



December 5, 2012

Via Electronic Mail

Office of Federal Procurement Policy
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Room 9013
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ATTN: Raymond J. M. Wong

Subject: Cost Accounting Standards: Revision of the Exemption From Cost Accounting Standards for Contracts and Subcontracts for the Acquisition of Commercial Items, "(b)(6) Commercial Item Exemption"

Mr. Wong:

3M Company welcomes the opportunity to comment on the OFPP's and CAS Board's proposed rule published in the Federal Register on November 19, 2012 to clarify the CAS exemption for contracts and subcontracts for commercial items.

3M is primarily a commercial company. Only a small percentage of its \$29 billion of annual sales is made to the Government. The vast majority of 3M's Government sales are commercial items. 3M holds a small number of relatively small dollar amount FAR-covered Government R&D contracts, which are subject to the FAR Part 31 cost principles and the Truth in Negotiations Act. 3M currently has no Government production contracts for noncommercial items.

Background

In general, there are three steps in determining Cost Accounting Standards (CAS) applicability, coverage, and disclosure requirements. These steps are determining whether (1) the contract or subcontract is subject to the CAS, (2) full CAS-coverage or modified CAS-coverage applies to the contract, and (3) a disclosure statement is required.

The threshold for each of these steps is based on the dollar value of the CAS-covered "award" or "net awards" received by the contractor or subcontractor. A business unit must first receive an award of a negotiated contract for \$7.5 million or more for modified CAS to apply to that contract. Thereafter, each award of a negotiated contract for \$700,000 or more to the same business unit will be subject to modified CAS. Full

CAS-coverage applies to contractor business units that receive either a single CAS-covered award of at least \$50 million or at least \$50 million in net CAS-covered awards during the preceding cost accounting period. 48 CFR § 9903.201-2(a).

A disclosure statement is required if a business unit receives a CAS-covered award of at least \$50 million, or if a company, together with its segments, receives net awards of at least \$50 million in its most recent cost accounting period. 48 CFR § 9903.202-1(b).

The CAS Board regulations do not define "award," but the term is used interchangeably with "CAS-covered contract," which is defined as "any negotiated contract or subcontract in which a CAS clause is required to be included. 48 CFR § 9903.301(a).

The CAS Board regulations define "net awards" as "the total value of negotiated CAS-covered prime contract and subcontract awards, including the potential value of contract options, received during the reporting period minus cancellations, terminations, and other related credit transactions." 48 CFR § 9903.301(a).

Proposed Revision to Commercial Item Exemption at 48 CFR 9903.201-1(b)(6)

In order to clarify the exemption found at 48 CFR 9903.201-1(b)(6) for contracts or subcontracts used for the acquisition of commercial items, the CAS Board proposes changing the wording of the regulatory text in (b)(6) from "[firm fixed-priced, fixed-priced with economic price adjustment (provided that price adjustment is not based on actual costs incurred), time-and-materials, and labor-hour contracts and subcontracts for the acquisition of commercial items]" to read:

"[c]ontracts and subcontracts for the acquisition of commercial items,".

This revision would reflect the statutory text and eliminate from (b)(6) the detailed listing of permissible contract types for the acquisition of commercial items exempted from CAS, as well as the current exception to the list of permissible contract types for the (b)(6) commercial item exemption from CAS for the fixed price economic price adjustment (FPEPA) contract type with the price adjustments based on actual costs incurred.

3M recommends that the proposed revision to (b)(6) not be made. Deleting the more detailed explanation of what is exempt may be confusing to the inexperienced, including both contractors and Government representatives, who do not understand immediately what the cross reference to "contracts and subcontracts for the acquisition of commercial items" means.

Alternatively, the proposed phrase "contracts or subcontracts for the acquisition of commercial items" should be followed by a specific cross reference to a specific statute or regulation for the reader to determine the exempt contract types. Without a specific statutory or regulatory cross reference cited for what that phrase means, a significant potential for confusion will exist.

“Hybrid Contracts” that include Commercial Items and Noncommercial Items

3M strongly recommends that the proposed rule cover “hybrid contracts” that include a CLIN for commercial items and a CLIN for noncommercial items where the total contract amount exceeds a certain CAS threshold, but would not exceed the CAS threshold if the total price of the commercial items is subtracted from the total contract amount. Currently, it is unclear from the regulations whether such hybrid contracts are exempt from CAS because a portion of the contract (a separate CLIN) (hereafter the “Cost Based Portion”) is for noncommercial items and requires submission of cost or pricing data, is subject to the FAR Part 31 cost principles, or provides for payment based on actual incurred costs.

CAS should apply only to the Cost Based Portion of the contract and only if it meets an applicable CAS threshold (i.e., the \$7.5 million trigger award threshold; \$700,000 subsequent award threshold, or \$50 million threshold). Whether modified or full CAS applies to the Cost Based Portion of the contract should depend on whether the \$50 million threshold has been met. In addition, full or modified CAS should not apply to the Cost Based Portion of the contract if another CAS exemption applies.

As an example of a situation that should be addressed in the regulations, assume a firm fixed price contract for \$55 million for commercial items is awarded on a sole source basis. The contract also includes a cost-plus-fixed-fee CLIN for \$4 million to make certain modifications to the commercial items where certified cost or pricing data was provided for that CPFF CLIN. The total amount of the contract is in excess of the \$50 million full CAS threshold. The regulations don’t specify whether the entire contract or just the CPFF CLIN is CAS covered, or whether the entire contract or just the CPFF CLIN is subject to modified or full CAS coverage. The regulations also do not specify whether a CAS disclosure statement is required in this situation.

In situations like the above, the regulations should be revised to clearly specify that the total amount of the hybrid contract should not be used to determine if the contract is CAS-covered. Only the total CPFF amount should be used to determine if the CPFF CLIN is subject to CAS and, if so, whether (1) the CLIN is subject to modified or full CAS coverage, and (2) whether a CAS disclosure statement is required.

An additional example is where a sole source firm fixed price contract for \$60 million is awarded for noncommercial items, which is subject to full CAS coverage. Subsequently, the contract is modified to add a firm fixed price CLIN for \$30 million of commercial items. This increases the total firm fixed price of the contract to \$90 million. The contractor later changes an accounting practice related exclusively to the commercial items, which has no impact on the cost of the noncommercial items. The contractor’s cost of the contract’s commercial items is reduced by \$5 million due to its accounting change. The regulations should be revised to clearly state that, under these types of situations, the Government is not entitled to a price adjustment under the contract’s FAR 52.230-2 CAS clause

In summary, in situations where the Cost Based Portion of a hybrid contract is subject to CAS, the regulations should be revised to make it clear that (1) the commercial item portion of the contract is exempt from CAS-coverage and CAS disclosure statement requirements, and (2) the CAS rules applicable to changes in cost accounting practices apply only to accounting changes that impact the Cost Based Portion of the contract.

ID/IQ “Hybrid Contracts” that include both Commercial Items and Noncommercial Items

FAR 16.504(a) defines an indefinite delivery/indefinite quantity (ID/IQ) contract to mean a contract that provides for an indefinite quantity, within stated limits, of supplies or services to be ordered during a fixed period. The Government places orders for individual requirements. Quantity limits may be stated as number of units or as dollar values.

ID/IQ contracts are not specifically mentioned in any of the CAS standards, CAS Board regulations, or any of the CAS working group items. The issue of CAS coverage with respect to ID/IQ contracts should be addressed in the regulations, since the total actual contract price or total actual amount of the contract is unknown at the time of award. The issue of CAS coverage with respect to ID/IQ “hybrid” contracts should be separately addressed in the regulations, since the total actual contract price or total actual amount of the Cost Based Portion of the contract is unknown at the time of award.

It is virtually impossible to determine the value of an ID/IQ contract at the time of award, particularly with respect to multiple award, ID/IQ contracts. ID/IQ contracts must specify the total minimum and maximum quantity of supplies or services the Government will acquire by the issuance of orders during the term of the contract. FAR 16.504(a)(4). Although the Government is obligated to purchase the specified minimum quantity under an ID/IQ contract, the specified maximum amount need not even be a realistic estimate of the Government’s requirements. This is particularly true with respect to multiple award, ID/IQ contracts. Determining the value of the award for CAS coverage is particularly difficult for multiple-award ID/IQ hybrid contracts, which may have only nominal guaranteed minimum quantities, large maximum dollar amounts, and very little chance that any one (or even all) of the multiple awardees will ever receive task or delivery orders totaling the specified maximum. Determining the value of the award of an ID/IQ contract for CAS coverage is even more difficult if it is a hybrid contract because only the Cost Based Portion of potential task or delivery orders should be considered.

Imposing CAS requirements on ID/IQ contracts, particularly when they are hybrid contracts, based on the specified maximum quantity in the contract, is a significant disincentive for many, if not most, commercial companies to compete for such contracts. For example, if a commercial company with no CAS-covered contracts were to accept a multiple-award ID/IQ “hybrid” contract with a specified minimum of \$50,000 and a maximum of \$60 million, and the maximum quantity was used to determine CAS-coverage, that ID/IQ contract, and all other negotiated contracts or subcontracts worth \$700,000 or more that the commercial company is awarded while “currently

performing" the ID/IQ hybrid contract, would be subject to full CAS-coverage, even though the commercial company is only guaranteed a total of \$50,000 of orders, and may never receive orders totaling more than \$50,000.

In summary the issue of indefinite delivery/indefinite quantity (ID/IQ) contracts, including hybrid contracts, should be addressed in the regulations, since the total actual contract price or total actual amount of the contract is unknown at the time of award. Multiple award ID/IQ contracts, including hybrid contracts, should be separately addressed. Professors Nash and Cibinic recommended that for ID/IQ contracts, the CAS thresholds, i.e., that the "value" of an IDIQ contract, should be determined based on the Government's estimate of what will actually be ordered over the life of the contract, which is a reasonable approach. 7 Nash & Cibinic Rep. 41 (July 1994). With respect CAS thresholds for ID/IQ "hybrid" contracts, the "value" of the ID/IQ contract, should also be determined based on the Government's estimate of what will actually be ordered under cost-based orders issued during the term of the contract.

Until the above questions are resolved in the regulations, they will limit the willingness of many, if not most, commercial companies to sell commercial items to the Government under hybrid contracts.

We appreciate the opportunity to comment on these important regulations.

Sincerely,



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