

April 17, 2017

809 Panel  
c/o Lawrence Trowel  
Square Corners Consulting, LLC

Dear Mr. Trowel,

Per the request from the 809 Panel, the Integrated Dual-use Commercial Companies (IDCC) compiled the following list of experiences and the impact that these experiences have on its members collaborating and contracting with the DoD, National Laboratories, or other Federal Agencies, including DOE, NIST and NSF. While the examples shared below are from individual companies, they tend to be representative of the overall experiences of IDCC member companies.

We have also included recommendations that would make it easier and less risky for commercial (non-defense establishment) companies to contract and sell to the Federal Government. Most importantly, many of the IDCC companies feel there is too much risk sharing their leading edge technology with the government, because the government regulations and agency policies work to expose and appropriate their intellectual assets, much of which was developed without government funding. Their leading edge technologies along with the capabilities of these companies enable their competitive advantage, which they utilize to sustain their enterprise, employ a US and global workforce, and provide sustainable returns to their investors. The government regulations and policies (especially those of the DoD), focus on obtaining government use rights of R&D, even for that which was funded solely by that company.

**IDCC:**

Integrated Dual-use Commercial Companies (IDCC) was founded in 1991 as a consortium of US global private and Fortune 1000 technology rich commercial firms that are leaders in their industries. The members sell commercial items (directly or indirectly) to the Government and perform a limited (when compared to their total R&D investment) amount of government R&D. Many of the technologies under development in their laboratories have substantial potential benefit for government applications. To help make available to our government the best leading

edge technologies, IDCC has worked extensively on issues that affect the availability of commercial technologies to the government, particularly protection of Intellectual Property, focus on pricing versus costs for commercial sales, and confidentiality of technical data. In addition, a new strategic focus for this group is sustainability and how the member companies may work with the other industrial and government partners to further their sustainability and that of their customers.

The IDCC Member firms include:

- Air Products and Chemicals, Inc.
- Covestro LLC (formerly Bayer Material Science)
- Corning Incorporation
- The Dow Chemical Company
- Lutron Electronics, Inc.
- The Sherwin Williams Company
- W. L. Gore & Associates, Inc.

Based on EOY 2015 data, the aggregate sales of the IDCC Members was greater than \$118 Billion, IDCC Members invested more than \$3.3 Billion in IR&D and employ about 145,000 people globally. Collectively on average, they file about 1,400 patent family applications annually.

## **ISSUES/CONCERNS:**

1. Unintended Consequences of 2011 NDAA for Noncritical Procurement:  
The changes required in the 2011 NDAA compel DoD to obtain additional data and capability to sustain major weapon systems and subsystems over their life cycle, including "Limited Internal & Emergency Repair & Overhaul Data Rights". This bled into policies and regulations for noncritical systems/subsystems and is impacting DoD's approach to COTS and commercial items "of a type". Leadership in the Office of Under Secretary of Defense for Acquisition, Technology, and Logistics (OUSD(AT&L) have worked to limit Commercial Item Acquisition, including increased efforts to view cost data and eliminate the "of a type" category of commercial items.
2. Overhead/Compliance Burdens:  
IDCC companies have experienced a rigidity in the various arms of the government when discussing any flexibility that the contracting officer may have in issuing a more favorable type of contract for a commercial company. Despite being empowered to negotiate Other Transaction (OT) type contracts, Contracting Officers have little or no training for this contract vehicle and work hard to avoid using OT's. Only in a few cases has a Contracting Officer or his representative entertained the use of an Other

Transaction Authority (OTA), and frequently, even if an OT contract is proposed, it appears very similar to a FAR contract but with the reference numbers removed.

As subcontractors or subs of subs, there is little incentive to take on all the complexity, years of audits, and requirements mandated in traditional FAR contracts. CAS, FAR, Uniform Guidance, DFARS etc., are making it next to impossible to engage in contracting activity for companies where government work is an extremely small part of their business. Several of the IDCC companies do not perform government contracting for money. They do it to build relationships, test theories, get feedback, push technology forward by proving a concept, and sometimes, it is just basic precompetitive research. Most of what they do is 50% to 100% cost share, or cost reimbursement with a very high cost share attached to it.

On top of the regulations already in place, we are also finding that agencies are adopting their own “policies”. Case in point, ARPA-E’s refusal to reimburse IR&D in indirect costs. When asked to see their policy, they state they do not publish their policies and the practice is at the discretion of their Contracting Officer. In addition, ARPA-E locks the proposer into their cost structure, then negotiates and adds the burden of Tech-to-Market milestones, which need to be absorbed at 100% cost share. Part of their practice is to require the awardee to spend 5 to 10% of the award on furthering ARPA-E's mission. This occurs on top of cost share, which they will not negotiate.

### 3. Factors Limiting Federal Government Access to Commercial Innovation:

Many large companies use accounting systems that are not compatible with CAS, or even modified CAS. This requires a separate accounting system to be set up for handling government contracts. The situation is even more difficult for large, private, multinational companies. These companies are not required to follow the SEC reporting standards for public companies nor do they need to follow the requirements in the Sarbanes-Oxley Act. To undertake cost-type government contracts, it would require private firms to establish significant accounting and audit systems to adequately administer standard FAR contract vehicles, essentially excluding their participation.

After doing a cost-benefit analysis of their federal government contracting over the past 10 years, an IDCC member decided it is not advantageous to pursue public funds to subsidize R&D, because the result is a very small percentage of the total cost to bring an innovation to market. In addition, the extra cost associated with government compliance, audits, and records management substantially reduces the benefit. Then the specific risks to intellectual property (foreground and background), in most cases, becomes a deal breaker for the company's critical leading-edge technology.

Agreements (contracts) that are for the direct benefit of the government will typically be subject to FAR (and DFAR or DEARS) and the government's Cost Accounting Standards (CAS) which is covered in FAR Part 30. Programs that are not for the direct benefit of the government such as Cooperative Agreements and Other Transactions are not typically subject to the full range of FAR and only the specific FAR and CAS which are included or referenced in the agreement documents apply to these types of programs. The Office of Management and Budget (OMB) has issued several circulars that may apply and are usually incorporated by reference.

Both FAR and CAS are written based on Generally Accepted Accounting Principles (GAAP) of a job cost accounting system. Many commercial companies, which do not have a significant amount of federal contracting, do not use a job cost accounting system. To meet the Government requirements for job cost accounting (modified CAS), the company needs to augment its general accounting system to provide project cost data in the required format and exclude unallowables that are included in commercial company accounting.

Many development programs in the government are targeted to early stage, pre-competitive R&D. From an industry perspective, these programs have a high risk of failure and at best a long term payback. The added costs associated with government contract management and accounting result in increased initial investment exposure. As programs move forward, added risks on the return side occur due to the assertiveness of government agencies regarding background and foreground intellectual property access and rights. The net effect for many large organizations is that, even though a given program might align with strategy, the return on investment of government programs becomes unacceptably low.

Consequently for several IDCC companies, new opportunities are considered on a case-by-case basis, preferring collaborations where no money changes hands and via agreements where there is little or no ambiguity regarding IP rights upfront. In the cases where reimbursement is available, other IDCC companies often make trade-offs as to the type and size of contracts they will accept. These companies keep the size of contracts below the threshold where full CAS is required. Activity is often restricted to R&D cost shared agreements that are not typically subject to the full range of FAR. These agreements are still subject to audit and often the audit cost for small agreements far exceeds the value of the agreement. Thus agreements that are too small or too large are avoided. To reduce audit risk, overhead rates are submitted and approved for only those sections of the company that are typically involved in the agreements. If resources are required in areas of the company for which no overhead rates exist, then these resources

are charged on a direct cost only basis. Thus the company will receive less reimbursement than is allowed.

4. Cost of Doing Government Collaboration:

What are the costs: It is hard to state typical costs since there are a wide variety of company situations, types of solicitations and contracts from a variety of agencies. Based on the collective experience of IDCC companies, the following factors are escalating the federal government costs that have no commercial corresponding practice or expense item:

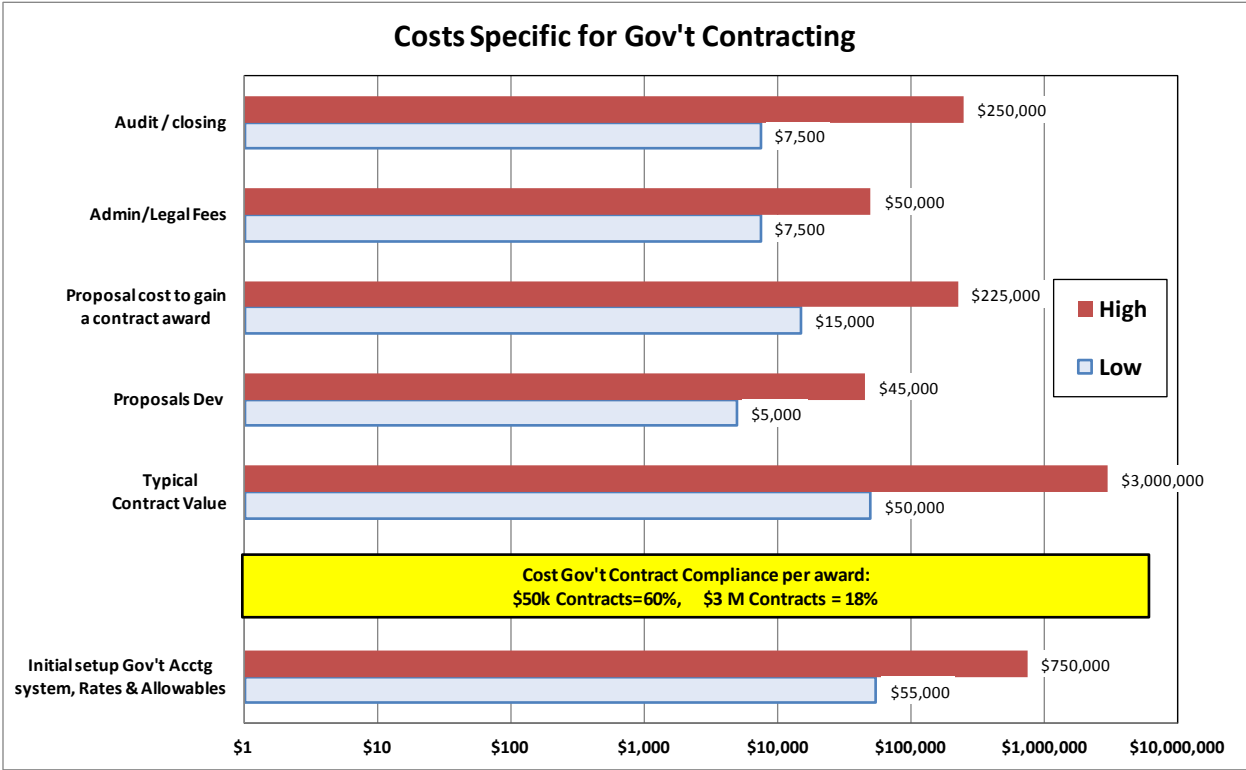
- To adequately manage a government cost plus or fixed cost contracts, a separate set of accounting “government books” needs to be established and maintained to exclude unallowable costs and provide the additional tracking of direct cost (i.e., labor hours) that is required for FAR Contracts. If contracts exceed higher limits, then full FAR cost accounting standards must be followed, which are not acceptable to most commercial only businesses, as this requires parallel accounting systems be established and maintained.
- In order to meet government cost accounting standards, one major cost contributor is extracting unallowable costs from commercial accounting. These costs are not simply excluded because often the unallowables are part of a collection of costs captured in most commercial books. Thus, the less expensive way to extract unallowable costs is to remove large categories further increasing the costs that are excluded (i.e., to exclude alcohol, then all meals and entertainment might be dropped from the project budget as there is no way to separate these overhead accounts for most current expense account systems.) However, modifying an expense account system to independently call out these unallowables for a global company could cost millions and result in additional expense preparation costs across the company for the commercial business.
- Bid/proposal costs are highly influenced by the number of partners and complexity of the IP arrangement and the respective risks. Bid/proposal success rates ranged from about 20% to 30%. So to get a contract award, 3 to 5 proposals need to be submitted. This raises the cost to submit a winning contract by 3x to 5x.
- Government contracts do not follow the Uniform Commercial Code, thus legal and contractual expertise must be obtained and developed for government contracting.
- Mostly, IDCC company contracts are less than \$10 million and often are several million dollars. Some IDCC companies have occasionally tackled substantially larger contracts.
- Often cost share is about 50%, though some have ranged from 0% to 100%. Audit costs do not scale with contract size, becoming a very significant cost of small

contracts, sometimes much larger for both the company and the government auditors than the face value of the contract. These audits have very high cost-to-benefit ratios, do not seem to justify the effort by the government, and are a waste of tax payer's and industry dollars. It goes well beyond common sense because the people making these decisions do not need to weigh the cost of the investigation to its outcome.

Based on substantial commercialization experience of the IDCC companies, we find:

- Project success rate (useful IP and product generated): ~ 40%
- Cost to scale an innovation to market: 20X the project (contract) cost. (This is a good approximation but can be highly variable between projects and contracts)
- Adoption rate of new technology in the market: ~ 8% of projects go to the commercialization phase.
- Typical incubation time for TR7 to market: 7 years.

The following are the incremental costs required by current government contracting requirements over and above what is required by the US Uniform Commercial Code:



5. Impact of Audit Backlogs at DCAA:

The years of backlog at DCAA is a real issue, especially when coupled with industry mergers, divestitures, changes in business systems, and employee turnover. This issue can be very important at companies that are not traditional government contractors.

6. Patent Waivers and Term Lengths for Company Data confidentiality:

Class Patent Waivers used by DOE provide clarity about intellectual assets derived from cooperative agreements at the beginning of the contract. This practice significantly reduces the upfront fear of contracting with the government and the risks for commercial entities when entering into cooperative agreements, and reduces unnecessary work and costs related to obtaining a patent waiver thereafter. If IP waivers are applied on a case by case basis (not through Class Waivers), the costs for a company to process the waiver application, filing, and maintenance can reach \$150k and many months to resolve.

Further extending the time period that a government agency must keep proprietary information confidential could lead contractors to offer or include higher-valued technology for government sponsored research and development.

7. Buy America versus Trade Agreements Act:

The vast majority of products used in building construction projects are Commercial Items/COTS. Per existing FAR clauses--for construction projects, once a contract exceeds ~\$8 million, the entire project migrates from Buy America Act (BAA) to Trade Agreements Act (TAA). "Bundling" of multiple projects (renovations, repairs, facility management contracts, etc.) is becoming commonplace. Such "bundled" contracts can be geographically dispersed or include broad, unrelated scopes of work all in the interest of minimizing the quantity of contracts being managed by the ordering agency. As such, this "Bundling" will tend to take what could be multiple BAA projects and when "Bundled" become one large TAA contract.

As a result, the decision for companies in determining where to expand or locate manufacturing capacity is quite complex. Absent a consistent need for US manufactured products, other factors for where to locate manufacturing facilities will often take precedence. To the extent the administration wishes to support a US manufacturing base, recognize that current contracting processes (to include significant expansions in the use of IDIQ contracts which exceed the BAA threshold) is discouraging a US manufacturing base.

8. Refusal to Utilize Available Commercial Friendly Contract Vehicles

Limited use of Other Transaction Authority (OTA), except for DARPA is problematic for companies that do little government contracting. Agency leadership and the Contracting

Officers appear not to be interested in advancing DoD's access to advanced technology. They are very focused on protecting the government pouring in all FAR clauses, which is the least risky position for them personally, but which limits the extent that leading edge technology could benefit their agency's mission. Even after challenging the Contracting Officer for months to provide an OTA, many times they provide a OTA that is nothing more than a standard FAR contract with the clause references removed, negating the concept of an OT Contract.

The following are experiences of some IDCC companies in requesting Other Transaction Authority Contracts:

- a. Early in the negotiations with one DoD Contracts Specialist, we requested an OTA. After consulting with her Contracting Officer, the Specialist offered the use of an OTA for Prototypes, which is a vehicle that requires at least one third of the total cost of the project to be paid by the company, e.g., in kind contribution. This was non-negotiable (and not interesting to our company); furthermore, the contracting office rejected the idea that they had the authority to start from a blank page to create an OTA. We ended up with a cost reimbursement type contract.
- b. In a DoD contract discussion when we asked about an OTA, we were told that it was their office's policy to offer Cost Reimbursement type contracts and that the only other option was Firm Fixed Price, if the award was less than \$100,000, which it was not. We have not yet been successful in securing anything other than a FAR-type contract.
- c. For our company to be willing to work on leading edge technology projects within the DoD procurement system environment, we very clearly define the Statement of Work (what we will and will not deliver in our technical reports, project updates, samples, etc.). Such language has been accepted by DoD contracting officers (and program managers) and has been incorporated in our contracts successfully. This approach has established expectations between our company and contracting/program offices and has afforded IP protection that, we believe, maintains our competitive advantage.

## **RECOMMENDATIONS:**

1. Contracting Officer Training and Responsiveness:
  - a. Set up true Centers of Contract Excellence - share best practices within and across departments.
  - b. Contracting and Technical Representatives should communicate more effectively, so the Contracting Officer is aware of how the project is actually progressing and the basis for what changes may need to be made.



- c. Standards need to be in place that layout expectations for Contracting Officers to respond to contract inquiries and challenges in a reasonable timeframe. As reinforcement for this, establish ombudsmen to channel vendor inquiries after efforts to resolve contract issues with the Contracting Officer has failed.
- d. More in depth training for OTs, GSA Schedules, and Commercial Item Acquisition is needed as well as modifications of the procurement culture limiting the use of these contract approaches which substantially reduce costs of procurement if used correctly.
- e. Focus on instituting a top-down culture change from adversarial relationships with contractors to one of mutual trust. Improving understanding within agencies and with contracting officers of commercial business and how it works would be a significant improvement. This training should also focus on learning the role of profit and IP rights in business and how these bolster innovation and allow companies to reinvest in the future, strengthening the defense industrial base as well as the US Economy. These should not be seen as evil, but rather how the free market system works efficiently.

2. Other Transaction Authority:

Use of Other Transaction Authority to obtain leading edge technology, spurred the Congressional review of Boeing's and Science Applications International Corp.'s Future Combat Systems OTs when management of the initially DARPA program was transferred to industry management by the US Army in the form of two Other Transaction Agreements.

- a. DARPA uses OTAs to attract nontraditional DoD contractors to work on leading edge defense problems and opportunities.
- b. Apparently, all the contracts need to agree in the contract hierarchy. If the integrator/prime contract is a FAR contract then all subcontracts need to be FAR contracts. Based on news articles in the spring 2005, the Army's rationale was to give Boeing an OTA so they could continue to provide OT contracts to nontraditional defense subcontractors and to steer the work more fluidly than a standard FAR contract would allow.
- c. The Problem: The Senate's Armed Services Committee mounted an investigation into the use of these OT contract. Senator McCain was outspoken about concerns of defense companies like Boeing if they did not have all the controls in place from a standard FAR contract.
- d. A Possible Solution: it seems that it would be prudent to provide provisions for the prime contractor to be able to let a OT contract to nontraditional defense subcontractors under the Prime's FAR Contract. This continues to be an issue today, as Congress and the Department of Defense continue to worry they are not

able to access leading edge technology that USA adversaries can incorporate in their military systems.

3. Make Contracting Officers' Contact Information Visible to the Public:

Not all people in DoD should hide behind the blanket order of not having email and telephone numbers on DoD and Armed Services websites. Further, having someone to speak with via phone about various issues, and who is knowledgeable of the practical and legal requirements of government contracting, would lead to better working relationships between the government and the contractors. Perhaps an ombudsman or ombudsman-like group or individual tasked with working through issues with contractors, answering contractor's questions, and/or escalating issues to the appropriate offices in a quick and efficient manner would lead to less time, less effort, and more efficient negotiations between the government and the contractors. Ultimately, these actions should lower the costs required for both the government and the industry contractors.

4. Flexibility of SOW on R&D Contracts:

R&D Contracts need to be flexible around the Statement of Work (SOW), especially for leading edge research. Requiring a contractor to finish a contract on a dead-end path, is a waste of tax payer's money and should be subject to early termination. However, terminating a contract that deviates from the original dead-end path to a new path that will achieve the desired outcome is not to anyone's benefit.

5. Flow-Down Clauses:

For FAR contracts, it is important to decide which FAR clauses are applicable and only flow those down to contractors and subcontractors. Doing so will reduce the amount of work needed to review and get to a final contract (see Appendix A).

For Commercial Item Purchases, it is doubly important to limit any flow-down clauses not applicable to FAR Part 12. Additional training in GSA Schedules and Commercial Item Procurement is definitely needed across most agencies.

6. Create Master Contracts:

Establishing Master Contracts with a company could provide Certifications, applicable FARs, and Regulation flow-downs for 4-5 years and then the agency can issue Technical, and Cost solicitations, proposals, SOW's, and contract appendices for these Master Contracts.

7. General Service Administration Sales:

GSA needs to include FAR Clauses Consistent with Commercial Items Procurement. The GSA Schedules program supports billions of dollars in commercial item/COTS products

and services offerings for DOD and other ordering agencies. Implementing a GSA Schedules contract is an extensive undertaking for industry - one of the touted benefits is the ability to navigate with consistent FAR clauses for all purchases under the awarded Schedules contract. The reality is that the majority of ordering agencies don't know how to properly use the Schedules program. Contracting Officers routinely issue extensive additional FAR clauses for orders initiated under a Schedules contract. Page after page of FAR clauses incorporated by reference are regularly appended to Schedules orders for COTS items. As a result, an IDCC member company exited the Schedules program as the overhead to maintain a Schedules Contract greatly exceeded the costs associated with similar commercial customers.

To support the fifth recommendation (above) about flow-down clauses, we have attached an Appendix that was provided to OUSD (AT&L) DPAP/CPIC on November 29, 2011 as part of our response to the request for comments on the Commercial Item Handbook - Draft Version #2, published in the Federal register on September 29, 2011, Vol. 76, No. 189, Page 60474. This appendix is our list of Lessons Learned about commercial item contracting and flow down clauses with our recommendations for guidance in each situation.

Respectfully submitted on behalf of the IDCC,



Alan D Ayers  
President

Appendix A

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## Appendix A

### Lessons Learned From Prime-Sub Transactions – IDCC Recommended for Commercial Item Handbook

Since the publication of the first Commercial Item Handbook in 2001, buyers (both government and upper-tier contractors) have made hundreds of thousands of commercial item determinations. While most have been conducted in accordance with the requirements of FASA and the FAR, many have fallen short. Most of these are probably the result of a failure to fully understand the commercial item definition. However, sellers report many instances of improper practices, such as buyers withholding a commercial item decision to extract cost data from the seller, mixing together a price reasonableness determination and a commercial item determination, and retaining clauses that only apply to non-commercial items.

The following examples are drawn from the experiences of subcontractors in dealing with prime or other higher-tier contractors. However, they are equally applicable to commercial item determinations made by the government. Accordingly, the term “buyer” could be the government or a higher-tier contractor. For consistency, we will use the terms “buyer” and “seller” wherever applicable throughout this appendix.

Example 1: The prime contractor for a military aircraft tells its suppliers that their products cannot be commercial items, because they are being used on a military aircraft.

Guidance: While this one seems to be such a clear misapplication of the commercial item definition that no one should make that mistake, it has happened in the field. Therefore it is important to emphasize that any product at any level of the supply chain can be a commercial item, regardless of the characterization of the product at the contract level above it.

Example 2: A seller asserts that its product is a commercial item. The buyer objects, stating that he has been buying the product for years, and the seller has not claimed it was commercial before; why should it now be commercial.

Guidance: The reasons why the seller would now claim that its product is commercial are irrelevant. The only issue is whether the product meets the commercial item definition. The buyer should evaluate the item and the seller’s justification in accordance with the commercial item definition, and determine whether the product is commercial. If it is, then FASA, the FAR, and DFARS spell out how the product is to be treated by the buyer.

Example 3: A seller asserts that an item meets the commercial item definition. The buyer refuses to agree that the item is commercial until the seller provides more “visibility” into its costs.

Guidance: This often happens on large programs, where prime contractors have become accustomed to obtaining cost data from sellers. As a result, some prime contractor buyers have

found it difficult to give up their reliance on cost data. They then condition their commercial item determination on whether the seller agrees to continue to provide cost data, even if it is not certified cost or pricing data.

This is a reversal of the way the process should work. In passing FASA, Congress determined that if an item is commercial, certain consequences follow as a result. Among those are exemptions from CAS and TINA, exemptions from other procurement laws that apply to non-commercial items, and a much-reduced set of mandatory FAR and DFARS clauses, both in a prime contract and in subcontracts. Therefore a prime contractor should first determine whether an item is commercial. If it is, the remainder of the buying process should follow commercial item procedures, as set forth by law and in the FAR and DFARS. Prime contractors should not use their buying power to force cost data from sellers when the item is commercial.

Example 4: A prime contractor requires sellers to fill out a “Commercial Item Justification” form. The form includes the criteria from the FAR commercial item definition. However, it also requires the seller to provide information on its previous sales and prices for the item.

Guidance: There are two issues involved in this situation: the commercial item determination, and a price reasonableness determination. A prime contractor is responsible for making both. While there is some overlap between the information that might be required for each, they are separate and independent determinations and should not be merged. In particular, the commercial item determination should not depend on an evaluation of the price.

A commercial item determination is based on the physical characteristics and function of the item itself. Note that in the definition of a commercial item, there is no mention of the price (except as part of the definition of commercial services). Accordingly, the decision on whether an item is commercial should be based on evaluation of the item itself, its physical characteristics, its function, and any modifications that were to it to meet the government’s requirements. Note also that the sample commercial item checklist at Appendix to this Handbook does not request price information.

A price reasonableness determination is, as the name suggests, based on the price at which the item itself is being offered, as compared to the prices of similar items on the commercial marketplace. A prime contractor is certainly entitled to request this information as part of its price reasonableness determination, and a seller should expect to provide it. However, this should be a separate step from the determination that the item itself is commercial.

There is nothing inherently improper with including a request for price information on a form for a commercial item justification. However, this practice may lead a buyer to merge the two steps, or make or make the commercial item determination contingent on receiving price information. It also allows the buyer to shift the responsibility for market research from itself to the seller. It may even lead a buyer to conclude that an item should not be treated as commercial (and receive

the full benefits and exemptions of being a commercial item) if the price seems unreasonable. This leads buyers to improperly use the commercial item determination as leverage in price negotiations.

Example 5: A buyer requires a seller to certify that its item is commercial, or requires a seller to indemnify it if the government disagrees with its commercial item determination.

Guidance: The DFARS makes a prime contractor responsible for determining whether a subcontract item is commercial (see DFARS 244.402). Prime contractors are understandably concerned over their liability if a contracting officer disagrees with its decision. As a result, they often add clauses to their subcontracts that require subcontractors to certify that their items are commercial, or require the subcontractor to indemnify the prime for any damages or losses incurred if the government disagrees with a commercial item determination.

The issue here is whether the prime contractor's concerns are justified, and what liability it actually faces if a contracting officer disagrees with its commercial item determination. The only regulatory guidance comes from DFARS 244.402, which states, after noting that a prime contractor is responsible for making a commercial item determination, that "This requirement does not affect the contracting officer's responsibilities or determinations made under FAR 15.403-1(c)(3)." FAR 15.403-1(c)(3) states in part:

If the contracting officer determines that an item claimed to be commercial is, in fact, not commercial and that no other exception or waiver applies, (*e.g.* the acquisition is not based on adequate price competition; the acquisition is not based on prices set by law or regulation; and the acquisition exceeds the threshold for the submission of certified cost or pricing data at 15.403-4(a)(1)) the contracting officer shall require submission of certified cost or pricing data.

Accordingly, it appears that the only consequence to a prime contractor if a contracting officer disagrees with its commercial item determination, would be a requirement to obtain certified cost or pricing data from the subcontractor. Prime contractors should consider this in creating an appropriate clause in their subcontracts.

Example 6: A buyer does not conduct market research for itself. Rather, it makes the seller provide information on its own sales and comparable sales from other sellers.

Guidance: Market research is primarily the responsibility of the buyer. While it is certainly reasonable to ask a seller to provide information on its own sales of the item and comparable products, the buyer should not place the entire burden on the seller. For example, when buying a consumer item for personal use, the individual would not require the seller to provide a list of prices from other sellers for comparison.

Chapter 4 of this Handbook provides a guide to conducting the research for pricing commercial items, and is an excellent resource for prime contractor buyers. Appendices G and H also have resources that can be used in the price-reasonableness analysis.

Example 7: The buyer obtains a commercial item justification from a seller. Instead of making a commercial item determination, the buyer says that its decision must get approved by the contracting officer.

Guidance: The buyer is responsible for making a commercial item determination, whether that buyer is the government or a prime or higher-tier contractor. As noted in the response to Example 5 above, the DFARS, at 244.402(a), specifically states that “Contractors shall determine whether a particular subcontract item meets the definition of a commercial item.” In this case, it is likely that the buyer is concerned about making a wrong decision, and is unwilling to make a decision without knowing the contracting officer would agree. However, as long as the buyer exercises reasonable business judgment in making his decision, there should be no reason to seek the approval of the contracting officer.

Example 8: A seller submits a commercial item justification for a product that is modified from its standard commercial product. The buyer demands to see evidence that the seller has sold the same item sold commercially.

Guidance: This is another example of a misapplication of the commercial item process. There are two responses to this.

First, there is no requirement that the seller have sold the same item commercially. The item could have been sold by any seller on the marketplace. The key is that the item itself must meet the commercial item definition, regardless of who sells it. Even if the item is a COTS item, there is no requirement that a seller must have sold that item itself previously.

Second, the item need not ever have been sold commercially, as long as it is “of a type” or modified from a commercial item in accordance with the definition. The modifications made for the government customer, whether unique to the government or the same as made for any commercial customer, may well make the item unique. Nevertheless, as long as the modifications fall with the parameters of the commercial item definition, the item is acceptable.

Example: A buyer agrees that a seller’s product is a commercial item. However, the buyer’s standard subcontract form has clauses in it that are far in excess of the mandatory clauses for commercial items. The buyer claims that all of the clauses are necessary to allow it to fulfill its contractual obligations in its contract with the customer.

Guidance: The issue of the flowdown of clauses from a higher-tier contract to a lower is complicated. Every buyer has its own subcontract forms that it uses for its purchases, and it is safe to assume that no two buyers flow down the same FAR and DFARS clauses. Nevertheless,



it is possible to state some general principles. First, there are certain minimum clauses that must be included in all subcontracts for commercial items. These are set forth in FAR 52.212-5(e) and 52.244-6(c), and in DFARS 52.212-7001(c) and 52.244-7000. The buyer must include these clauses in the appropriate subcontract.

Second, there are certain other clauses that are generally considered to be “necessary” clauses in subcontracts, even though the FAR and DFARS do not make them mandatory. Included in this category are the Stop Work clause, the DPAS clause, any clause dealing with manufacturing or content requirements, such as a Buy American Act clause or a Trade Agreements Act clause, and data rights clauses. The buyer should include any clauses that are considered “necessary.”

Finally, there are all other clauses that show up in a prime contract. The buyer should only include those clauses that state obligations that the seller must perform to enable the buyer to fulfill its obligations in its contract. The FAR states that “the contractor may include in its subcontracts for commercial items a minimal number of additional clauses necessary to satisfy its contractual obligations.” (FAR 52.212-5(e)(2)). A similar statement is at 52.244-6(c)(2). Note that there are two concepts in that statement. First, that the number of additional clauses must be “minimal”, and second, that they must be necessary to satisfy the buyer’s contractual obligations.

With respect to whether a clause is necessary, buyers should ask what obligation they would not be able to meet without the seller performing the obligation in the clause. When viewed from that perspective, there are few clauses that would be necessary.

In summary, a common complaint from sellers is that buyers flow down too many clauses in their subcontracts. This then becomes an unnecessary point of contention in negotiations. Buyers may do this out of an excess of caution, or because they have not fully transitioned their purchasing practices to a commercial item process. Whatever the reason, the intent of Congress is not fully realized when buyers simply flow down what is in their contracts without regard to the simplified provisions that are allowed for commercial items.