(ii) Take all cash and trade discounts, rebates, allowances, credits, salvage, commissions, and other benefits. When unable to take advantage of the benefits, the Contractor shall promptly notify the Contracting Officer and give the reasons. The Contractor shall give credit to the Government for cash and trade discounts, rebates, scrap, commissions, and other amounts that have accrued to the benefit of the Contractor, or would have accrued except for the fault or neglect of the Contractor. The Contractor shall not deduct from gross costs the benefits lost without fault or neglect on the part of the Contractor, or lost through fault of the Government.

(7) Except as provided for in 31.205–26(e) and (f), the Government will not pay profit or fee to the prime Contractor on materials.

(c) If the Contractor enters into any subcontract that requires consent under the clause at 52.244–2, Subcontracts, without obtaining such consent, the Government is not required to reimburse the Contractor for any costs incurred under the subcontract prior to the date the Contractor obtains the required consent. Any reimbursement of subcontract costs incurred prior to the date the consent was obtained shall be at the sole discretion of the Government.

(d) *Total cost.* It is estimated that the total cost to the Government for the performance of this contract shall not exceed the ceiling price set forth in the Schedule, and the Contractor agrees to use its best efforts to perform the work specified in the Schedule and all obligations under this contract within such ceiling price. If at any time the Contractor has reason to believe that the hourly rate payments and material costs that will accrue in performing this contract in the next succeeding 30 days, if added to all other payments and costs previously accrued, will exceed 85 percent of the ceiling price in the Schedule, the Contractor shall notify the Contracting Officer giving a revised estimate of the total price to the Government for performing this contract with supporting reasons and documentation. If at any time during performing this contract, the Contractor has reason to believe that the total price to the Government for performing this contract will be substantially greater or less than the then stated ceiling price, the Contractor shall so notify the Contracting Officer, giving a revised estimate of the total price for performing this contract, with supporting reasons and documentation. If at any time during performing this contract, the Government has reason to believe that the work to be required in performing this contract will be substantially greater or less than the stated ceiling price, the Contracting Officer will so advise the Contractor, giving the then revised estimate of the total amount of effort to be required under the contract.

(e) *Ceiling price.* The Government will not be obligated to pay the Contractor any amount in excess of the ceiling price in the Schedule, and the Contractor shall not be obligated to continue performance if to do so would exceed the ceiling price set forth in the Schedule, unless and until the Contracting Officer notifies the Contractor in writing that the ceiling price has been increased and specifies in the notice a revised ceiling that shall constitute the ceiling price for performance under this contract. When and to the extent that the ceiling price set forth in the Schedule has been increased, any hours expended and material costs incurred by the Contractor in excess of the ceiling price before the increase shall be allowable to the same extent as if the hours expended and material costs had been incurred after the increase in the ceiling price.

(f) *Audit.* At any time before final payment under this contract, the Contracting Officer may request audit of the vouchers and supporting documentation. Each payment previously made shall be subject to reduction to the extent of amounts, on preceding vouchers, that are found by the Contracting Officer or authorized representative not to have been properly payable and shall also be subject to reduction for overpayments or to increase for underpayments. Upon receipt and approval of the voucher designated by the Contractor as the ''completion voucher'' and supporting documentation, and upon compliance by the Contractor with all terms of this contract (including, without limitation, terms relating to patents and the terms of paragraphs (f) and (g) of this clause), the Government shall promptly pay any balance due the Contractor. The completion voucher, and supporting documentation, shall be submitted by the Contractor as promptly as practicable following completion of the work under this contract, but in no event later than 1 year (or such longer period as the Contracting Officer may approve in writing) from the date of completion.

(g) *Assignment and Release of Claims.* The Contractor, and each assignee under an assignment entered into under this contract and in effect at the time of final payment under this contract, shall execute and deliver, at the time of and as a condition precedent to final payment under this contract, a release discharging the Government, its officers, agents, and employees of and from all liabilities, obligations, and claims arising out of or under this contract, subject only to the following exceptions:

(1) Specified claims in stated amounts, or in estimated amounts if the amounts are not susceptible of exact statement by the Contractor.

(2) Claims, together with reasonable incidental expenses, based upon the liabilities of the Contractor to third parties arising out of performing this contract, that are not known to the Contractor on the date of the execution of the release, and of which the Contractor gives notice in writing to the Contracting Officer not more than 6 years after the date of the release or the date of any notice to the Contractor that the Government is prepared to make final payment, whichever is earlier.

(3) Claims for reimbursement of costs (other than expenses of the Contractor by reason of its indemnification of the Government against patent liability), including reasonable incidental expenses, incurred by the Contractor under the terms of this contract relating to patents.

(h) *Interim payments on contracts for other than services.* (1) Interim payments made prior to the final payment under the contract are contract financing payments. Contract financing payments are not subject to the interest penalty provisions of the Prompt Payment Act.

(2) The designated payment office will make interim payments for contract financing on the _____ [*Contracting Officer insert day as prescribed by agency head; if not prescribed, insert ''30th''*] day after the designated billing office receives a proper payment request. In the event that the Government requires an audit or other review of a specific payment request to ensure compliance with the terms and conditions of the contract, the designated payment office is not compelled to make payment by the specified due date.

(i) *Interim payments on contracts for services.* For interim payments made prior to the final payment under this contract, the Government will make payment in accordance with the Prompt Payment Act (31 U.S.C. 3903) and prompt payment regulations at 5 CFR part 1315.

(End of Clause)

Alternate I (FEB 2007). If a labor-hour contract is contemplated, the Contracting Officer shall add the following paragraph (i) to the basic clause:

(i) The terms of this clause that govern reimbursement for materials furnished are considered to have been deleted.

[FR Doc. 06–9610 Filed 12–6–06; 8:45 am]

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DEPARTMENT OF DEFENSE

GENERAL SERVICES ADMINISTRATION

NATIONAL AERONAUTICS AND SPACE ADMINISTRATION

48 CFR Parts 2, 10, 12, 16, and 52

[FAC 2005–15; FAR Case 2003–027; Item II; Docket 2006–0020, Sequence 22]

RIN 9000–AK07

Federal Acquisition Regulation; FAR Case 2003–027, Additional Commercial Contract Types

AGENCIES: Department of Defense (DoD), General Services Administration (GSA), and National Aeronautics and Space Administration (NASA).

ACTION: Final rule.

SUMMARY: The Civilian Agency Acquisition Council and the Defense Acquisition Regulations Council (Councils) have agreed on a final rule amending the Federal Acquisition Regulation (FAR) to implement section 1432 of the National Defense Authorization Act for Fiscal Year 2004. Title XIV of the Act, referred to as the Services Acquisition Report Act of 2003 (SARA), amended section 8002(d) of the Federal Acquisition Streamlining Act of

1994 (FASA) to expressly authorize the use of time-and-materials (T&M) and labor-hour (LH) contracts for certain commercial services under specified conditions.

DATES: *Effective Date*: February 12, 2007.

FOR FURTHER INFORMATION CONTACT: For clarification of content, contact Mr. Jeremy Olson, at (202) 501–3221. Please cite FAC 2005–15, FAR case 2003–027. For information pertaining to status or publication schedules, contact the FAR Secretariat at (202) 501–4755.

SUPPLEMENTARY INFORMATION:

A. Background

This final rule amends the Federal Acquisition Regulation to implement section 1432 of the National Defense Authorization Act for Fiscal Year 2004 (Pub. L. 108–136). Title XIV of the Act, referred to as the Services Acquisition Reform Act of 2003 (SARA), amended section 8002(d) of the Federal Acquisition Streamlining Act of 1994 (FASA) (Pub. L. 103–355, 41 U.S.C. 264) to expressly authorize the use of time-and-materials (T&M) and labor-hour (LH) contracts for commercial services under specified conditions.

Section 8002(d)(3) of the Act limits use of T&M and LH contracts to the following categories of commercial services:

- Commercial services procured for support of a commercial item, as described in 41 U.S.C. 403(12)(E).
- Any other category of commercial services that is designated by the Administrator of Office of Federal Procurement Policy (OFPP) on the basis that—

1. The commercial services in such category are of a type of commercial services that are commonly sold to the general public through use of T&M or LH contracts; and

2. It would be in the best interests of the Federal Government to authorize use of T&M or LH contracts for purchase of the commercial services in such category.

In furtherance of its statutory responsibilities, OFPP worked in coordination with the Councils on a series of questions for the advance notice of proposed rulemaking (ANPR), the proposed rule, and the notices of public meeting published in the **Federal Register** at 69 FR 56316 on September 20, 2004 and at 70 FR 56318 on September 26, 2005, to obtain information describing how T&M and LH contracts are used commercially. In particular, the questions elicited information on the types of services that are commonly acquired on this basis and the circumstances under which these arrangements are used. Interested parties offered a variety of written observations in response to the ANPR and proposed rule. See the **Federal Register** at 70 FR 56320 on September 26, 2005. In addition, a number of interested parties provided oral comments during the public meetings that were held on October 19, 2004 and October 18, 2005, to facilitate an open dialogue with Government procurement policy officials.

OFPP and several Council staff members also received a briefing from the Government Accountability Office (GAO) on a survey the GAO conducted late last year to determine how often commercial companies use T&M and LH contracts in their commercial practices, either as a buyer or a provider. The GAO received 23 responses to its survey. Some of the responses came from Fortune 500 companies. Although responses were limited, the GAO indicated that they represented buying practices from a relatively wide range of industries, including airline, automotive and truck manufacturers, automotive and truck parts, business services, communications equipment, computer hardware, computer services, electric utilities, insurance, major drugs (pharmaceutical), money center bank, non-profit financial services, oil and gas, regional bank, retail (grocery and technology), scientific and technical instruments, and semiconductor.

Finally, OFPP reviewed testimony offered to the Acquisition Advisory Panel established pursuant to section 1423 of SARA to evaluate commercial practices and other acquisition-related issues. The Panel specifically sought input regarding industry's use of T&M and LH contracts. See *http://www.acquisition.gov/comp/aap/index.html*.

OFPP made three main findings from these inputs. First, commercial services are commonly sold on a T&M and LH basis in the marketplace when requirements are not sufficiently well understood to complete a well-defined scope of work and when risk can be managed by maintaining surveillance of costs and contractor performance. Second, these same services are also commonly sold on a fixed-price basis. Third, a few types of services are sold predominantly on a T&M and LH basis—specifically, emergency repair services. By their nature, emergency repair services are difficult to capture in a well-defined scope of work and therefore are not generally conducive to purchase on a fixed-price basis. Industry associations, representing a wide range of service industries, supported these findings in their comments in response to the ANPR, proposed rule, public meetings, and SARA Panel hearings.

OFPP advised the Councils that it is designating all categories of services (*i.e.*, any service) as being available for acquisition on a T&M and LH basis because the findings made in conjunction with the rulemaking indicate that: (1) services under any general categorization of services, such as those examined by the GAO, are *commonly* sold to the general public on a T&M and LH basis *under certain conditions*; and (2) use of T&M and LH contracts under these conditions may be in the Government's best interest. However, OFPP further advised that its designation is limited to the same circumstances that exist when T&M and LH contracting is commonly used to sell services to the general public and where the other prerequisites set forth in section 8002(d) have been met. OFPP concluded, in view of the findings, that the identification of effective boundaries for the use of T&M and LH contracts is a function of the specific circumstances surrounding the acquisition rather than the specific type of service being sold. OFPP requested that the Councils reflect its designation in the final FAR rule.

Specifically, OFPP requested that the rule allow an agency to purchase any commercial service on a T&M or LH basis if it has completed a determination and findings (D&F) containing sufficient facts and rationale to justify that a firm-fixed pricing arrangement is not suitable. With respect to the contents of the required D&F, OFPP advised the Councils that the rationale supporting use of a T&M or LH contract for commercial services must establish that a T&M or LH contract is being used under the same conditions where the private sector would commonly rely on these arrangements—namely, where it is not possible at the time of placing the contract or order to accurately estimate the extent or duration of the work or to anticipate costs with any reasonable degree of certainty. In addition, if the need is of a recurring nature and is being acquired through a contract extension or renewal, OFPP expects, consistent with FAR 7.103(r), that the D&F reflect why knowledge gained from the prior acquisition could not be used to further refine requirements and acquisition strategies in a manner that would enable purchase on a fixed-price basis.

OFPP reminded the Councils that agencies will also need to comply with the other limitations set forth in 8002(d)—*i.e.*, the service is acquired under a contract awarded using competitive procedures, the contract or

order includes a ceiling price that the contractor exceeds at its own risk, and any subsequent change in the ceiling price is authorized only upon a determination, documented in the contract file, that it is in the best interest of the procuring agency to change the ceiling price. Finally, OFPP requested that the rule include appropriate additional mechanisms that help agencies manage risk by maintaining surveillance of costs and contractor performance, since effective surveillance is emphasized in commercial use of T&M and LH contracts.

The Councils concur with OFPP's findings and conclusions and have shaped the rule accordingly.

DoD, GSA, and NASA published an advance notice of public rulemaking (ANPR) in the **Federal Register** at 69 FR 56316 on September 20, 2004 and a proposed rule at 70 FR 56318 on September 26, 2005. Comments were received from 13 respondents in response to the proposed rule. The Councils considered all of the comments and recommendations in developing the final rule. The Councils made the following changes to the rule as a result of the public comments and deliberations:

(1) 16.601(d)—Added a requirement for the head of contracting activity to approve any D&Fs that would extend the period of performance beyond five years for both commercial and non-commercial T&M contracts to help ensure T&M contracts are only used when no other type of contract is suitable, to maximize the use of fixed price commercial contracts consistent with the statute, and to avoid protracted use of non-commercial time-and-materials contracts after experience provides a basis for firmer pricing.

(2) Clause 52.212–4 Alternate I—

(a) Paragraph (i)(1)(ii)(B)—Eliminate the provisions that only permitted reimbursement of subcontract costs at the hourly rates in the contract schedule when the subcontractors are listed in contract because the provisions were problematic and contrary to standard commercial practice (see Comment 4.b.(6)(a)). Instead added provisions that require the subcontract to be reimbursed at the hourly rates prescribed in the contract except when the employees performing the work do not meet the qualifications specified in the contract.

(b) Paragraph (i)(1)(ii)(C)(2)—Eliminated the provisions that required commercial contractors to give the Government credit for rebates, refunds, or discounts that ''accrued to'' the contractor because the provision could have imposed unique Government accounting requirements on commercial T&M contracts (see Comment 4.b.(7)(b)).

(c) Paragraph (i)(1)(ii)(C)—Excluded indirect costs as a type of cost that could be reimbursed at actual costs since the indirect costs will be reimbursed at the fixed amount in the schedule(see Comment 4.b.(8)(a)).

(d) Paragraph (i)(1)(ii)(D)(1)—Revised the rule to allow contracting officers to establish the types of other direct costs (ODC) that will be reimbursed at actual costs and the fixed amounts for indirect costs at the order level on indefinite delivery indefinite quantity (IDIQ) contracts. The type of ODC that will be needed to perform an order and any fixed amount for indirect costs may need to be established on an order-by-order basis (see Comment 4.b.(8)(a)).

(e) Paragraph (i)(4)(ii)(A)—Revised the rule to recognize that companies use both paper-based and electronic timecards (see Comment 4.b.(9)(b)).

(f) Paragraph (u)—Eliminated the subcontract consent provisions because the provisions were unduly restrictive, inappropriate, and the provisions could have permitted the Government to inappropriately impact a company's commercial reputation (see Comment 4.b.(6)(a)).

Public Comment

The public comments are discussed below:

Comment: Commercial Item Definition. Agree with deleting the exclusion of ''services that are sold based on hourly rates without an established catalog or market price for a specific service performed or a specific outcome to be achieved'' from the definition of a commercial item to be consistent with SARA.

Comment: Market Research. Agree with adding ''type of contract'' to the examples provided for determining practices of firms engaged in producing, distributing, and supporting commercial items because it assists with the implementation of SARA.

Appropriate Use

Comment: Support OFPP's decision to restrict commercial T&M/LH contracts to circumstances where no other contract type is suitable instead of developing a list of commercial services commonly sold on a T&M/LH basis. The conditions for using commercial T&M/LH contracts (*i.e.*, the contracting officer executes a determination and finding that no other contract type is suitable, the contract includes a ceiling price that the contractor exceeds at its own risk, and subsequent changes in the ceiling price only authorized upon a determination that it is in the best interest of the Government) implement the statute in a clear and concise manner.

Comment: Support OFPP's conclusion that the use of T&M/LH contracts should not be limited to a list of specific categories of services. Many types of commercial services are sold and purchased on both T&M/LH and firm fixed-price (FFP) basis depending on the circumstances of the particular project. There are no general rules or practices that restrict use of T&M/LH to any specific service categories. Regardless of the service type, there are often times when work cannot be sufficiently defined at contract award to provide for meaningful firm-fixed prices.

Comment: Limit as much as possible the types of services eligible to be procured on a commercial T&M/LH basis. A list of the types of services commonly sold using commercial T&M vehicles would help contracting officers chose the appropriate contract type and draft the required D&F.

Response: As discussed above, OFPP's decision is based on its findings that— (a) commercial services are commonly sold on a T&M and LH basis in the marketplace when requirements are not sufficiently well understood to complete a well-defined scope of work and when risk can be managed by maintaining surveillance of costs and contractor performance; (b) these same services are also generally offered on a fixed-price basis; and (c) a few types of services are sold predominantly on a T&M and LH basis—specifically, emergency repair services. Based on these findings, OFPP recommended to the Councils that the rule allow an agency to purchase any commercial service on a T&M or LH basis if it has completed a determination and findings (D&F) containing sufficient facts and rationale to justify that a firm-fixed pricing arrangement is not suitable. OFPP stated that this conclusion is consistent with the statutory requirement in section 8002(d) that contracting officers must execute a D&F that establishes that no contract type is suitable before pursuing one of these arrangements. The Councils agree with OFPP's finding and shaped the rule accordingly. The Councils do not believe it is practical or feasible to develop and maintain a comprehensive list of services sold on a T&M/LH basis because many services may be sold on both a T&M/LH and fixed price basis depending on the circumstances of the acquisition. The rule clearly provides that commercial T&M/LH contracts can only be used when the other commercial services' contract types are not suitable.

Comment: Clarify whether competitive procedures means ''full and open competition'' or ''limited competition'' when the competition is conducted with as many sources as practicable under one of the authorities listed in FAR 6.302.

Response: Sole source commercial T&M/LH contracts are not authorized. Commercial T&M/LH contracts may be awarded under the statutory authorities that permit contracting without providing for full and open competition. When these authorities are used, contracting officers are required to solicit offers from as many potential sources as is practicable under the circumstances. Nothing in this rule requires ''full and open'' competition.

Comment: Restrict the use of T&M contracts to when it is not ''practicable'' instead of not ''possible'' at the time of placing the contract or order to accurately estimate the extent or duration of the work or to anticipate costs with any reasonable degree of certainty. It may be ''possible'' to estimate the duration and cost of work but impracticable given the time and effort that would be required, the urgency of the work, and the agencies competing priorities.

Response: T&M contracts comprise the highest contract type risk to the Government. As such, they should only be used when it is not possible at the time of award to estimate accurately the extent or duration of the work or to anticipate costs with any reasonable degree of confidence. Also, restricting the use of T&M contracts to when it is not ''possible'' is consistent with the requirements for non-commercial T&M contracts.

Determination and Finding (D&F)

Comment: Delete the minimum D&F requirements for justifying no other contract type is suitable because specifying the minimum requirements imposes a potentially greater burden on contracting officers than the corresponding provisions for non-commercial T&M/LH contracts. Delete the requirement to execute a D&F for each order when the indefinite-delivery contract is priced on a T&M/LH or FFP basis because it is inconsistent with FAR 1.602–2 which stipulates ''contracting officers should be allowed wide latitude to exercise business judgment.'' SARA requires a D&F to justify the contract type, not the use of the contract once justified.

Comment: Eliminate the requirement for approval one level above the contracting officer for a commercial T&M/LH IDIQ contract that only allows for issuance of orders on a T&M/LH basis to be consistent with non-commercial T&M/LH contracts. Commercial T&M/LH contracts pose no greater risk to the Government than non-commercial T&M/LH contracts.

Comment: The rule contradicts and goes beyond the intent of SARA by potentially creating, in practice and effect, a prohibition on the use of T&M contracts. Specifically, the rule adds administrative burden and procedural complication to the use of T&M contracts which would inhibit the use of these contracts as a practical contracting tool, *e.g.*, requiring a D&F for each T&M task order is beyond the intent of Section 1432 and appears to show little confidence in the business judgment of contracting officers.

Comment: Develop an approval level for D&Fs commensurate with the risk to the Government.

Response: The Councils acknowledge that the rule contains additional requirements for commercial T&M/LH IDIQ D&Fs than those required for noncommercial T&M/LH IDIQ D&Fs. While the Councils recognize these additional requirements may be more burdensome, the Councils believe the additional requirements are needed to encourage the preference for the use of fixed price contracts for commercial items. In addition, the Councils believe additional controls are needed to ensure both commercial and non-commercial T&M contracts are only used when no other type of contract is suitable. The Councils revised the rule to require head of contracting activity approval for any D&Fs that extend the performance period beyond five years for both commercial and non-commercial T&M contracts.

Comment: Establish a $100,000 threshold for D&F to recognize a reasonable level at which tangible deliverable would be expected.

Comment: Exempt small purchases at or below the five million dollar commercial item threshold at FAR 12.203 from the D&F requirements. This threshold allows agencies to use simplified acquisition procedures up to five million dollars for commercial item acquisitions. The Councils have discretion to implement the statutory provisions addressing D&Fs. See Chevron, U.S.A. v. Natural Resources Defense Council, Inc., 467 U.S. 837, 844 (1984).

Response: When a statute is silent or ambiguous with respect to a certain issue, agencies have discretion to interpret the statute in a reasonable manner, consistent with its legislative history. However, the statute is not ambiguous and the legislative history contains nothing which would support an interpretation that the D&F condition can be limited to a dollar threshold. The statute requires a D&F for T&M/LH contracts regardless of the dollar amount.

Nonconforming

Comment: Paying for reperformance, excluding profit, is a significant improvement over the ANPR and properly reflects commercial practices. The parties will be permitted to tailor the provision pursuant to FAR 12.302 when customary commercial practices provide different warranty terms.

Comment: Except for the default 10 percent profit rate, the proposed provisions are the same as those used for non-commercial T&M contracts. These provisions contain significant departures from terms typically found in the commercial marketplace. The proposed 10 percent default profit rate is irrelevant if the contracting officer knows the contractor's profit rate. Contracting officers could terminate the contract or retain another contractor to complete the work as provided in FAR 52.246–6(f) and (g) if a contractor is expending best efforts and still not performing properly. Require contracting officers to better focus on the requirements of FAR 7.105, Contents of Written Acquisition Plans, rather than adopting the proposed inspection and acceptance clause.

Comment: Contractors are under less budgetary pressure to perform under a T&M contract than a FFP contract and should be held to as stringent quality standards as FFP contracts. Paying for rework will not discourage ''shoddy work'' since the contractor will be reimbursed, without profit, for its costs. Develop an appropriate profit percentage based on historical data or some other measure to avoid a potential unintended consequence of establishing a 10 percent profit standard for T&M contracts. A 10 percent profit may be excessive for low risk T&M contracts.

Response: The comments reflect a varying set of commercial practices for nonconforming supplies and services. The ANPR required contractors to repair or replace rejected supplies or reperform rejected services at no cost to the Government. Public commenters on the ANPR said requiring contractors to repair or replace rejected supplies or reperform rejected services at no cost to the Government imposed more contract risk on the contractor than the non-commercial clause. The Government is essentially imposing a fixed-price level of risk. Combining a ceiling price that contractors exceed at their own risk and a requirement that the contractor use ''best efforts'' to perform within the

ceiling price means contractors are required accomplish a certain result (*i.e.*, performance of the work specified in the Schedule) within a specified dollar amount (*i.e.*, the ceiling price). The Councils agreed that contractors are generally only required to use ''best efforts'' to accomplish the desired results within the established ceiling price on both commercial and non-commercial T&M contracts as opposed to FFP contracts which requires contractors to accomplish stated results within the fixed price. Therefore, the Councils revised the proposed rule to be consistent with the non-commercial T&M requirements. The 10 percent default profit rate will only be used when the contracting officer does not know the contractor's actual profit rate, which may be commonplace in competitive awards. Contractors are under less budgetary pressure to perform under a T&M than a FFP contract. However, it is not appropriate to hold contractors to the same standards used on FFP contracts. The risk of ''shoddy work'' is inherent to all ''best efforts'' type contracts. Accordingly, T&M/LH contracts are only authorized when no other contract type is suitable. The 10 percent default profit rate is arbitrary, not necessarily representative of the actual profit rates. However, the rate is intended to protect the Government by helping to ensure profit is not paid for replacement or reperformance.

Comment: The proposed rule does not address reimbursement of costs for providing accommodations to the Government for testing and inspections at contractor and subcontractors' facility. Fairness dictates that the Government reimburse contractors and subcontractors for reasonable costs incurred for the required accommodations.

Response: The costs for providing accommodations to the Government for testing and inspecting at contractor and subcontractors' facilities are generally included in the fully burdened labor rate.

Subcontracts and Interdivisional Labor

Comment: Reimburse subcontract labor at the schedule labor rates without listing the subcontractors in the contract for standard commercial services, *e.g.*, ''on-call'' IT installation and repair services in support of commercial IT products. Reimburse subcontract labor at the schedule labor rates without listing the subcontractors in the contract when the contractor's proposal indicates that some of the work may be performed by subcontractors that meet the contract's qualification requirements and that the price for that ''type of work'' will be the prime contract's labor rate which may be blended or other rate. Reimburse subcontract labor at the schedule labor rates without subcontract consent when the subcontractor personnel satisfy the qualification and other requirements for the labor categories for which the contractor is seeking compensation. T&M/LH contracts specify the required labor qualifications. Whether the person filling the position is an employee of the prime or a subcontractor, the qualifications must be met. The Government has already determined the price for the ''type of work'' to be fair and reasonable by competition. Include interdivisional transfers and subcontracted labor costs as elements of ''time'' instead of ''materials'' to allow prime contractors to recover adequate compensation for the time and resources it expends on administering subcontracts and for the financial exposure is assumes for its subcontractor's performance.

Comment: Appreciate the Councils efforts to clarify the treatment for subcontracts and interdivisional transfers but recommends reimbursing all subcontract labor at the schedule labor rates to avoid confusion over whether the costs are reimbursable as ''material'' or ''labor.'' Separately address the proper treatment for subcontracts and interdivisional labor to avoid inevitable disputes over whether the costs should be treated as ''labor'' or ''material.'' Contractors frequently require use of subcontractors for any number of reasons included to:

(a) Secure specific skill sets;

(b) Augment an existing workforce;

(c) Use small and/or small, disadvantaged businesses to meet socioeconomic goals;

(d) Incorporate small business innovative solutions; and

(e) Replace subcontractors during contract performance for failure to achieve the prime contractor's performance standards.

Prime contractors may not know which subcontractors will be used to perform the work since T&M contracts are used when it is not possible to estimate accurately the extent or duration of work at the time of award. Contractors will not know at the time of award which subcontractors may be used to fulfill ''on call'' or ''on demand'' services. It is unfair to require contractors to perform services without knowing in advance whether the necessary subcontractors can be brought to task and how the contractor will be reimbursed. Expand the definition of ''subcontract'' to clarify that subcontracts on commercial contracts includes ''transfers of commercial items between divisions, subsidiaries, or affiliates of a contractor or subcontractor'' to be consistent with FASA which specified interdivisional transfers for commercial items are to be treated as subcontracts (see FAR 12.001). Clarify the provisions that allow contractors to be reimbursed for its own material at the contractor's established catalog or the market price includes services that meet the definition of a commercial item at FAR 2.101. Do not object to appropriate subcontractor disclosure requirements when the contractor does not have an approved purchasing system and the subcontract will be cost-reimbursement, time-and-materials, labor-hour, or letter contract (see FAR 44.201(b)(1)) but the Government should not interject its authority over the prime contractor's determination of how to accomplish the work being bid and awarded. Recommend the Councils instead consider a notification requirement without the need for formal contract amendment. In the commercial world, sellers are generally free to delegate their duties to subcontractors as they see fit. In the Government world, agencies make these determinations in the evaluation of a contractor's proposal and through oversight of awarded work. The Government could be exposed to claims for delay or disruption when the contractor is attempting to substitute one qualified subcontractor for another and approvals are improperly denied or unreasonable delayed. The Councils concerns that the basis for ''best value'' determination used to award the contract may be altered by contractors adding or substituting subcontractors after award do not justify the provisions that limit reimbursement of subcontract costs to those listed in the contract or those subsequently approved by the contracting officer. The question is not one of reimbursement but of Government payment for services rendered. The attendant administrative procedures in the proposed rule might impede the contractor's ability to deliver services in accordance with the terms of the contract. The ''consent to subcontract'' provisions and payment limitations significantly increase the risk to contractors for meeting contract deliverables. The administrative and financial burden of establishing and maintaining a list of subcontractors that can be reimbursed at the hourly schedule rates increases contract execution risk.

Comment: Consent to subcontract is inconsistent with the underlying intent of commercial acquisitions.

Coalition and Comment: Reimburse interdivisional transfers at the schedule hourly rates like subcontract labor. The proposed rule restricts reimbursement for interdivisional transfers (*e.g.*, transfers from divisions, subsidiaries, and affiliates under the common control of the commercial contractor) to cost, without profit or fee, unless the interdivisional transfer meets the definition of a commercial item at FAR 2.101. Commercial contractors will be required to identify the actual costs, potentially subjecting their allowability to a determination under the cost principles. Commercial contractors should have the ability to use any of their resources without penalty of profit erosion. These contracts have commercial market reference points and disallowing profit discourages vendors from using their best employees to meet the Government's needs.

Comment: Revise the instructions for reimbursing subcontracts at the schedule rate to clearly permit the listing of actual or ''potential'' subcontractor name(s) since the subcontractors listed for reimbursement at the schedule hourly rates may reflect a pool of ''potential'' subcontractors that may or may not actually work on the contract.

Comment: Reimburse all subcontract costs at the schedule hourly rates without requiring contracting officer consent to be consistent with commercial practices.

Comment: Reimburse subcontract efforts requiring consent only if proper advance consent is obtained. Do not allow contracting officers to retroactively grant consent for subcontracts.

Comment: Restrict reimbursement of subcontract costs to actual costs because the prime contractor could subsequently negotiate lower rates with subcontractors that were authorized to be paid at the schedule rates and the Government would pay excessive prices for subcontracted effort that may be of a level less than that envisioned by the Government. Reimbursement at the schedule rates encourages contractors to maximize profit by subcontracting out more of the effort at lower subcontract rates. Government will expend additional resources to monitor the quality and efficiency of subcontract labor since the subcontract effort will not be readily apparent when billed at the schedule rates.

Comment: Restrict reimbursement of subcontract costs to actual costs as long as those costs do not exceed the prime's rates. Subcontractors have reported primes charging prime contractor labor rates for the subcontractor's labor while paying the subcontractors significantly lower rates. Vendors should make a reasonable profit on services provided to the Government but there is no justification for unduly enriching contractors by allowing them to charge their own higher rates for subcontract effort. Permitting contractors to bill their established rates for work they subcontract out will likely have the unintended consequence of creating new vendor organizations developed solely to extract higher profits from Government projects. Contractors that believe the Government is best served by permitting the wide use of subcontracts are free to do so in FFP agreements. Revise or restate in a clearer fashion the provisions regarding reimbursement for subcontract efforts at proposed FAR 52.212–4(i)(1)(ii)(B) because the provisions are difficult to follow.

Response: The methodology in the proposed rule was problematic and contrary to standard commercial practice.

First, the rule permitted reimbursement of commercial materials, including subcontracts and interdivisional transfers, at the contractor's established catalog or market price. At the same time, the rule limited reimbursement of qualifying commercial subcontracts to actual costs unless the subcontracts were listed in the contract for reimbursement at the hourly schedule rates. For some commercial companies, the established catalog or market price for its commercial material (including subcontracts and interdivisional transfers) is the prime contractor's established catalog or market price for labor. Reimbursing commercial materials at actual cost is inconsistent with commercial practices and contrary to the statutory preference for acquisitions of commercial items and the intent of FASA, *i.e.*, established acquisition policies more closely resembling those of the commercial marketplace. In addition, subcontracts under FAR Part 12 include transfers of commercial items between divisions, subsidiaries, or affiliates of a contractor or subcontractor. While the actual costs for subcontracts other than interdivisional transfers can be easily determined from an independent third party invoice, actual costs for interdivisional transfers can only be determined using the procedures of FAR Part 31. Imposing FAR Part 31 requirements on commercial interdivisional transfers is contrary to commercial practices and the intent of FASA. Further, the proposed rule failed to fully consider the implications of subsequently altering the elements included in the catalog or market prices. The catalog or market prices will be determined fair and reasonable based on competition. Subsequent modifications to the elements of those prices could impact the overall pricing integrity and the fair and reasonable determination. Finally, limiting reimbursement to actual costs discourages subcontracting and would have a negative impact on small businesses. Small businesses traditionally receive approximately 35 percent of subcontracts on Government prime contracts and only 24 percent of prime Government contracts. Reimbursing subcontracts at actual costs is not consistent with the treatment on all other flexibly priced Government contracts where prime contractors are paid profit on subcontract costs. Restricting reimbursement of subcontract costs to actual costs ''as long as those costs do not exceed the prime's rates'' is not equitable or fair. Upon further consideration, the Councils believe it is appropriate to reimburse commercial subcontracts at the schedule labor rates without listing the subcontracts when the contractor's established catalog or market price includes the price of its subcontracts for the reasons discussed above. The Councils revised the rule accordingly. In addition, the Councils believe imposing subcontract consent requirements on these commercial subcontracts is unduly restrictive and inappropriate and revised the rule accordingly. If a contracting officer failed to provide a timely consent or disagreed with the subcontract award, the Government could wrongly affect contract performance and potentially impact a company's commercial reputation. The Councils also revised the rule to recognize that subcontracts under FAR Part 12 include transfers of commercial items between divisions, subsidiaries, and affiliates of a contractor or subcontractor to be consistent with FAR 12.001. Finally, the Councils did not believe it was necessary to clarify that qualifying services are commercial items since the definition of commercial items at FAR 2.101 clearly identifies the services that meet the definition of commercial services.

Comment: Agree subcontract consent applies only to costs that are directly charged to the contract and not overhead expenses and G&A but recommend explicitly stating so in the final rule to avoid future questions about the application of this provision.

Response: As noted above, the final rule does not require subcontract consents.

Material Costs

Comment: Agree there should be no ''most favored customer'' pricing requirement because it is a barrier for market entry and inconsistent with the Government pricing policies at FAR Subpart 15.4.

Comment: Refunds. Reimbursement of material at actual costs less any rebates, refunds, or discounts received by or accrued to the contractor is contrary to commercial practice which does not rely on cost accounting information. If an accrual entry is made at all, the accrual is typically identified to more global considerations (*e.g.*, total volume of purchases), not individual contract actions. The reference to accruals and other cost accounting data is not appropriate.

Comment: Delete the requirement for commercial companies to give the Government credit for rebates from interdivisional labor since the divisions will likely have little visibility into the other business units.

Comment: Delete the requirement to provide the Government credit for rebates on commercial T&M contracts. Vendors typically provide some services (*e.g.*, maintenance on standard equipment) through the organizational resources of their commercial business. Federal entities have little visibility into those business units, creating a dilemma as to how to account for a rebate.

Response: The Councils do not believe it is appropriate to require unique Government accounting requirements for materials on commercial T&M/LH contracts. The Councils revised the rule to only require contractors to reduce the costs of material for any rebates, refunds, or discounts that are identifiable to the contract.

Comment: Revise the proposed provisions to say modification to items that meet the definition of commercial items at FAR 2.101 are reimbursed at ''price'' instead of ''actual costs'' for to be consistent with FAR Subpart 15.4.

Response: Depending on the circumstance of a particular acquisition, it may be appropriate to pay ''price'' instead of ''costs'' for modifications to commercial items. To provide maximum flexibility to the contracting officer, the Councils revised the rule to permit reimbursement at either price or cost.

Indirect Costs and Other Direct Costs

Comment: Exclude indirect costs from the definition of material costs to eliminate the two contradictory methods for reimbursing indirect costs. The proposed rule permits reimbursement at a fixed amount but also defines indirect costs as an element of material costs that can only be reimbursed at actual costs unless the material meets the definition of commercial item.

Response: The Councils revised the rule to eliminate the contradictory methods. Instead of excluding indirect costs from the definition of materials, the Councils revised the provisions in the alternate clause at FAR 52.212–4, Alternate I (i)(1)(ii)(D)(2) to exclude indirect costs from being reimbursed at actual cost.

Comment: Agree with the provisions that permit reimbursement of indirect costs at a fixed price on a pro-rata basis over the period of contract performance but recommend clarifying that the fixed price could be adjusted as new work is added and also allowing contractors to be reimbursed at the Government approved percentage mark-up for non-commercial contracts. Cost Accounting Standards (CAS) covered contractors are required to allocate material handling in accordance with their approved accounting practices. Material handling rates are well-recognized in Federal and commercial markets. The Councils are proposing to reimburse indirect costs at a fixed price because of concerns over violating the cost-plus-a-percentage-of-cost prohibition. Material handling rates do not add fee or any other price component to cost and therefore could not be considered a cost-plus-a-percentage-of-cost violation. Recommend revising the coverage to permit contractors to recover material handling provided it is excluded from the hourly rates.

Response: If new work is added, a fixed amount may be added for indirect expenses if appropriate. Nothing in the rule prevents contract changes. The approved percentage mark-up for non-commercial contracts is subject to the allowability provisions of FAR Part 31. The Councils believe it is more appropriate to reimburse indirect costs without imposing the requirements of FAR Part 31 to be consistent with commercial practices. While the commenter disagrees, the Councils believe use of a fixed rate violates the cost plus percentage of cost contract prohibition. CAS covered contractors already allocate material handling and other indirect costs to commercial and non-commercial FFP contracts in accordance with their disclosed accounting practices. While the costs are allocated to those FFP contracts, the allocation may be different from the amounts recovered under the contracts for those elements of cost.

Comment: Clarify which contracting officer (the contracting officer who awards the contract or the one that awards the task order) has the authority and ability to make determination on the method for reimbursing subcontract efforts and the allowability of ODC and indirect costs for IDIQ or Multiple Award Schedule (MAS) contracts.

Response: As stated in the alternate clause at (i)(1)(ii)(D)(1) and (2) of 52.212–4, Alternate I, the contracting officer awarding the indefinite delivery contract can authorize other contracting officers to determine how ODC and indirect costs will be reimbursed.

Comment: Revise the rule to clarify ODC and indirect costs will only be recovered as stand alone elements of costs if the amounts are not also included in the loaded labor rates.

Response: ODC and indirect costs should only be recovered as separate elements of costs if they are excluded from the schedule labor rates. However, contracting officers will not always know the elements of costs included in the schedule labor rates since commercial T&M/LH contracts can only be awarded using competitive procedures. Generally, contracting officers are precluded from obtaining detailed cost information on these types of acquisitions. However, contracting officers will know the proposed amount for indirect expenses and the types of ODC proposed to be reimbursed at actual costs for each competing contractor during the proposal evaluation phase.

Government Oversight

Comment: The right to interview contractor employees is unreasonable intrusive and contrary to customary commercial practice. Notwithstanding a statement by the Councils to the contrary, no similar right exists in the FAR for any contract type. The audit clause at FAR 52.215–2 gives the contracting officer the right to examine ''records and other evidence'' to verify claimed costs. Records are not defined to include interviews and it is hard to believe ''other evidence'' includes employee interviews. This new right lacks precedent in the FAR. Not even the Offices of Inspector General under the Inspectors General Act has this authority. The Government does not need this newly created contractual right because the Government already has this right in cases of alleged fraud or wrongdoing pursuant to its subpoena powers under applicable statutes. The Government should rely on the invoices which are required, under penalty of

law, to be accurate. The right to interview employees is not required by SARA or any other law. This authority also conflicts with FASA which requires commercial item contracts contain only those terms and conditions that are required by law or customary in the commercial marketplace. There is no provision in SARA for this approach, a fact recognized by Defense Contract Audit Agency (DCAA) in its April 9, 2004 ''GSA Schedule'' memorandum.

Comment: Commercial T&M/LH contracts are subject to a strict oversight process performed by company project managers that are accountable for the successful completion of the work.

Comment: Oppose the rule because commercial contracts will not be subject to full oversight and audit provisions. To protect taxpayer interests, commercial T&M/LH contracts should be subject to full oversight, audits, and CAS. Additionally, the commercial T&M contracts need clauses for refunds or price reduction so the Government can recoup overages identified in the audit.

Comment: Remove the restriction that limits the Government's access to records to those listed in the contract because the Government should not limit its access to records.

Response: The rule permits, but does not require, contracting officers to have access to contractor employees. While such access may not be a standard commercial practice, the Councils believe employee interviews may be necessary in some cases to verify the hours claimed by the contractor. According to one commenter in response to the ANPR, requiring access to contractor employees is a standard commercial practice for T&M contracting. The provisions for access to contractor employees are no broader than what is currently provided for under non-commercial T&M contracts. FAR 52.215–2, Audit and Records—Negotiation, provides the Government the right to examine and audit all records and other evidence sufficient to reflect properly all cost claimed to have been incurred or anticipated to be incurred directly or indirectly in performance of the contract. The Government routinely conducts employee interviews and other audit procedures to verify that labor costs at contractor locations having fixed-price, cost-reimbursement, incentive, non-commercial time-and-material and labor hour, commercial, or price redeterminable contracts are charged to the correct contract and not inappropriately shifted to the flexibly priced Government contracts. Employee interviews are part of DCAA's normal surveillance of Government contracts and are required by DCAA's Mandatory Annual Audit Requirements (MAARs). The Government should not have to allege wrongdoing to interview contractor employees when their labor hours are included on invoices submitted to the Government. The Councils do not believe that SARA or FASA requires the Government to make payments based on actual hours incurred without being able to verify the employees actually worked the hours charged. The Councils have carefully considered existing requirements for T&M contracts as well as differences between commercial and non-commercial contracts. The Councils believe that the rule provides the proper balance between the need to verify compliance with contract terms and the need to minimize access to contractor records. Finally, the Councils believe the oversight provided in the rule will provide sufficient information to verify the validity of amounts claimed on the contract without the oversight requirements in FAR and CAS that are imposed on noncommercial T&M/LH contracts.

Comment: Define the term ''original timecards'' broadly enough to encompass both paper-based and electronic timecards because many companies use electronic timecards.

Response: The Councils revised the final rule to provide access to original timecards (paper-based or electronic).

Comment: Provide contracting officers specific guidance regarding what prime oversight efforts are adequate for subcontracts listed in the contract and reimbursed at the schedule rates. Contracting officers may lack the expertise or time to assess the existence or quality of a contractor's mechanism to oversee the qualifications and hours worked by subcontractor employees. The only way to substantiate qualifications and hours worked is through examination of payrolls and resumes for each subcontractor.

Response: The prime contractor is responsible for the oversight of its subcontractors. When requested by the Government, the contractors are required to substantiate invoices (including any subcontractor hours reimbursed at the hourly rate in the schedule) by evidence of actual payment, individual daily job timecards, records that verify the employees meet the qualifications for the labor categories specified in the contract, or other substantiation specified in the contract. Contracting officers can seek the advice of the cognizant audit office when needed. Training would be more appropriately addressed in agency training materials.

Withholds

Comment: Explicitly state contracting officers cannot withhold on commercial T&M/LH contracts because some contracting officers may elect to withhold even though the practice is not specifically allowed by the payment clause.

Response: We do not contemplate withholds in commercial contracts but there may be circumstances, at the contracting officer's discretion, where withholds are appropriate.

Contractor Purchasing System Review (CPSR)

Comment: The proposed rule prohibits contractors with firm fixed-price (FFP) or FFP with economic price adjustment (EPA) contracts from obtaining approved purchasing systems thereby creating a ''class of contractor'' that can never obtain an approved purchasing system. This new class of contractors will have more oversight in terms of subcontractor approval and approval of subcontract modifications. These contractors are currently exempt from the subcontract approval process—an exemptions supported by FASA and FARA.

Comment: Do not impose CPSR on commercial contractors because doing so may deter commercial companies from doing business with the Government. Commercial contractors may not perform sufficient Government business to justify the establishment of a CPSR.

Response: The objective of a contractor purchasing system review (CPSR) is to evaluate the efficiency and effectiveness with which the contractor spends Government funds. The review provides the cognizant contracting officer a basis for granting, withholding, or withdrawing approval of the contractor's purchasing system. Under the existing FAR requirements, the Government does not review a contractor's purchasing system if all the contractor's Governments sales are commercial FFP and FFP EPA contracts. The same is true if all a contractor's Government sales are non-commercial competitively awarded firm-fixed-price and competitively awarded fixed-price with economic price adjustment contracts. For these types of contracts, the Government has no reason to evaluate the efficiency and effectiveness with which the contractor spends Government funds since the amounts paid to the contractor are not affected by the efficiency and effectiveness of the contractors' purchasing practices. The

proposed rule did not impose a CPSR requirement but simply recognized that contractors who otherwise have approved purchasing systems require less oversight of their subcontractors because the contractor's overall system provides adequate controls and procedures to protect the Government. However, the Councils revised the rule to eliminate the subcontract consent requirement which means subcontracts for T&M contracts awarded pursuant to FAR Part 12 will be excluded from CPSRs.

Cost Accounting Standards (CAS)

Comment: Do not apply CAS and other onerous Government-only requirements to commercial T&M/LH contracts because doing so is counter to acquisition reform legislation that envisions the Government purchasing more like its commercial counterparts. Congress exempted commercial item contracts from CAS; however, the CAS Board only exempted FFP and FFP EPA contracts. Agree the Councils lack the authority to make CAS changes but recommend the Councils implement the statute and treat T&M contracts as covered by the existing CAS exclusions.

Response: The decision as to whether CAS applies to commercial T&M/LH contracts rests with the CAS Board. The Councils have limited the imposition of other Government-only requirements to the maximum extent practicable. The Councils do not believe commercial T&M/LH contracts are currently exempted by any CAS exemption and therefore cannot simply waive the requirements of CAS.

Total Cost

Comment: The rule establishes a notification procedure much like the limitation of cost and limitation of funds clauses for non-commercial items. Since this rule involves contracts for commercial items, suggest it instead refer to ''Total Price.''

Response: While the rule relates to commercial T&M/LH contracts, some material and ODC will be reimbursed at ''cost'' not ''price.'' Therefore, the Councils did not revise the title as suggested.

General Comments

Comment: Do not support the rule in its present form.

Comment: In a number of areas, the proposed rule simply imports into this commercial items regulation many of the terms and conditions already used by the Government when purchasing non-commercial T&M/LH contracts. This action results in the inclusion of provisions that are significant departures from standard commercial practices, contrary to the spirit of FASA and in violation of FAR 12.301(a)(2) that require commercial item contracts to only include those clauses determined to be consistent with customary commercial practices. Other provisions of the rule extend the Government's audit and oversight inappropriately and unnecessary. Deeply concerned that the proposed rule will undercut the intent of SARA by creating what effectively amounts to a prohibition on the use of T&M contracts. The rule adds significant administrative burden, procedural complications, and certain significant financial disincentives. Recommend the Councils reconsider the entire approach to T&M contracting and the expansive rulemaking in the proposed rule. Also, recommend the Councils hold additional public meetings to provide the public additional opportunities to explain the submitted comments. Recommend delaying issuance of a final rule until the Acquisition Advisory Panel has released its report and recommendations since there may be a conflict between their recommendations and this rule.

Response: The Councils reviewed public comments and held two public meetings, obtaining a very complete picture of the views of interested parties on this rule, and have determined it is appropriate to go forward with a final rule. It is highly unlikely that further comments or public meetings would provide any information or opinions not already provided and evaluated.

Comment: Concur.

Comment: Industry does not prefer T&M contracts and would avoid them for IT work.

Response: T&M/LH contracts represent the highest contract type risk and industry, like the Government, avoids using them to the maximum extent practicable. However, there are circumstances when these contract types are needed and used.

Comment: The main difference between the commercial market and the rule is the rule only requires the contractor to use its ''best efforts'' to perform within the ceiling. There is no consumer in the commercial market that would blindly allow a car repair shop to work on their car for up to $1,000 without any guarantee that the car will be fixed.

Response: T&M/LH contracts, commercial and non-commercial, are ''best effort'' contracts that can only be used when it is not possible at the time of placing the contract or order to accurately estimate the extent or duration of the work or to anticipate costs with any reasonable degree of certainty. If it is possible to estimate the extent or duration of work or anticipate costs with a reasonable degree of certainty, T&M/LH contracts should not be used.

Comment: The use of the term ''schedule'' may be confusing to some who understand it to refer to MAS or FSSs contracts. The subcontract reimbursement provisions that permit reimbursement of subcontracts at the hourly rates prescribed in the schedule could be interpreted to mean there are separate subcontract rates on MAS contracts. Clarify the final rule the term is not meant to connote MAS contracts.

Response: The term is used throughout the FAR and widely understood by contracting professionals. The Councils are unaware of any issues with its interpretation and does not believe changing the term could be confusing to contracting professionals.

This is not a significant regulatory action and, therefore, was not subject to review under Section 6(b) of Executive Order 12866, Regulatory Planning and Review, dated September 30, 1993. This rule is not a major rule under 5 U.S.C. 804.

B. Regulatory Flexibility Act

The Regulatory Flexibility Act, 5 U.S.C. 601, *et seq.*, applies to this final rule. The Councils prepared a Final Regulatory Flexibility Analysis (FRFA), and it is summarized as follows:

1. Statement of need for, and objectives of, the rule.

This final rule revises the Federal Acquisition Regulation to allow contracting officers to award Time and Material and Labor Hour (T&M/LH) contracts when procuring commercial items. This FAR case was initiated to implement Section 1432 of the National Defense Authorization Act for Fiscal Year 2004 (Pub. L. 108–136).

2. Summary of significant issues raised by the public comments in response to the Initial Regulatory Flexibility Analysis (IRFA), a summary of the assessment of the agency of such issues, and a statement of any changes made in the proposed rule as a result of such comments.

Thirteen (13) comments were received from the public in response to the proposed rule. One of the most significant areas of controversy in the proposed rule issued for public comment concerned the matter of labor provided by subcontractors. The proposed rule required that the prime contractor be reimbursed at actual cost for all subcontractors providing labor under the contract, unless a subcontractor was specifically authorized under the prime contract by inclusion on a list of subcontractors to be reimbursed at the prime contract labor hour rate. Public commenters complained that this procedure created major administrative burdens and, because reimbursement at actual cost did not permit

prime contractors to obtain profit of those subcontracts, it would significantly reduce the use of subcontractors. The commenters pointed out that the subcontractors at issue are commonly small businesses.

The final rule eliminates this feature regarding payment of labor subcontractors at actual cost and use of a list of approved subcontractors. The final rule provides that a prime contractor can provide qualifying labor hours under the contract through use of subcontractors and the government will pay the prime contract labor hour rate, without use of any pre-authorization list in the contract. Prime contractors will be able to include profit on this labor and there will be no special administrative approvals required. The final rule approach eliminates the part of the proposed rule that was most objectionable to small entities.

3. Description of, and an estimate of the number of, small entities to which the rule will apply or an explanation of why no such estimate is available.

This rule will apply to small and large entities that accept Time-and-Material or Labor-Hour contracts for commercial items. Because this rule is the first FAR authorization for use of these types of contracts for commercial items, no history is available on the number of awards made to small businesses. However, the Federal Procurement Data System (FPDS) data from FY 2004 show that small businesses received approximately 50 percent of the 42,840 noncommercial item T&M/LH awards made and approximately 30% of the $17 Billion obligated under those awards.

4. Description of the projected reporting, recordkeeping, and other compliance requirements of the rule, including an estimate of the classes of small entities which will be subject to the requirement and the type of professional skills necessary for preparation of the report or record.

The rule would require contractors to maintain records to support invoices presented to the Government for payment. Such records would include original timecards, the contractor's timekeeping procedures, distribution of labor, invoices for material, and so forth. These are standard records maintained by any company, large or small, and the fact that the contract would require that these records be made available to the Government should not place any additional record keeping burden on the entity.

5. Description of steps the agency has taken to minimize significant economic impact on small entities consistent with the stated objectives of applicable statutes, including a statement of the factual, policy, and legal reasons for selecting the alternative adopted in the final rule and why each of the other significant alternatives to the rule considered by the agency was rejected.

Public comments submitted in response to the proposed rule were reviewed and substantial policy adjustments to the rule were made as a result. One of the most significant areas of controversy in the proposed rule issued for public comment concerned the matter of labor provided by subcontractors. The proposed rule required that the prime contractor be reimbursed at actual cost for all subcontractors providing labor under the contract, unless a subcontractor was specifically authorized under the prime contract by inclusion on a list of subcontractors to be reimbursed at the prime contract labor hour rate. Public commenters complained that this procedure created major administrative burdens and, because reimbursement at actual cost did not permit prime contractors to obtain profit of those subcontracts, it would significantly reduce the use of subcontractors. The commenters pointed out that the subcontractors at issue are commonly small businesses.

The final rule eliminates this feature regarding payment of labor subcontractors at actual cost and use of a list of approved subcontractors. The final rule provides that a prime contractor can provide qualifying labor hours under the contract through use of subcontractors and the government will pay the prime contract labor hour rate, without use of any pre-authorization list in the contract. Prime contractors will be able to include profit on this labor and there will be no special administrative approvals required. The final rule approach eliminates the part of the proposed rule that was most objectionable to small entities.

Interested parties may obtain a copy of the FRFA from the FAR Secretariat. The FAR Secretariat has submitted a copy of the FRFA to the Chief Counsel for Advocacy of the Small Business Administration.

C. Paperwork Reduction Act

The Paperwork Reduction Act does not apply because the changes to the FAR do not impose information collection requirements that require the approval of the Office of Management and Budget under 44 U.S.C. 3501, *et seq.*

List of Subjects in 48 CFR Parts 2, 10, 12, 16, and 52

Government procurement.

Dated: December 4, 2006.

Linda K. Nelson,

Deputy Director, Contract Policy Division.

■ Therefore, DoD, GSA, and NASA amend 48 CFR parts 2, 10, 12, 16, and 52 as set forth below:

■ 1. The authority citation for 48 CFR parts 2, 10, 12, 16, and 52 continues to read as follows:

Authority: 40 U.S.C. 121(c); 10 U.S.C. chapter 137; and 42 U.S.C. 2473(c).

PART 2—DEFINITIONS OF WORDS AND TERMS

2.101 [Amended]

■ 2. Amend section 2.101 in paragraph (b), in the definition ''Commercial item'', by removing the second sentence in the introductory text of paragraph (6).

PART 10—MARKET RESEARCH

10.001 [Amended]

■ 3. Amend section 10.001 by removing from paragraph (a)(3)(iv) ''as terms'' and adding ''as type of contract, terms'' in its place.

■ 4. Amend section 10.002 by revising paragraph (b)(1)(iii) to read as follows:

10.002 Procedures.

* * * * *

(b) * * *

(1) * * *

(iii) Customary practices, including warranty, buyer financing, discounts, contract type considering the nature and risk associated with the requirement, etc., under which commercial sales of the products or services are made;

* * * * *

PART 12—ACQUISITION OF COMMERCIAL ITEMS

■ 5. Revise section 12.207 to read as follows:

12.207 Contract type.

(a) Except as provided in paragraph (b) of this section, agencies shall use firm-fixed-price contracts or fixed-price contracts with economic price adjustment for the acquisition of commercial items.

(b)(1) A time-and-materials contract or labor-hour contract (see Subpart 16.6) may be used for the acquisition of commercial services when—

(i) The service is acquired under a contract awarded using—

(A) Competitive procedures (*e.g.*, the procedures in 6.102, the set-aside procedures in Subpart 19.5, or competition conducted in accordance with Part 13);

(B) The procedures for other than full and open competition in 6.3 provided the agency receives offers that satisfy the Government's expressed requirement from two or more responsible offerors; or

(C) The fair opportunity procedures in 16.505, if placing an order under a multiple award delivery-order contract; and

(ii) The contracting officer—

(A) Executes a determination and findings (D&F) for the contract, in accordance with paragraph (b)(2) of this section (but see paragraph (c) of this section for indefinite-delivery contracts), that no other contract type authorized by this subpart is suitable;

(B) Includes a ceiling price in the contract or order that the contractor exceeds at its own risk; and

(C) Authorizes any subsequent change in the ceiling price only upon a determination, documented in the

contract file, that it is in the best interest of the procuring agency to change the ceiling price.

(2) Each D&F required by paragraph (b)(1)(ii)(A) of this section shall contain sufficient facts and rationale to justify that no other contract type authorized by this subpart is suitable. At a minimum, the D&F shall—

(i) Include a description of the market research conducted (see 10.002(e));

(ii) Establish that it is not possible at the time of placing the contract or order to accurately estimate the extent or duration of the work or to anticipate costs with any reasonable degree of certainty; and

(iii) Establish that the requirement has been structured to maximize the use of firm-fixed-price or fixed-price with economic price adjustment contracts (*e.g.*, by limiting the value or length of the time-and-material/labor-hour contract or order; establishing fixed prices for portions of the requirement) on future acquisitions for the same or similar requirements.

(iv) Describe actions planned to maximize the use of firm-fixed-price or fixed-price with economic price adjustment contracts on future acquisitions for the same requirements.

(3) See 16.601(d)(1) for additional approval required for contracts expected to extend beyond three years.

(c)(1) Indefinite-delivery contracts (see Subpart 16.5) may be used when—

(i) The prices are established based on a firm-fixed-price or fixed-price with economic price adjustment; or

(ii) Rates are established for commercial services acquired on a time-and-materials or labor-hour basis.

(2) When an indefinite-delivery contract is awarded with services priced on a time-and-materials or labor-hour basis, contracting officers shall, to the maximum extent practicable, also structure the contract to allow issuance of orders on a firm-fixed-price or fixed-price with economic price adjustment basis. For such contracts, the contracting officer shall execute the D&F required by paragraph (b)(2) of this section, for each order placed on a time-and-materials or labor-hour basis. Placement of orders shall be in accordance with Subpart 8.4 or 16.5, as applicable.

(3) If an indefinite-delivery contract only allows for the issuance of orders on a time-and-materials or labor-hour basis, the D&F required by paragraph (b)(2) of this section shall be executed to support the basic contract and shall also explain why providing for an alternative firm-fixed-price or fixed-price with economic price adjustment pricing structure is not practicable. The D&F for this contract shall be approved one level above the contracting officer. Placement of orders shall be in accordance with Subpart 16.5.

(d) The contract types authorized by this subpart may be used in conjunction with an award fee and performance or delivery incentives when the award fee or incentive is based solely on factors other than cost (see 16.202–1 and 16.203–1).

(e) Use of any contract type other than those authorized by this subpart to acquire commercial items is prohibited.

■ 6. Amend section 12.301 by adding a sentence after the first sentence in paragraph (b)(3) to read as follows:

12.301 Solicitation provisions and contract clauses for the acquisition of commercial items.

* * * * *

(b) * * *

(3) * * * Use this clause with its Alternate I when a time-and-materials or labor-hour contract will be awarded. * * *

* * * * *

■ 7. Amend section 12.403 by revising paragraph (d)(1)(i) to read as follows:

12.403 Termination.

* * * * *

(d) * * *

(1) * * *

(i)(A) The percentage of the contract price reflecting the percentage of the work performed prior to the notice of the termination for fixed-price or fixed-price with economic price adjustment contracts; or

(B) An amount for direct labor hours (as defined in the Schedule of the contract) determined by multiplying the number of direct labor hours expended before the effective date of termination by the hourly rate(s) in the Schedule; and

* * * * *

PART 16—TYPES OF CONTRACTS

■ 8. Amend section 16.601 by adding a sentence to the end of paragraph (c) introductory text and revising paragraph (d) to read as follows:

16.601 Time-and-materials contracts.

* * * * *

(c) *Application.* * * * See 12.207(b) for the use of time-and-material contracts for certain commercial services.

* * * * *

(d) *Limitations.* A time-and-materials contract may be used only if—

(1) The contracting officer prepares a determination and findings that no other contract type is suitable. The determination and finding shall be—

(i) Signed by the contracting officer prior to the execution of the base period or any option periods of the contracts; and

(ii) Approved by the head of the contracting activity prior to the execution of the base period when the base period plus any option periods exceeds three years; and

(2) The contract includes a ceiling price that the contractor exceeds at its own risk. The contracting officer shall document the contract file to justify the reasons for and amount of any subsequent change in the ceiling price. Also see 12.207(b) for further limitations on use of Time-and-Materials or Labor Hour contracts for acquisition of commercial items.

* * * * *

■ 9. Revise section 16.602 to read as follows:

16.602 Labor-hour contracts.

Description. A labor-hour contract is a variation of the time-and-materials contract, differing only in that materials are not supplied by the contractor. See 12.207(b), 16.601(c), and 16.601(d) for application and limitations, for time-and-materials contracts that also apply to labor-hour contracts. See 12.207(b) for the use of labor-hour contracts for certain commercial services.

PART 52—SOLICITATION PROVISIONS AND CONTRACT CLAUSES

■ 10. Amend section 52.212–4 by—

■ a. Revising the date of the clause;

■ b. Adding a new sentence after the third sentence in the introductory text of paragraph (a); and

■ c. Adding Alternate I;

■ The revised and added text reads as follows:

52.212–4 Contract Terms and Conditions—Commercial Items.

* * * * *

CONTRACT TERMS AND CONDITIONS—COMMERCIAL ITEMS (FEB 2007)

(a) *Inspection/Acceptance.* * * * If repair/replacement or reperformance will not correct the defects or is not possible, the Government may seek an equitable price reduction or adequate consideration for acceptance of nonconforming supplies or services. * * *

* * * * *

(End of clause)

Alternate I (FEB 2007). When a time-and-materials or labor-hour contract is contemplated, substitute the following paragraphs (a), (e), (i) and (l) for those in the basic clause.

(a) *Inspection/Acceptance.* (1) The Government has the right to inspect and test all materials furnished and services performed under this contract, to the extent practicable at all places and times, including

the period of performance, and in any event before acceptance. The Government may also inspect the plant or plants of the Contractor or any subcontractor engaged in contract performance. The Government will perform inspections and tests in a manner that will not unduly delay the work.

(2) If the Government performs inspection or tests on the premises of the Contractor or a subcontractor, the Contractor shall furnish and shall require subcontractors to furnish all reasonable facilities and assistance for the safe and convenient performance of these duties.

(3) Unless otherwise specified in the contract, the Government will accept or reject services and materials at the place of delivery as promptly as practicable after delivery, and they will be presumed accepted 60 days after the date of delivery, unless accepted earlier.

(4) At any time during contract performance, but not later than 6 months (or such other time as may be specified in the contract) after acceptance of the services or materials last delivered under this contract, the Government may require the Contractor to replace or correct services or materials that at time of delivery failed to meet contract requirements. Except as otherwise specified in paragraph (a)(6) of this clause, the cost of replacement or correction shall be determined under paragraph (i) of this clause, but the ''hourly rate'' for labor hours incurred in the replacement or correction shall be reduced to exclude that portion of the rate attributable to profit. Unless otherwise specified below, the portion of the ''hourly rate'' attributable to profit shall be 10 percent. The Contractor shall not tender for acceptance materials and services required to be replaced or corrected without disclosing the former requirement for replacement or correction, and, when required, shall disclose the corrective action taken. [*Insert portion of labor rate attributable to profit.*]

(5)(i) If the Contractor fails to proceed with reasonable promptness to perform required replacement or correction, and if the replacement or correction can be performed within the ceiling price (or the ceiling price as increased by the Government), the Government may—

(A) By contract or otherwise, perform the replacement or correction, charge to the Contractor any increased cost, or deduct such increased cost from any amounts paid or due under this contract; or

(B) Terminate this contract for cause.

(ii) Failure to agree to the amount of increased cost to be charged to the Contractor shall be a dispute under the Disputes clause of the contract.

(6) Notwithstanding paragraphs (a)(4) and (5) above, the Government may at any time require the Contractor to remedy by correction or replacement, without cost to the Government, any failure by the Contractor to comply with the requirements of this contract, if the failure is due to—

(i) Fraud, lack of good faith, or willful misconduct on the part of the Contractor's managerial personnel; or

(ii) The conduct of one or more of the Contractor's employees selected or retained by the Contractor after any of the Contractor's managerial personnel has reasonable grounds to believe that the employee is habitually careless or unqualified.

(7) This clause applies in the same manner and to the same extent to corrected or replacement materials or services as to materials and services originally delivered under this contract.

(8) The Contractor has no obligation or liability under this contract to correct or replace materials and services that at time of delivery do not meet contract requirements, except as provided in this clause or as may be otherwise specified in the contract.

(9) Unless otherwise specified in the contract, the Contractor's obligation to correct or replace Government-furnished property shall be governed by the clause pertaining to Government property.

(e) *Definitions.* (1) The clause at FAR 52.202–1, Definitions, is incorporated herein by reference. As used in this clause—

(i) *Direct materials* means those materials that enter directly into the end product, or that are used or consumed directly in connection with the furnishing of the end product or service.

(ii) *Hourly rate* means the rate(s) prescribed in the contract for payment for labor that meets the labor category qualifications of a labor category specified in the contract that are—

(A) Performed by the contractor;

(B) Performed by the subcontractors; or

(C) Transferred between divisions, subsidiaries, or affiliates of the contractor under a common control.

(iii) *Materials* means—

(A) Direct materials, including supplies transferred between divisions, subsidiaries, or affiliates of the contractor under a common control;

(B) Subcontracts for supplies and incidental services for which there is not a labor category specified in the contract;

(C) Other direct costs (*e.g.*, incidental services for which there is not a labor category specified in the contract, travel, computer usage charges, etc.);

(D) The following subcontracts for services which are specifically excluded from the hourly rate: [*Insert any subcontracts for services to be excluded from the hourly rates prescribed in the schedule.*]; and

(E) Indirect costs specifically provided for in this clause.

(iv) *Subcontract* means any contract, as defined in FAR Subpart 2.1, entered into with a subcontractor to furnish supplies or services for performance of the prime contract or a subcontract including transfers between divisions, subsidiaries, or affiliates of a contractor or subcontractor. It includes, but is not limited to, purchase orders, and changes and modifications to purchase orders.

(i) *Payments.* (1) *Services accepted.* Payment shall be made for services accepted by the Government that have been delivered to the delivery destination(s) set forth in this contract. The Government will pay the Contractor as follows upon the submission of commercial invoices approved by the Contracting Officer:

(i) *Hourly rate.*

(A) The amounts shall be computed by multiplying the appropriate hourly rates prescribed in the contract by the number of direct labor hours performed. Fractional parts of an hour shall be payable on a prorated basis.

(B) The rates shall be paid for all labor performed on the contract that meets the labor qualifications specified in the contract. Labor hours incurred to perform tasks for which labor qualifications were specified in the contract will not be paid to the extent the work is performed by individuals that do not meet the qualifications specified in the contract, unless specifically authorized by the Contracting Officer.

(C) Invoices may be submitted once each month (or at more frequent intervals, if approved by the Contracting Officer) to the Contracting Officer or the authorized representative.

(D) When requested by the Contracting Officer or the authorized representative, the Contractor shall substantiate invoices (including any subcontractor hours reimbursed at the hourly rate in the schedule) by evidence of actual payment, individual daily job timecards, records that verify the employees meet the qualifications for the labor categories specified in the contract, or other substantiation specified in the contract.

(E) Unless the Schedule prescribes otherwise, the hourly rates in the Schedule shall not be varied by virtue of the Contractor having performed work on an overtime basis.

(*1*) If no overtime rates are provided in the Schedule and the Contracting Officer approves overtime work in advance, overtime rates shall be negotiated.

(*2*) Failure to agree upon these overtime rates shall be treated as a dispute under the Disputes clause of this contract.

(*3*) If the Schedule provides rates for overtime, the premium portion of those rates will be reimbursable only to the extent the overtime is approved by the Contracting Officer.

(ii) *Materials.*

(A) If the Contractor furnishes materials that meet the definition of a commercial item at FAR 2.101, the price to be paid for such materials shall be the contractor's established catalog or market price, adjusted to reflect the—

(*1*) Quantities being acquired; and

(*2*) Any modifications necessary because of contract requirements.

(B) Except as provided for in paragraph (i)(1)(ii)(A) and (D)(2) of this clause, the Government will reimburse the Contractor the actual cost of materials (less any rebates, refunds, or discounts received by the contractor that are identifiable to the contract) provided the Contractor—

(*1*) Has made payments for materials in accordance with the terms and conditions of the agreement or invoice; or

(*2*) Makes these payments within 30 days of the submission of the Contractor's payment request to the Government and such payment is in accordance with the terms and conditions of the agreement or invoice.

(C) To the extent able, the Contractor shall—

(*1*) Obtain materials at the most advantageous prices available with due regard to securing prompt delivery of satisfactory materials; and

(*2*) Give credit to the Government for cash and trade discounts, rebates, scrap, commissions, and other amounts that are identifiable to the contract.

(D) *Other Costs.* Unless listed below, other direct and indirect costs will not be reimbursed.

(*1*) *Other Direct Costs.* The Government will reimburse the Contractor on the basis of actual cost for the following, provided such costs comply with the requirements in paragraph (i)(1)(ii)(B) of this clause: [Insert each element of other direct costs (*e.g., travel, computer usage charges, etc. Insert ''None'' if no reimbursement for other direct costs will be provided. If this is an indefinite delivery contract, the Contracting Officer may insert ''Each order must list separately the elements of other direct charge(s) for that order or, if no reimbursement for other direct costs will be provided, insert 'None''.'*]

(*2*) *Indirect Costs (Material Handling, Subcontract Administration, etc.*). The Government will reimburse the Contractor for indirect costs on a pro-rata basis over the period of contract performance at the following fixed price: [*Insert a fixed amount for the indirect costs and payment schedule. Insert ''$0'' if no fixed price reimbursement for indirect costs will be provided. (If this is an indefinite delivery contract, the Contracting Officer may insert ''Each order must list separately the fixed amount for the indirect costs and payment schedule or, if no reimbursement for indirect costs, insert 'None').''*]

(2) *Total cost.* It is estimated that the total cost to the Government for the performance of this contract shall not exceed the ceiling price set forth in the Schedule and the Contractor agrees to use its best efforts to perform the work specified in the Schedule and all obligations under this contract within such ceiling price. If at any time the Contractor has reason to believe that the hourly rate payments and material costs that will accrue in performing this contract in the next succeeding 30 days, if added to all other payments and costs previously accrued, will exceed 85 percent of the ceiling price in the Schedule, the Contractor shall notify the Contracting Officer giving a revised estimate of the total price to the Government for performing this contract with supporting reasons and documentation. If at any time during the performance of this contract, the Contractor has reason to believe that the total price to the Government for performing this contract will be substantially greater or less than the then stated ceiling price, the Contractor shall so notify the Contracting Officer, giving a revised estimate of the total price for performing this contract, with supporting reasons and documentation. If at any time during performance of this contract, the Government has reason to believe that the work to be required in performing this contract will be substantially greater or less than the stated ceiling price, the Contracting Officer will so advise the Contractor, giving the then revised estimate of the total amount of effort to be required under the contract.

(3) *Ceiling price.* The Government will not be obligated to pay the Contractor any amount in excess of the ceiling price in the Schedule, and the Contractor shall not be obligated to continue performance if to do so would exceed the ceiling price set forth in the Schedule, unless and until the Contracting Officer notifies the Contractor in writing that the ceiling price has been increased and specifies in the notice a revised ceiling that shall constitute the ceiling price for performance under this contract. When and to the extent that the ceiling price set forth in the Schedule has been increased, any hours expended and material costs incurred by the Contractor in excess of the ceiling price before the increase shall be allowable to the same extent as if the hours expended and material costs had been incurred after the increase in the ceiling price.

(4) *Access to records.* At any time before final payment under this contract, the Contracting Officer (or authorized representative) will have access to the following (access shall be limited to the listing below unless otherwise agreed to by the Contractor and the Contracting Officer):

(i) Records that verify that the employees whose time has been included in any invoice meet the qualifications for the labor categories specified in the contract;

(ii) For labor hours (including any subcontractor hours reimbursed at the hourly rate in the schedule), when timecards are required as substantiation for payment—

(A) The original timecards (paper-based or electronic);

(B) The Contractor's timekeeping procedures;

(C) Contractor records that show the distribution of labor between jobs or contracts; and

(D) Employees whose time has been included in any invoice for the purpose of verifying that these employees have worked the hours shown on the invoices.

(iii) For material and subcontract costs that are reimbursed on the basis of actual cost—

(A) Any invoices or subcontract agreements substantiating material costs; and

(B) Any documents supporting payment of those invoices.

(5) *Overpayments/Underpayments.* (i) Each payment previously made shall be subject to reduction to the extent of amounts, on preceding invoices, that are found by the Contracting Officer not to have been properly payable and shall also be subject to reduction for overpayments or to increase for underpayments. The Contractor shall promptly pay any such reduction within 30 days unless the parties agree otherwise. The Government within 30 days will pay any such increases, unless the parties agree otherwise. The contractor's payment will be made by check. If the Contractor becomes aware of a duplicate invoice payment or that the Government has otherwise overpaid on an invoice payment, the Contractor shall immediately notify the Contracting Officer and request instructions for disposition of the overpayment.

(ii) Upon receipt and approval of the invoice designated by the Contractor as the ''completion invoice'' and supporting documentation, and upon compliance by the Contractor with all terms of this contract, any outstanding balances will be paid within 30 days unless the parties agree otherwise. The completion invoice, and supporting documentation, shall be submitted by the Contractor as promptly as practicable following completion of the work under this contract, but in no event later than 1 year (or such longer period as the Contracting Officer may approve in writing) from the date of completion.

(6) *Release of claim*s. The Contractor, and each assignee under an assignment entered into under this contract and in effect at the time of final payment under this contract, shall execute and deliver, at the time of and as a condition precedent to final payment under this contract, a release discharging the Government, its officers, agents, and employees of and from all liabilities, obligations, and claims arising out of or under this contract, subject only to the following exceptions.

(i) Specified claims in stated amounts, or in estimated amounts if the amounts are not susceptible to exact statement by the Contractor.

(ii) Claims, together with reasonable incidental expenses, based upon the liabilities of the Contractor to third parties arising out of performing this contract, that are not known to the Contractor on the date of the execution of the release, and of which the Contractor gives notice in writing to the Contracting Officer not more than 6 years after the date of the release or the date of any notice to the Contractor that the Government is prepared to make final payment, whichever is earlier.

(iii) Claims for reimbursement of costs (other than expenses of the Contractor by reason of its indemnification of the Government against patent liability), including reasonable incidental expenses, incurred by the Contractor under the terms of this contract relating to patents.

(7) *Prompt payment.* The Government will make payment in accordance with the Prompt Payment Act (31 U.S.C. 3903) and prompt payment regulations at 5 CFR part 1315.

(8) *Electronic Funds Transfer (EFT*). If the Government makes payment by EFT, see 52.212–5(b) for the appropriate EFT clause.

(9) *Discount.* In connection with any discount offered for early payment, time shall be computed from the date of the invoice. For the purpose of computing the discount earned, payment shall be considered to have been made on the date that appears on the payment check or the specified payment date if an electronic funds transfer payment is made.

(l) *Termination for the Government's convenience.* The Government reserves the right to terminate this contract, or any part hereof, for its sole convenience. In the event of such termination, the Contractor shall immediately stop all work hereunder and shall immediately cause any and all of its suppliers and subcontractors to cease work. Subject to the terms of this contract, the Contractor shall be paid an amount for direct labor hours (as defined in the Schedule of the contract) determined by multiplying the number of direct labor hours expended before the effective date of termination by the hourly rate(s) in the contract, less any hourly rate payments already made to the Contractor

plus reasonable charges the Contractor can demonstrate to the satisfaction of the Government using its standard record keeping system that have resulted from the termination. The Contractor shall not be required to comply with the cost accounting standards or contract cost principles for this purpose. This paragraph does not give the Government any right to audit the Contractor's records. The Contractor shall not be paid for any work performed or costs incurred that reasonably could have been avoided.

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DEPARTMENT OF DEFENSE

GENERAL SERVICES ADMINISTRATION

NATIONAL AERONAUTICS AND SPACE ADMINISTRATION

48 CFR Chapter 1

[Docket FAR—2006—0023, Sequence 8]

Federal Acquisition Regulation; Federal Acquisition Circular 2005–15; Small Entity Compliance Guide

AGENCIES: Department of Defense (DoD), General Services Administration (GSA), and National Aeronautics and Space Administration (NASA).

ACTION: Small Entity Compliance Guide.

SUMMARY: This document is issued under the joint authority of the Secretary of Defense, the Administrator of General Services and the Administrator of the National Aeronautics and Space Administration. This Small Entity Compliance Guide has been prepared in accordance with Section 212 of the Small Business Regulatory Enforcement Fairness Act of 1996. It consists of a summary of rules appearing in Federal Acquisition Circular (FAC) 2005–15 which amend the FAR. An asterisk (*) next to a rule indicates that a regulatory flexibility analysis has been prepared. Interested parties may obtain further information regarding these rules by referring to FAC 2005–15 which precedes this document. These documents are also available via the Internet at *http://www.regulations.gov*.

FOR FURTHER INFORMATION CONTACT Laurieann Duarte, FAR Secretariat, (202) 501–4225. For clarification of content, contact the analyst whose name appears in the table below.

LIST OF RULES IN FAC 2005–15

Item	Subject	FAR case	Analyst
*I	Payments Under Time-and-Materials and Labor-Hour Contracts	2004–015	Olson.
*II	Additional Commercial Contract Types	2003–027	Olson.

SUPPLEMENTARY INFORMATION: Summaries for each FAR rule follow. For the actual revisions and/or amendments to these FAR cases, refer to the specific item number and subject set forth in the documents following these item summaries.

FAC 2005–15 amends the FAR as specified below:

Item I—Payments Under Time-and-Materials and Labor-Hour Contracts (FAR Case 2004–015)

This final rule revises and clarifies policies related to award and administration of noncommercial item Time-and-Materials (T&M) and Labor-Hour (LH) contracts and the policies regarding payments made under those contracts. The objectives of the changes are to ensure fair and reasonable prices under T&M and LH contracts and to eliminate confusion related to payment amounts for subcontractor provided labor.

Item II—Additional Commercial Contract Types (FAR Case 2003–027)

This final rule implements section 1432 of the National Defense Authorization Act for Fiscal Year 2004 (Pub. L. 108–136). Title XIV of the Act, referred to as the Services Acquisition Reform Act of 2003 (SARA), amended section 8002(d) of the Federal Acquisition Streamlining Act of 1994 (FASA) (Pub. L. 103–355, 41 U.S.C. 264) to expressly authorize the use of Time–and–Materials (T&M) and Labor–Hour (LH) contracts for commercial services under specified conditions.

Dated: December 4, 2006.

Linda K. Nelson,

Deputy Director, Contract Policy Division.

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