or BOA in the FAR). The Uniform Commercial Code underlies some of the T&C's as well as other applicable laws and statutes applying to the products or services.

b. Do you use the same terms and conditions for your Government customers as you do for your commercial customers? If not, how do they differ?

Under FAR Part 12, we attempt to use the same T&Cs as we would if the Government were a commercial customer. However, there may be some tailoring – e.g., in some cases it is more reasonable for the Government to self-insure, self-finance, etc. Termination for convenience is not typically provided in commercial contracts, which is usually handled as a “breach.” However, in extreme circumstances, a seller can negotiate a termination for convenience for appropriate consideration.

c. Do you ever renegotiate your “standard” terms and conditions with your commercial customers? If so, under what circumstances? What factors might cause you to renegotiate contract terms?

Commercial buyers and sellers become accustomed to the prevailing T&C's and tend to operate within that marketplace paradigm. The General Terms Agreements referenced above (like a BOA), once negotiated with a buyer, provide the standard terms and conditions for all subsequent orders. A commercial company is normally reluctant to accommodate

many changes in those General Terms Agreements (standard terms) – because any nonstandardization increases costs and complexity and process disruptions; and it can set an unfavorable precedent. Price, deliveries, and other factors tend to be the focus of negotiations.

d. Who has authority to negotiate and change terms and conditions?

The Seller's Contracts organization is usually the authorized party although they may delegate this within approved boundaries. Contracts delegation flows down from Board of Directors through executive management line.

e. Are there any terms or conditions that you will not renegotiate for commercial customers? - What are they?

This is a pretty broad question – and would vary considerably by product and service, market and other factors. Warranties and indemnities are usually nonnegotiable – because they are areas that, if changed, would change the Seller's level of liability and risk. A good example of this in the Government purchasing arena is the inability to obtain P.L. 85-804 coverage, which would indemnify the contractor for work involving extremely hazardous risks, and the SAFETY Act, which provides a limitation of liability for a contractor supplying anti-terrorist technology to the Government.

f. As a seller, which contract terms do you frequently renegotiate (e.g., payment terms, volume discounts, acceptance, warranties, license rights, limitation of liability, limitation of remedies, indemnification, most favored customer, disputes, etc.)?

Payment terms and volume discounts are frequently negotiated – the others are not frequently renegotiated, if at all.

11. Have you encountered circumstances where commercial buyers refuse to change their terms? How do you handle that situation?

The commercial seller typically proposes the T&C's, not the buyer.

a. Walk away? Yes

b. Price the risk? Yes

12. What intellectual property terms are usually included in your commercial contracts?

Manuals and technical information are licensed to the Buyer so that the buyer can maintain and operate the item. Technical information is generally not licensed to permit a buyer to contract with third parties for support or repairs. If that were

desired, we would rather license to the third party directly and usually train them and approve their process (or have them obtain some independent approval). Then they could contract with the original buyer(s).

13. Do you compete head-to-head for private sector contracts? Yes

a. What information regarding the buyer's requirements is available to you?

In many cases, we design a product or fashion a service to a perceived market need – identifying a market segment composed of many potential buyers who have a common set of needs. In some cases, we will invite a variety of potential buyers to join our team during the process of defining a new product offering. We also take into account specific requirements from a buyer. These could be options or modifications to the basic product or service.

14. Does the Government disclose sufficient information concerning its requirements for maximum competition in its solicitations?

Generally less, although there are a lot of layers and people between the ultimate user (e.g., the war fighter) and the supplier. All the many layers of bureaucracy that define requirements, buying practices, and then individual procurements put their own slant on the requirements. Since this takes a lot of time and changes frequently – sometimes due to political influences – it is a very difficult process to track for a potential seller.

15. What steps could the Government undertake to improve its requirement definition process?

Shorten the process and keep the ultimate customer/user closely engaged throughout.

16. Are you aware of any specific practices in federal acquisition that prevent fair and equal treatment of offerors in federal acquisitions?

In general, no. However, doing business with the government presents its own barriers – a hurdle of time and investment and adoption of non-commercial business practices as well as risks – that some companies address by creating a separate Government division.

17. Viewing from a commercial standpoint, are you aware of examples where the Government is purchasing goods or services in excess of what is actually needed to fulfill the agency's mission? No

18. Does your organization or any segment thereof, decline to compete in the federal acquisition process?

a. If so, what are the reasons for not participating?

Generally speaking, our commercial segments do not sell directly to the Government. The military products segment sells the commercial products and services to the DoD instead, after incorporating the Government's requirements for special equipment and combined with continuing contractor logistics support.

b. Is the failure to participate in federal acquisitions related to any particular products or services?

No – it is a function of Government buying practices – e.g., CAS, TINA, etc.

19. Do any of your commercial customers obtain cost data? Under what circumstances?

Almost never – they just want the product or service.

20. Do any of your commercial customers obtain audit rights? Under what circumstances? Never.

21. Do commercial firms itemize and define labor categories for the purpose of soliciting proposals and/or responding to solicitations? If so, what benefits does such practice provide to the buyer and seller?

Since their contracts are generally firm, fixed price and costs are not divulged, commercial manufacturing firms do not prepare proposals with breakdowns of labor categories. Many consulting, accounting and IT firms segregate labor categories – i.e., manager, professional, manual labor, etc.

22. What is the commercial practice related to creating, issuing, and releasing service labor categories and rates when competing for service contracts?

Prices for labor categories are based on market and skills as well as underlying wages, fringe benefits and overhead.

23. What is the commercial practice related to service labor hour pricing strategies from a corporate vs. regional field office level? If field offices are permitted to deviate from corporate pricing strategies, how does that work with the corporate level rates or Most Favored Customer rates?

24. How do commercial firms handle direct contract support cost and what types of cost control measures are in place?

25. How is subcontract pricing handled in the commercial market and what happens if subcontractors negotiate price reduction with prime?

Since the Buyer of the end item is paying a firm fixed price for a commercial product from the Seller, the Buyer has no stake in the relations between the prime and its suppliers (and therefore no visibility). It is only in a cost reimbursement environment that suppliers' prices would be relevant to the ultimate customer.

26. How do commercial firms package and price requirements (i.e., by total solution, performance-based or by specific tasks)? What is the current trend?

Increasingly we are offering a total solution, with performance-based features. This could include product purchase as well as an offer for life-time support.

27. To the extent commercial practice increasingly uses total solutions to meet operational needs, what are the key considerations and/or features used to ensure a commercial contract actually provides an effective "total solution?"

The test is the marketplace acceptance of the offering. One way to enter and enlarge the market is to offer just the product and then varying degrees of total life cycle support, letting the customer choose.

28. How do commercial firms approach outsourcing overseas and prime's use of overseas subcontractors? How about security concerns pertaining to Government contracts?

We are in a global marketplace. Even small business may sell globally on the internet. We prudently use overseas suppliers both to achieve competitive cost benefits and to obtain market access. U.S. Government security concerns with using overseas suppliers are addressed via the appropriate regulations that govern all U.S. companies (Commerce's EAR, or State's ITAR). Notwithstanding the foregoing, no responsible American firm is going to place their country at risk knowingly by exporting critical technology. Furthermore, companies have their own concerns about protecting their intellectual property rights that result in certain protective measures for any overseas relationships.