Types of Contracts

A quick walk through FAR Part 16
Contract Types

Contract types vary according to --

(1) The degree and timing of the responsibility assumed by the contractor for the costs of performance; and

(2) The amount and nature of the profit incentive offered to the contractor for achieving or exceeding specified standards or goals.
Factors in Selecting Contract Types

• Type and complexity of the requirement
• Urgency of the requirement
• Adequacy of the contractor's accounting system
• Acquisition history
• Contractor’s technical capability and financial responsibility
• Extent and nature of proposed subcontracting
• Competition
Two Broad Categories of Contract Types

**Fixed-Price Category**

- Firm price or,
- Adjustable price constrained by a ceiling price and/or guided by a target price adjusted only by operation of contract clause

**Cost-Reimbursement Category**

- Payment of allowable incurred costs
- Contain a total cost estimate for the purpose of obligating funds and
- a ceiling that the contractor may not exceed

*These two categories describe the financial contractual relationship*
Fixed-Price Contracts

• Firm-Fixed-Price
• Fixed-Price Contracts with Economic Price Adjustment
• Fixed-Price Incentive Contracts
Firm-Fixed-Price

No adjustment to price on the basis of the contractor’s cost experience in performing the contract

Fixed Price – Cost to Perform = Profit

Contractor absorbs 100% of cost variance through change in profit or loss
Fixed-Price with Economic Price Adjustment

Adjustment to price on the basis of the contractor’s cost experience in pre-specified labor or material

Fixed Price – Cost to Perform = Profit

Contractor absorbs 100% of non-EPA cost variance through change in profit or loss
Fixed-Price Incentive

Price is adjusted using a predetermined formula based on the contractor's cost experience in performing the contract.

\[ \text{Price} - \text{Cost to Perform} = \text{Profit} \]

Contractor absorbs less than 100% of cost variance through change in profit or loss. Price has a ceiling.
Fixed-Price Incentive
Essential Elements

Contract Schedule - CLINS
– Target Cost
– Target Profit

FAR Clause 52.216-16
– Ceiling Price
– Over Target Contractor Share
– Under Target Contractor Share
Cost-Reimbursement Contracts

- Cost
- Cost-Sharing
- Cost-Plus-Fixed-Fee
- Cost-Plus-Incentive-Fee
- Cost-Plus-Award-Fee
Cost & Cost-Sharing Contracts

• **Cost**
  - No fee
  - Contractor reimbursed for all of its allowable costs

• **Cost-Sharing**
  - No Fee
  - Contractor reimbursed only for an agreed-upon portion of its allowable costs
Cost-Plus-Fixed-Fee

No adjustment to price on the basis of the contractor’s cost experience in performing the contract

Cost to USG = Cost to Perform + Fee

Contractor absorbs 0% of cost variance with no change in fee and no chance of loss
Cost-Plus-Incentive-Fee

Cost-reimbursement contract with an initially negotiated fee adjusted later by a formula based on the relationship of total allowable costs to total target costs.

Cost to USG = Cost to Perform + Fee

Contractor absorbs less than 100% of cost variance through change in fee. Fee has a guaranteed min and max.
Cost-Plus-Incentive-Fee
Essential Elements

Contract Schedule - CLINS
– Target Cost
– Target Fee

FAR Clause 52.216-10
– Min Fee
– Max Fee
– Over Target Contractor Share
– Under Target Contractor Share
A cost-reimbursement contract with a fee consisting of:

• A base amount (which may be zero) fixed at inception of the contract

• An award amount, based upon a judgmental evaluation by the Government, sufficient to provide motivation for excellence determined after performance
Definite vs. Indefinite Contracts

Definite Contracts
Defined delivery schedule & quantity

Indefinite Contracts

Definite-Quantity - deliveries or performance to be scheduled at designated locations upon order

Requirements - all actual during a specified contract period (from one contractor) by placing orders with the contractor

Indefinite-Quantity - stated min/max limits of supplies or services during a fixed period; multiple award preference

These categories describe the delivery contractual relationship Can be any contract type.
**Time & Material, Labor-Hours, Firm-Fixed-Price Level of Effort**

**T&M** - Supplies or services acquired on the basis of:

- Direct labor hours at specified fixed hourly rates that include wages, overhead, general and administrative expenses, and profit; and

- Actual cost for materials

  - *Used only when it is not possible to estimate accurately the extent or duration of the work*

**Labor Hours** – T&M without materials

**Firm-Fixed-Price LOE** - A specified level of effort, over a stated period of time, on work that can be stated only in general terms for a fixed dollar amount
Selecting Contract Type

Risk Analysis

Low Risk – “Easy to estimate” type requirements

• Contractors can be expected to accept Fixed Price with little “risk premium”

• Subsequent Production, Commercial items, etc.

High Risk – “Hard to estimate” type requirements

• Contractors will price in “risk premium” for acceptable chance of breaking even on FFP; cost reimbursement contract will have higher chance of costing the Government less

• R&D, Engineering Development, etc.
Selecting Contract Type

Requirement (a) – easy to estimate
80% chance of at least breaking even
$5M above the mean/ most likely cost

Requirement (c) – hard to estimate
80% chance of at least breaking even
$20M above the mean/ most likely cost
## Selecting Contract Type

<table>
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<th>Cost Reimbursement</th>
<th>Fixed Price</th>
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<td>Extra-contractual incentives</td>
<td>100% cost incentive</td>
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<tr>
<td>Best Efforts</td>
<td>Deliver or default</td>
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<tr>
<td>“Estimated” Cost &amp; fee fixed</td>
<td>Only fixed price stated in contract</td>
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<tr>
<td>Paid per AC&amp;P (52.216-7) &amp; fee schedule (comp. vs. term)</td>
<td>Price paid at delivery per CLIN, SLIN, ELIN in schedule</td>
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<tr>
<td>Allowable cost audit to close</td>
<td>Financing (PP &amp; PBP) for large $, long delivery; PP requires approved accounting system</td>
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<tr>
<td>Approved accounting system</td>
<td>Production, full funding required</td>
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<tr>
<td>No financing needed with AC&amp;P clause paying 100% cost every two weeks</td>
<td>Latent defects, other warranties</td>
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<td>RDT&amp;E, incremental funding</td>
<td>Contractor Acquired Property (CAP) – Contractor owns.</td>
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<td>No warranties, its yours</td>
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RDT&E, incremental funding

No warranties, its yours

Contractor Acquired Property (CAP) – Government owns.

Work may be less well defined
Types of Contracts

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