



# 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



**Profit  
or Fee**

**Cost of Performance**

# 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

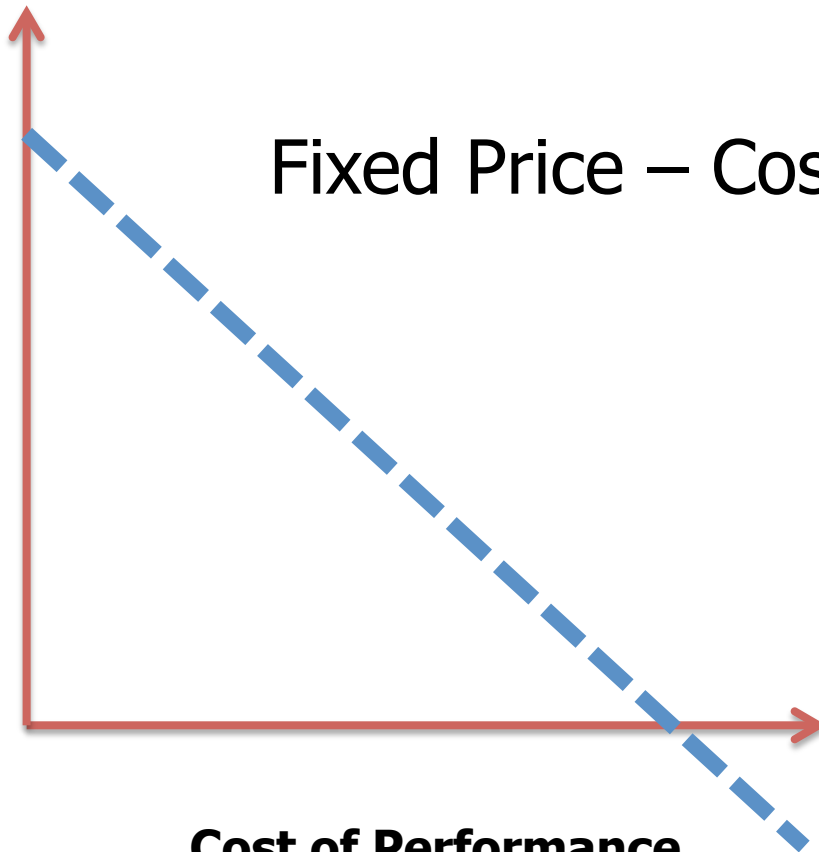
# Firm-Fixed-Price

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

$$\text{Fixed Price} - \text{Cost to Perform} = \text{Profit}$$



Profit  
or Fee

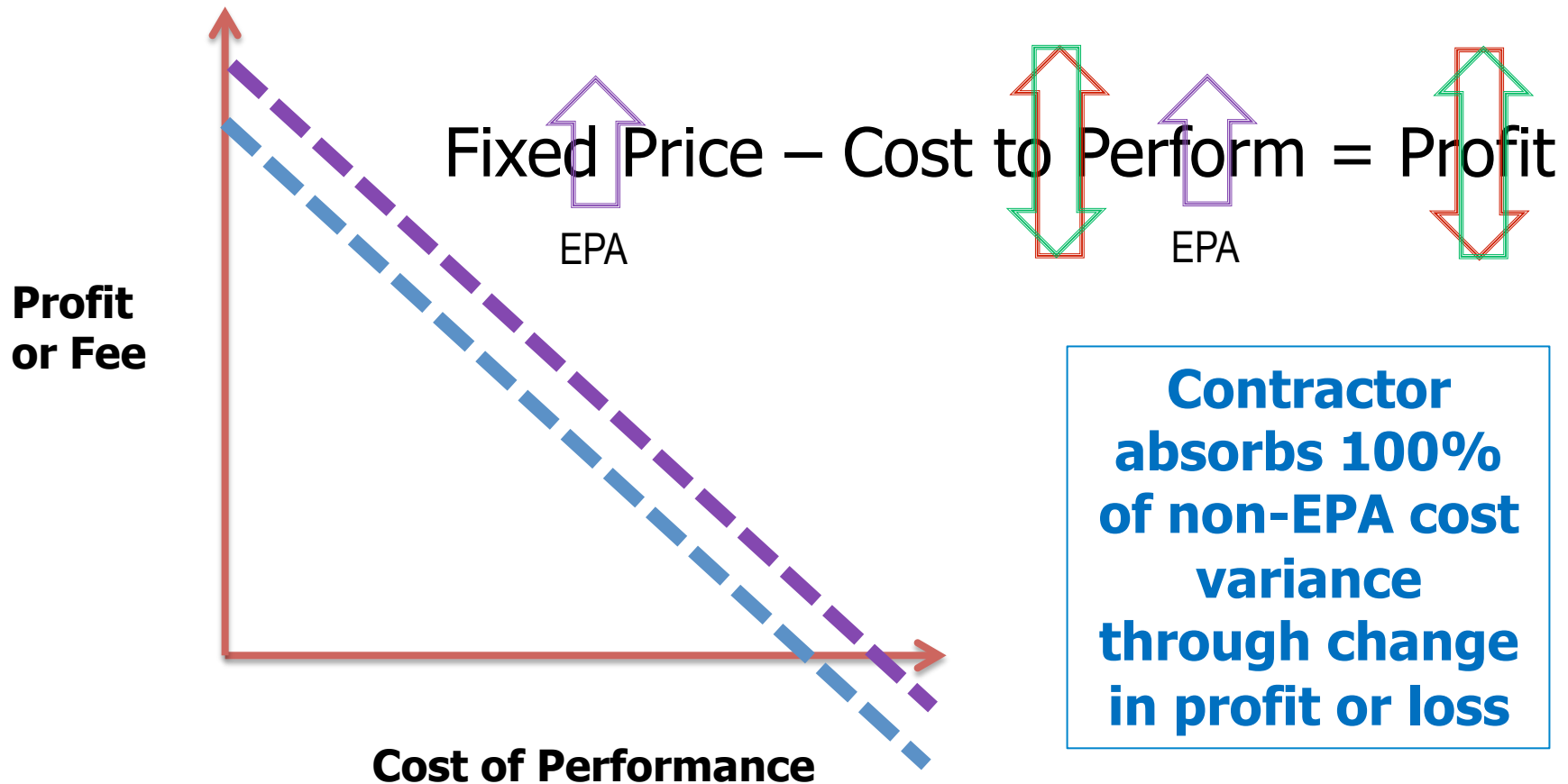


**Contractor  
absorbs 100%  
of cost variance  
through change  
in profit or loss**

Cost of Performance

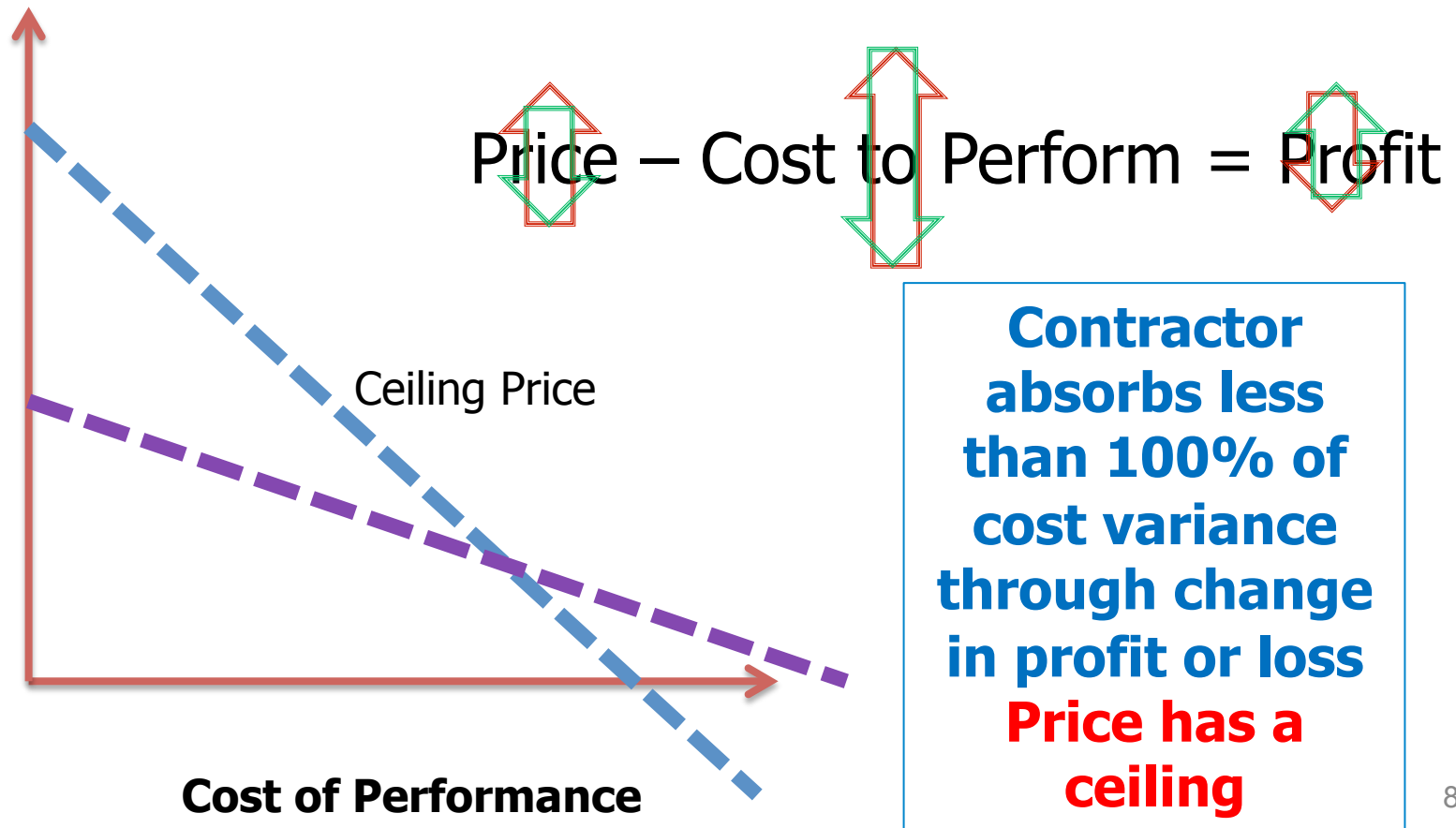
# Fixed-Price with Economic Price Adjustment

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



# Fixed-Price Incentive

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





# 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

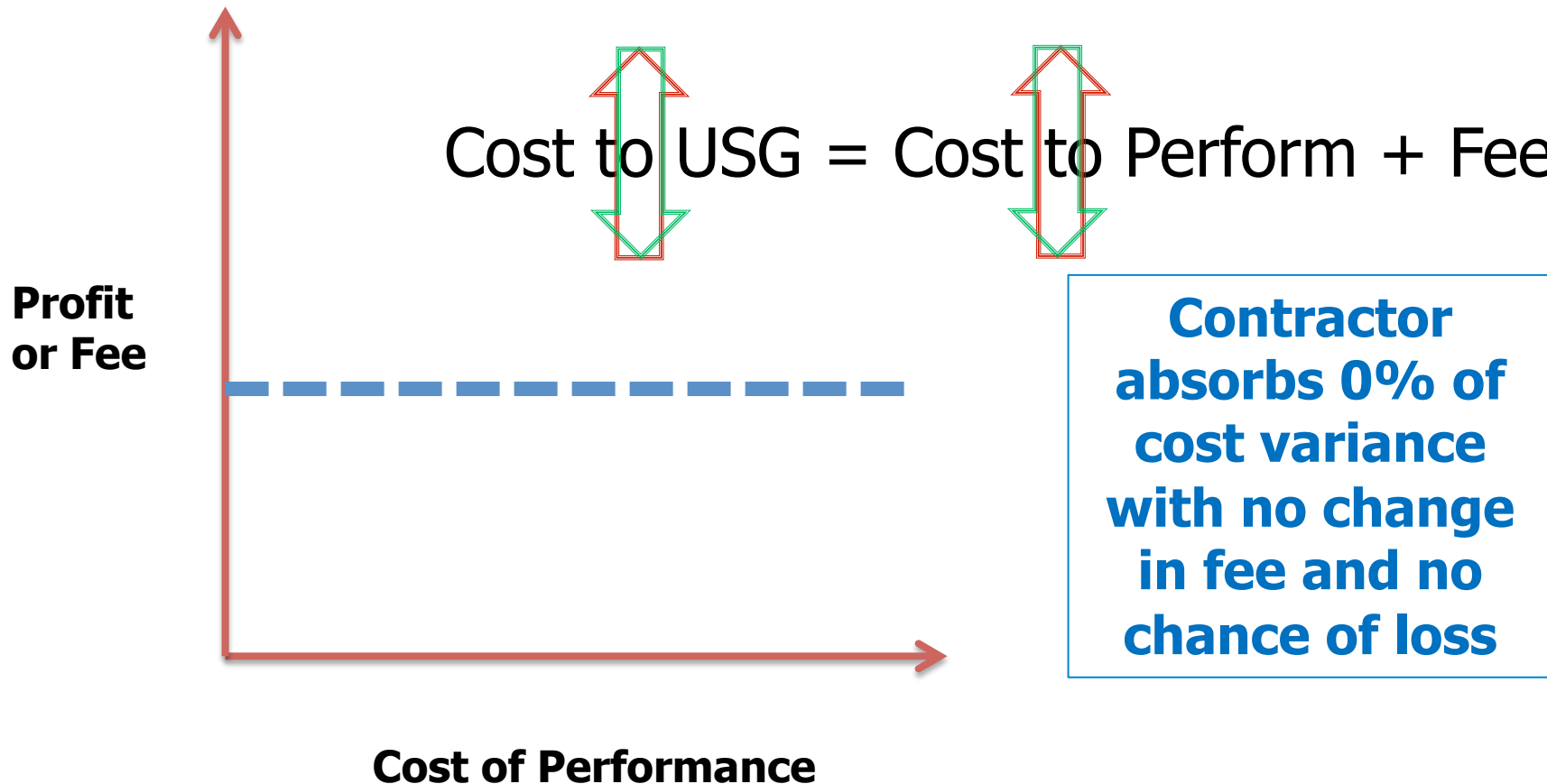
# Cost & Cost-Sharing Contracts

- 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

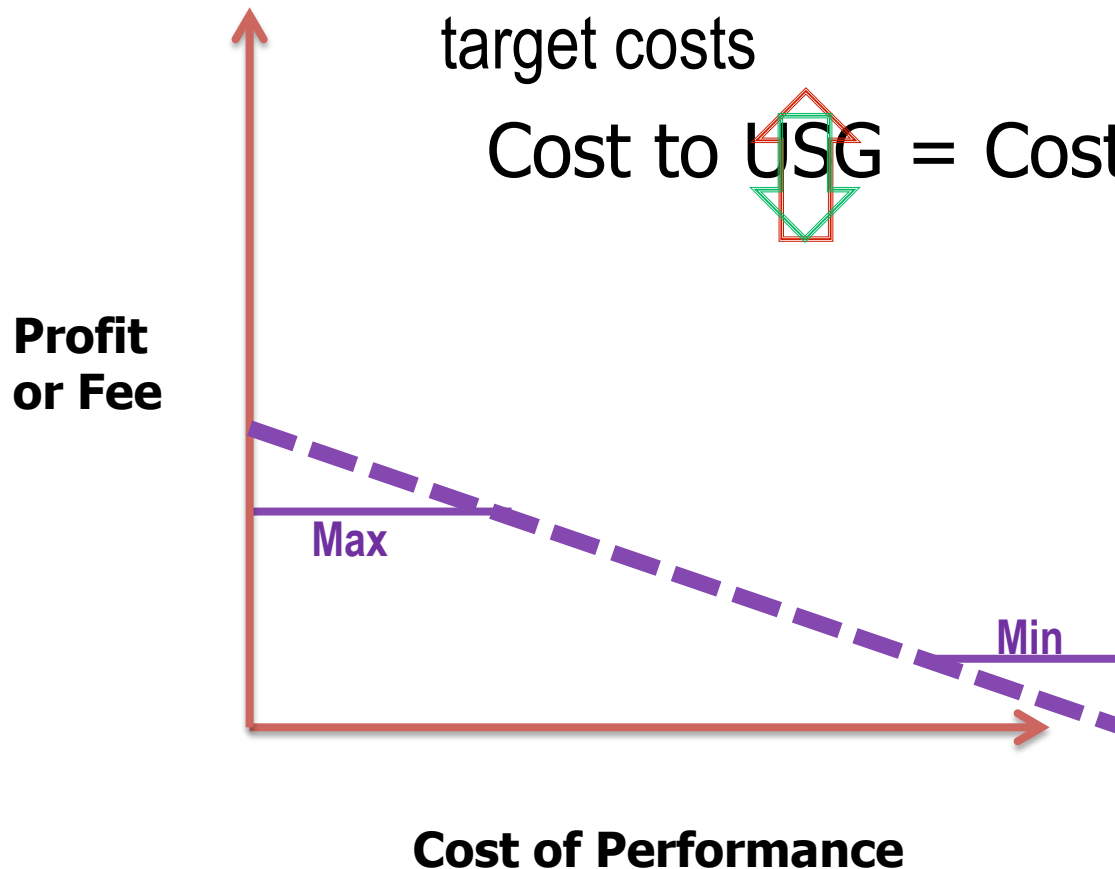
$$\text{Cost to USG} = \text{Cost to Perform} + \text{Fee}$$



# 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

$$\text{Cost to USG} = \text{Cost to Perform} + \text{Fee}$$



**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

# Cost-Plus-Award-Fee

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

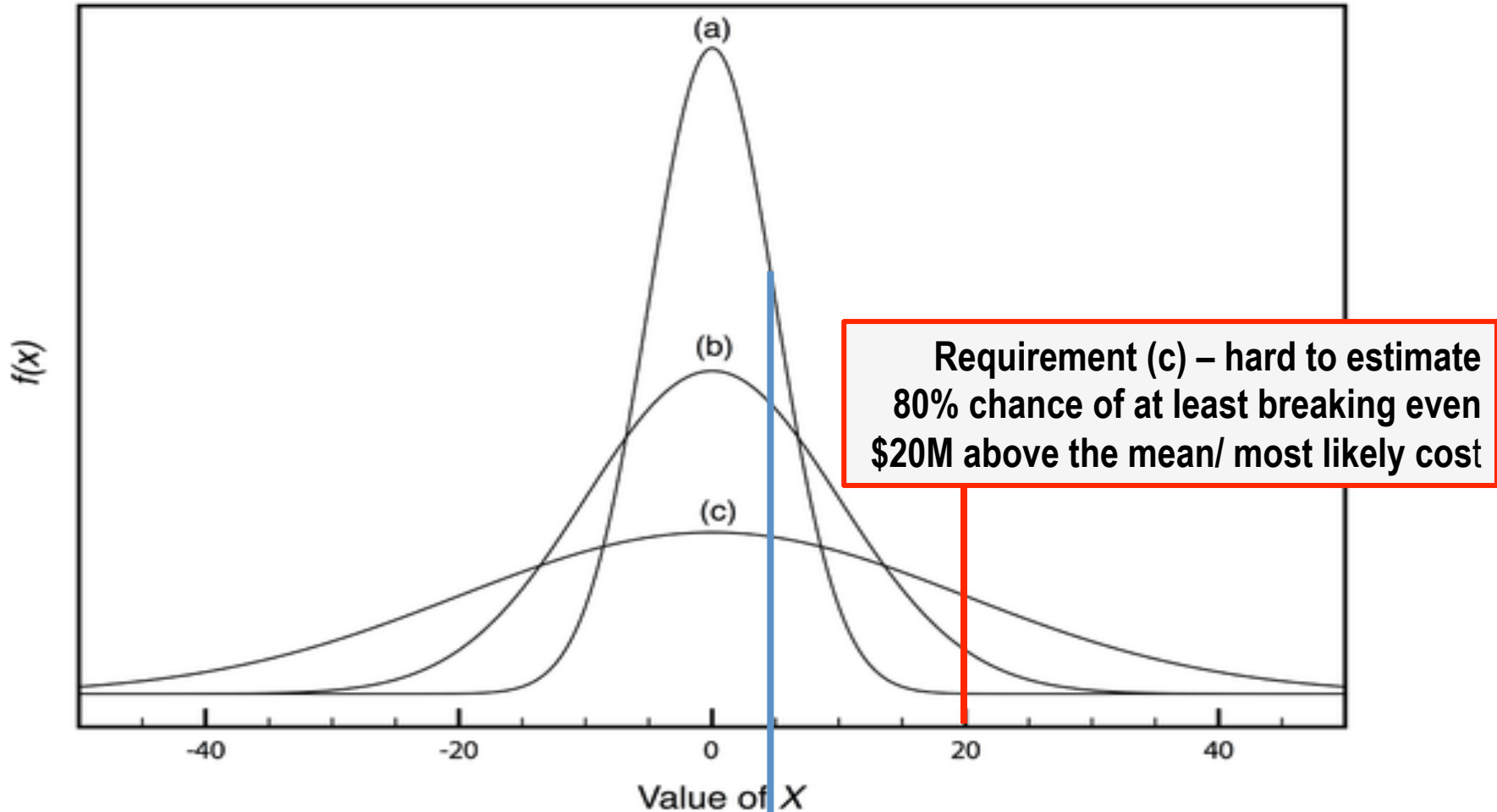
Low Risk – “Easy to estimate” type requirements

- 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

## Cost Reimbursement

- Extra-contractual incentives
- Best Efforts
- “Estimated” Cost & fee fixed
- Paid per AC&P (52.216-7) & fee schedule (comp. vs. term)
- Allowable cost audit to close
- Approved accounting system
- No financing needed with AC&P clause paying 100% cost every two weeks
- RDT&E, incremental funding
- No warranties, its yours
- Contractor Acquired Property (CAP) – Government owns.
- Work may be less well defined

## Fixed Price

- 100% cost incentive
- Deliver or default
- Only fixed price stated in contract
- Price paid at delivery per CLIN, SLIN, ELIN in schedule
- Financing (PP & PBP) for large \$, long delivery; PP requires approved accounting system
- Production, full funding required
- Latent defects, other warranties
- Contractor Acquired Property (CAP) – Contractor owns.
- Work must be well defined



# **Types of Contracts**

*Fred.Schlich@DAU.MIL*