

DEPARTMENT OF DEFENSE

GENERAL SERVICES
ADMINISTRATIONNATIONAL AERONAUTICS AND
SPACE ADMINISTRATION

48 CFR Parts 32 and 52

[FAR Case 98-400]

RIN 9000-A127

Federal Acquisition Regulation;
Progress Payments and Related
Financing Policies

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

ACTION: Proposed rule.

SUMMARY: The Civilian Agency Acquisition Council and the Defense Acquisition Regulations Council are proposing to amend the Federal Acquisition Regulation (FAR) to reduce the burdens imposed on contractors and contracting officers by the progress payment type of financing; to permit the use of performance-based payments in contracts for research and development, and contracts awarded through competitive negotiation procedures; to expand the use of subcontractor performance-based or commercial financing payments; and to simplify and clarify related provisions.

DATES: Comments should be submitted on or before April 12, 1999 to be considered in the formulation of a final rule.

ADDRESSES: Interested parties should submit written comments to: General Services Administration, FAR Secretariat (MVR), Attn: Laurie Duarte, 1800 F Street, NW, Room 4035, Washington, DC 20405.

E-mail comments submitted over Internet should be addressed to: farcase.98-400@gsa.gov.

Please cite FAR case 98-400 in all correspondence related to this case.

FOR FURTHER INFORMATION CONTACT: For clarification of content, contact Mr. Ralph De Stefano, Procurement Analyst, at (202) 501-1758. Please cite FAR case 98-400. For information on status or publication schedules, contact the FAR Secretariat, Room 4035, GS Building, Washington, DC 20405, (202) 501-4755.

SUPPLEMENTARY INFORMATION:

A. Background

The Director of Defense Procurement at the Department of Defense established a special interagency team

to review existing policies and procedures related to progress payments, to make them easier to understand and to minimize the burdens imposed on contractors and contracting officers. Regulatory requirements pertaining to progress payments that were not required by statute, required to ensure adequately standardized Government business practices, or required to protect the public interest were considered for revision or elimination.

An advance notice of proposed rulemaking (ANPR) was published in the **Federal Register** on May 1, 1997 (62 FR 23740). The ANPR solicited comments from industry and Government personnel on how the FAR could be revised to result in a simplified and streamlined process of applying for and administering progress payments.

After reviewing progress payment policies and public comments received in response to the ANPR, the team identified potential changes to the FAR. A second ANPR was published in the **Federal Register** on March 5, 1998 (63 FR 11074), that solicited comments on the potential changes identified in the notice. The ANPR also announced a public meeting, that was subsequently held on April 23, 1998. After considering written comments received in response to the two notices, and verbal comments provided during the public meeting, the working group submitted a report including a draft proposed rule for consideration by the Defense Acquisition Regulations Council and the Civilian Agency Acquisition Council.

The councils have reviewed the report, and propose the following revisions to the FAR:

1. Increase Thresholds for Contract Financing and Establish a Threshold for Individual Progress Payment Requests

To reduce the administrative burden that small dollar actions place on the contract administration and payment process, the proposed rule:

(a) Raises the dollar threshold at FAR 32.104(d) for use of contract financing with large businesses, from \$1 million to \$2 million. This threshold applies to an individual contract or a group of contracts or orders that total \$2 million or more;

(b) Revises FAR 32.104(d)(2), adds FAR 32.502-4(d), and adds Alternate III to the contract clause at FAR 52.232-16, Progress Payments, to indicate that, in calculating this \$2 million threshold, only those groups of contracts or orders whose individual prices exceed the simplified acquisition threshold will be considered; and

(c) Adds, at FAR 32.503-1 and at FAR 52.232-16, a minimum dollar threshold of \$2,500 for individual progress payment requests, unless a lower amount is authorized in accordance with agency procedures.

2. Elimination of the "Paid Cost Rule"

Currently, a large business is required to pay a subcontractor before including the payment in its progress payment billings to the Government. This is referred to as the "paid cost rule." The proposed FAR rule revises the contract clause at FAR 52.232-16, Progress Payments, to eliminate the "paid cost rule." The revised clause allows a large business to include, in its progress payment billings, subcontract costs that it has incurred but not actually paid, provided the payment to the subcontractor will be made in the ordinary course of business. The proposed rule, likewise, amends the contract clauses at FAR 52.216-7, Allowable Cost and Payment, and at FAR 52.232-7, Payments Under Time-and-Materials and Labor-Hour Contracts, to provide consistent treatment in all payment clauses. This proposed change affects large businesses only. The FAR currently permits a small business concern to include, in its progress payment billings, subcontract costs that it has incurred but not actually paid.

3. Permit Subcontractor Performance-based Payments or Commercial Financing Payments Under Prime Contracts That Have Progress Payments or Cost-reimbursement Type of Financing

The proposed rule amends FAR 32.504 and the contract clause at FAR 52.232-16, Progress Payments, and adds FAR 32.110, to permit prime contractors that receive progress payments or cost-reimbursement type of payments to use performance-based payments or commercial financing payments with their subcontractors, provided the subcontracts that include such payments meet the same criteria and use provisions substantially similar to those in the prime contractor's contract.

4. Elimination of the Limitation on General and Administrative Expenses

The proposed rule removes the limitation at FAR 32.503-7, which applies to only those contractors that have established an inventory suspense account under 48 CFR 9904.410, Allocation of Business Unit General and Administrative Expenses to Final Cost Objectives. This provision dates from 1979 and currently applies to very few remaining contractors.

5. *Elimination of the Contracting Officer Review of Quarterly Statements*

The proposed rule removes the requirement at FAR 32.503-13 for the contractor to submit quarterly statements under price revision or redeterminable contracts. This requirement is unnecessary, as the Government's interests are protected adequately by the contracting officer that has the responsibility for administering progress payments.

6. *Permit the Use of Performance-based Payments in Contracts for Research and Development, and in Contracts Awarded Through Competitive Negotiation Procedures*

The proposed rule amends FAR 32.1000 by removing the prohibition against using performance-based payments type of financing in contracts for research and development and contracts awarded through competitive negotiation procedures. In addition, the rule adds a new subsection at FAR 32.1004-2 and a new solicitation provision at FAR 52.232-XX, Invitation to Propose Performance-Based Payments, for use in competitive solicitations when offerors are invited to propose performance-based payments.

However, the prohibition against using performance-based type of financing in contracts awarded using sealed bid procedures remains in FAR 32.1000. The evaluation process necessitates discussions when performance-based payments are proposed to ensure the payment events and payment amounts are reasonable, credible, and consistent with all other aspects of the offeror's proposal. Since sealed bid procedures are used when it is not necessary to conduct discussions with the responding offerors about their bids, sealed bid procedures cannot accommodate performance-based payments.

7. *Ensure Consideration of Performance-based Payments*

The proposed rule revises FAR 32.502-1 and 32.1004 to emphasize that performance-based payments are the preferred method of financing; their use should be considered and deemed impracticable by the contracting officer before a decision is made to provide customary progress payments; and each payment amount should represent what the contractor could reasonably be expected to incur to achieve the payment event rather than resemble an advance payment or a reward to the contractor for achieving performance levels over and above what is required

for successful completion of the contract.

8. *Other Changes*

The proposed rule also revises FAR 32.503-6(f) to simplify and clarify that, on a loss contract, application of the loss ratio constitutes the adjustment that ensures progress payments do not exceed the value of work performed; amends FAR 32.501-1(a) to delete the authorization for the Department of Defense to establish customary progress payment rates for foreign military sales (FMS) and flexible progress payments that differ from the customary rates cited in the same paragraph (DoD no longer uses flexible progress payments and does not intend to establish alternate rates for FMS); and makes related editorial changes.

This regulatory action was not subject to Office of Management and Budget review under Executive Order 12866, dated September 30, 1993, and is not a major rule under 5 U.S.C. 804.

B. *Regulatory Flexibility Act*

This proposed rule is not expected to have a significant economic impact on a substantial number of small entities within the meaning of the Regulatory Flexibility Act, 5 U.S.C. 601, *et seq.*, because most contracts awarded to small entities have a dollar value less than the simplified acquisition threshold, and, therefore, do not require the progress payment or performance-based payment type of financing. Therefore, an Initial Regulatory Flexibility Analysis has not been performed. Comments are invited from small businesses and other interested parties. Comments from small entities concerning the affected FAR subparts also will be considered in accordance with 5 U.S.C. 610. Such comments must be submitted separately and should cite FAR Case 98-400 in correspondence.

C. *Paperwork Reduction Act*

The Paperwork Reduction Act (44 U.S.C. 3501, *et seq.*) is deemed to apply because the proposed rule contains information collection requirements.

1. *Office of Management and Budget (OMB) Control Number 9000-0010 (Progress Payments)*

The proposed rule decreases the collection requirements currently approved under OMB/Control Number 9000-0010, since the rule raises the threshold for permitting contract financing in the form of customary progress payments, and establishes a dollar threshold for contractor requests for progress payments. The estimated number of respondents per year:

reduced from 27,000 to 18,090; yearly responses per respondent: 32 (unchanged); average per response: 33 minutes (unchanged); total yearly burden hours: from 475,000 to 318,384; frequency: as required. Accordingly, a request for amendment of information collection requirements will be submitted to OMB at the final rule stage.

2. *OMB Control Number 9000-0138 (Contract Financing)*

There is no net impact to the collection requirements currently approved under OMB Control Number 9000-0138. The increase in hours resulting from adding the provision at 52.232-XX, Invitation to Propose Performance-Based Payments, in competitive solicitations when the performance-based payment method of contract financing is used, is offset by the decrease in hours resulting from raising the contract dollar threshold for permitting performance-based payments.

D. *Request for Comments Regarding Paperwork Burden*

Members of the public are invited to comment on the recordkeeping and information collection requirements and estimates set forth above. Please send comments to: Office of Information and Regulatory Affairs, Office of Management and Budget, Attention: Mr. Peter N. Weiss, FAR Desk Officer, New Executive Office Building, Room 10102, 725 17th Street, NW, Washington, DC 20503.

Also send a copy of any comments to the FAR Secretariat at the address shown under ADDRESSES. Please cite the corresponding OMB clearance numbers in all correspondence related to the estimate.

List of Subjects in 48 CFR Parts 32 and 52

Government procurement.

Dated: February 4, 1999.

Edward C. Loeb,

Director, Federal Acquisition Policy Division.

Therefore, it is proposed that 48 CFR Parts 32 and 52 be amended as set forth below:

1. The authority citation for 48 CFR Parts 32 and 52 continues to read as follows:

Authority: 40 U.S.C. 486(c); 10 U.S.C. chapter 137; and 42 U.S.C. 2473(c).

PART 32—CONTRACT FINANCING

2. Section 32.104 is revised to read as follows:

32.104 Providing contract financing.

(a) Prudent contract financing can be a useful working tool in Government acquisition by expediting the performance of essential contracts. Government financing shall be provided only to the extent actually needed for prompt and efficient performance, considering the availability of private financing and the probable impact on working capital of the pre-delivery expenditures and production lead times associated with the contract or groups of contracts or orders (e.g., indefinite-delivery contracts, basic ordering agreements, or their equivalent). Contract financing shall be administered so as to aid, not impede, the acquisition. At the same time, the contracting officer shall avoid any undue risk of monetary loss to the Government through the financing. Include the form of contract financing deemed to be in the Government's best interest in the solicitation (see 32.106 and 32.113). The contractor's use of the contract financing provided and the contractor's financial status shall be monitored.

(b) If the contractor is a small business concern, the contracting officer shall give special attention to meeting the contractor's contract financing need. However, a contractor's receipt of a certificate of competency from the Small Business Administration has no bearing on the contractor's need for or entitlement to contract financing.

(c) Subject to specific agency regulations and paragraph (d) of this section, the contracting officer may provide customary contract financing in accordance with 32.113. Unusual contract financing shall not be provided except as authorized in 32.114.

(d) The contracting officer may provide contract financing in the form of performance-based payments (see 32.10) or customary progress payments (see 32.5)—

(1) For individual contracts when the contract price is \$2 million or more (or for small business concerns, when the contract price exceeds the simplified acquisition threshold) if the contractor—

(i) Will not be able to bill for the first delivery of products for a substantial time after work must begin (normally 4 months or more for small business concerns, and 6 months or more for others), and will make expenditures for contract performance during the pre-delivery period that have a significant impact on the contractor's working capital; or

(ii) Demonstrates actual financial need or the unavailability of private financing.

(2) For a group of contracts or orders that total \$2 million or more. In calculating this threshold, only those contracts or orders whose prices exceed the simplified acquisition threshold will be considered.

3. Section 32.106 is amended by revising paragraph (b) to read as follows:

32.106 Order of preference.

* * * * *

(b) Customary contract financing other than loan guarantees and certain advance payments (see 32.113).

* * * * *

4. Section 32.110 is added to read as follows:

32.110 Payment of subcontractors under cost-reimbursement prime contracts.

If the contractor makes financing payments to a subcontractor under a cost-reimbursement prime contract, the contracting officer shall accept the financing payments as reimbursable costs of the prime contract only under the following conditions—

(a) The payments are made under the criteria in subpart 32.5 for customary progress payments based on costs, 32.202–1 for commercial item purchase financing, or 32.1003 for performance-based payments, as applicable.

(b) If customary progress payments are made, the payments do not exceed the progress payment rate in 32.501–1, unless unusual progress payments to the subcontractor have been approved in accordance with 32.501–2.

(c) If customary progress payments are made, the subcontractor complies with the liquidation principles of 32.503–8, 32.503–9, and 32.503–10.

(d) If performance-based payments are made, the subcontractor complies with the liquidation principles of 32.1004–1(d).

(e) The subcontract contains financing payments terms as prescribed in this section.

5. Section 32.112 is amended by revising the section heading to read as follows:

32.112 Nonpayment of subcontractors under contracts for non-commercial items.

* * * * *

6. Section 32.113 is amended by revising paragraph (c); redesignating paragraphs (d) through (g) as (e) through (h), respectively; and adding a new paragraph (d) to read as follows:

32.113 Customary contract financing.

* * * * *

(c) Financing of contracts for supplies or services awarded under the sealed bid method of procurement in accordance with part 14 through

progress payments based on costs in accordance with subpart 32.5;

(d) Financing of contracts for supplies or services awarded under the competitive negotiation method of procurement in accordance with part 15, through either progress payments based on costs in accordance with subpart 32.5, or performance-based payments in accordance with subpart 32.10 (but not both);

* * * * *

7. Section 32.205 is amended by revising the first sentence of paragraph (c)(4) to read as follows:

32.205 Procedures for offeror-proposed commercial contract financing.

* * * * *

(c) * * *

(4) The time value of proposal-specified contract financing arrangements shall be calculated using as the interest rate the Nominal Discount Rate specified in Appendix C of the Office of Management and Budget (OMB) Circular A–94, "Guidelines and Discount Rates for Benefit-Cost Analysis of Federal Programs", appropriate to the period of contract financing. * * *

8. Section 32.500 is amended by revising paragraph (a) to read as follows:

32.500 Scope of subpart.

* * * * *

(a) Payments under cost-reimbursement contracts, but see 32.110 for progress payments made to subcontractors under cost-reimbursement prime contracts; or

* * * * *

9. Section 32.501–1 is amended in paragraph (a) by removing the last sentence; and in paragraph (d) by revising the first sentence to read as follows:

32.501–1 Customary progress payment rates.

* * * * *

(d) In accordance with 10 U.S.C. 2307(e)(2) and 41 U.S.C. 255, progress payments are limited to 80 percent on work accomplished under undefinitized contract actions. * * *

10. Section 32.502–1 is revised to read as follows:

32.502–1 Use of customary progress payments.

When the criteria for the use of performance-based payments are not met (see 32.1001(a) and 32.1003), the use of a progress payments clause in solicitations and resulting contracts may be considered in accordance with this subpart. Bids conditioned on progress payments when the solicitation did not provide for progress payments shall be rejected as nonresponsive.

11. Section 32.502-4 is amended by redesignating paragraph (d) as (e) and adding a new paragraph (d) to read as follows:

32.502-4 Contract clauses.

* * * * *

(d) If progress payments are authorized under an indefinite-delivery contract, the contracting officer shall use the clause with its Alternate III to make progress payments applicable only to orders that exceed the simplified acquisition threshold.

* * * * *

12. Section 32.503-1 is amended at the end of paragraph (b) by removing “and”; in paragraph (c) by removing the period and adding “; and”; and adding paragraph (d) to read as follows:

32.503-1 Contractor requests.

* * * * *

(d) Be \$2,500 or more, unless a lower amount is authorized in accordance with agency procedures.

13. Section 32.503-5 is amended by revising paragraph (c) to read as follows:

32.503-5 Administration of progress payments.

* * * * *

(c) Progress payments made under indefinite-delivery contracts should be administered under each individual order as if the order constituted a separate contract, unless agency procedures provide otherwise.

14. Section 32.503-6 is amended by revising paragraphs (f) and (g)(4) to read as follows:

32.503-6 Suspension or reduction of payments.

* * * * *

(f) *Fair value of undelivered work.* Progress payments must be commensurate with the fair value of work accomplished in accordance with contract requirements. Governed by the principles of paragraphs (c) and (e) of this section, the contracting officer shall adjust progress payments when necessary to ensure that the fair value of undelivered work equals or exceeds the amount of unliquidated progress payments. On loss contracts, the application of a loss ratio as described in paragraph (g) of this section constitutes this adjustment.

(g) * * *

(4) The following is an example of the supplementary analysis required in paragraph (g)(3) of this section:

Section I	
Contract price	\$2,850,000
Change orders and unpriced orders (to extent funds have been obligated)	150,000
Revised contract price	3,000,000
Section II	
Total costs incurred to date	2,700,000
Estimated additional costs to complete	900,000
Total costs to complete	3,600,000
Loss ratio factor $\$3,000,000 \div \$3,600,000 = 83.3\%$	
Total costs eligible for progress payments	2,700,000
Loss ratio factor	$\times 83.3\%$
Recognized costs for progress payments	2,249,100
Progress payment rate	$\times 80.0\%$
Alternate amount to be used	1,799,280
Section III	
Factored costs of items delivered*	750,000
Recognized costs applicable to undelivered items $\$2,249,100 - \$750,000$	1,499,100

* This amount shall be the same as the contract price of the items delivered.

32.503-7 [Reserved]

15. Section 32.503-7 is removed and reserved.

16. Section 32.503-8 is revised to read as follows:

32.503-8 Liquidation rates—ordinary method.

Progress payments are recouped by the Government through the deduction of liquidations from payments that would otherwise be due to the contractor for completed contract items. To determine the amount of the liquidation, a liquidation rate is applied to the contract price of contract items delivered and accepted. The ordinary method is that the liquidation rate is the same as the progress payment rate; at the beginning of a contract, only this method may be used.

17. Section 32.503-10 is amended by revising paragraphs (b)(1) and (b)(3) to read as follows:

32.503-10 Establishing alternate liquidation rates.

* * * * *

(b) * * *

(1) The contracting officer shall compute the expected progress payments by multiplying the estimated cost of performing the contract by the progress payment rate.

* * * * *

(3) The following are examples of the computation. Assuming an estimated price of \$2,200,000 and total estimated costs eligible for progress payments of \$2,000,000:

(i) If the progress payment rate is 80 percent, the minimum liquidation rate should be 72.7 percent, computed as follows:

$$\frac{\$2,000,000 \times 80\%}{\$2,200,000} = 72.7\%$$

(ii) If the progress payment rate is 85 percent, the minimum liquidation rate

should be 77.3 percent, computed as follows:

$$\frac{\$2,000,000 \times 85\%}{\$2,200,000} = 77.3\%$$

* * * * *

32.503-13 [Reserved]

18. Section 32.503-13 is removed and reserved.

19. Section 32.504 is amended by revising the section heading and paragraphs (a) and (b); in the second sentence of paragraph (c) by revising “(j)(4)” to read “(j)(6)”; in the first sentence of paragraph (d) by removing “progress” and adding “financing”, and by revising the second sentence; in the introductory text of paragraph (e) by revising the first sentence; by revising paragraph (f); and by adding paragraph (g) to read as follows:

32.504 Subcontracts under prime contracts providing progress payments.

(a) Subcontracts may include either performance-based payments, provided they meet the criteria in 32.1003, or progress payments on terms that meet the criteria in subpart 32.5 for customary progress payments, but not both. Subcontracts for commercial purchases may include commercial item purchase financing terms, provided they meet the criteria in 32.202–1.

(b) The contractor's requests for progress payments may include the full amount of commercial item purchase financing payments, performance-based payments, or progress payments to subcontractors, whether paid, or approved for current payment in the ordinary course of business, under the contract and subcontracts.

* * * * *

(d) * * * Although the contracting officer should, to the extent appropriate, review the subcontract as part of the overall administration of progress payments in the prime contract, there is no special requirement for contracting officer review or consent merely because the subcontract includes financing payments, except as provided in paragraph (c) of this section. * * *

(e) When financing payments are in the form of progress payments, the subcontract terms shall include the substance of the Progress Payments clause in the prime contract, modified to indicate that the contractor, not the Government, awards the subcontract and administers the progress payments.

* * * * *

(f) When financing payments are in the form of performance-based payments, the subcontract terms shall include the substance of the Performance-Based Payments clause at 52.232–32, modified to indicate that the contractor, not the Government, awards the subcontract and administers the performance-based payments, and include appropriate wording modifications similar to those noted in paragraph (e) of this section.

(g) When financing payments are in the form of commercial item purchase financing, the subcontract shall include a contract financing clause structured in accordance with 32.206.

20. Section 32.1000 is amended at the end of paragraph (b) by adding “or” after the semicolon; removing paragraph (c) and redesignating paragraph (d) as (c), respectively; and revising newly designated (c) to read as follows:

32.1000 Scope of subpart.

* * * * *

(c) Contracts awarded through sealed bid procedures.

21. Section 32.1001 is amended by removing paragraph (e), redesignating paragraphs (a) through (d) as (b) through (e), respectively, and adding a new paragraph (a).

The added text reads as follows:

32.1001 Policy.

(a) Performance-based payments are the preferred financing method when the contracting officer finds them practical, and the contractor agrees to their use.

* * * * *

32.1004 [Amended] [Text redesignated as 32.1004–1]

22. Section 32.1004 is amended by revising the section heading to read as set forth below; and the text is redesignated as 32.1004–1 and revised. The revisions read as follows:

32.1004 Procedures.**32.1004–1 General.**

Performance-based payments may be made either on a whole contract or on a deliverable item basis, unless otherwise prescribed by agency regulations. Financing payments to be made on a whole contract basis are applicable to the entire contract, and not to specific deliverable items. Financing payments to be made on a deliverable item basis are applicable to a specific individual deliverable item. (A deliverable item for these purposes is a separate item with a distinct unit price. Thus, a contract line item for 10 airplanes, with a unit price of \$1,000,000 each, has ten deliverable items—the separate planes. A contract line item for 1 lot of 10 airplanes, with a lot price of \$10,000,000, has only one deliverable item—the lot.)

(a) Establishing performance bases.

(1) The basis for performance-based payments may be either specifically described events (e.g., milestones) or some measurable criterion of performance. Each event or performance criterion that will trigger a finance payment shall be an integral and necessary part of contract performance and shall be identified in the contract, along with a description of what constitutes successful performance of the event or attainment of the performance criterion. The signing of contracts or modifications, the exercise of options, or other such actions shall not be events or criteria for performance-based payments. An event need not be a critical event in order to trigger a payment, but successful performance of each such event or performance criterion shall be readily verifiable.

(2) Events or criteria may be either severable or cumulative. The successful completion of a severable event or criterion is independent of the accomplishment of any other event or criterion. Conversely, the successful accomplishment of a cumulative event or criterion is dependent upon the previous accomplishment of another event. A contract may provide for more than one series of severable and/or cumulative performance events or criteria performed in parallel. The following shall be included in the contract:

(i) The contract shall not permit payment for a cumulative event or criterion until the dependent event or criterion has been successfully completed.

(ii) Severable events or criteria shall be specifically identified in the contract.

(iii) The contract shall identify which events or criteria are preconditions for the successful achievement of each cumulative event or criterion.

(iv) Because performance-based payments are contract financing, events or criteria shall not serve as a vehicle to reward the contractor for completion of performance levels over and above what is required for successful completion of the contract.

(v) If payment of performance-based finance amounts is on a deliverable item basis, each event or performance criterion shall be part of the performance necessary for that deliverable item and shall be identified to a specific contract line item or subline item.

(b) *Establishing performance-based finance payment amounts.* (1) The contracting officer shall establish a complete, fully defined schedule of events or performance criteria and payment amounts when negotiating contract terms. If a contract action significantly affects the price, or event or performance criterion, the contracting officer responsible for pricing the contract modification shall adjust the performance-based payment schedule appropriately.

(2) Total performance-based payments shall—

(i) Reflect prudent contract financing provided only to the extent needed for contract performance (see 32.104(a)); and

(ii) Not exceed 90 percent of the contract price if on a whole contract basis, or 90 percent of the delivery item price if on a delivery item basis.

(3) The amount of each performance-based payment shall be specifically stated either as a dollar amount or as a percentage of a specifically identified price (e.g., contract price, or unit price

of the deliverable item). The payment of contract financing has a cost to the Government in terms of interest paid by the Treasury to borrow funds to make the payment. Because the contracting officer has wide discretion as to the timing and amount of the performance-based payments, the contracting officer shall ensure that—

(i) The total contract price is fair and reasonable, all factors (including the financing costs to the Treasury of the performance-based payments) considered; and

(ii) Performance-based payment amounts are commensurate with the value of the performance event or performance criterion, and will not result in an unreasonably low or negative level of contractor investment in the contract. Accordingly, contracting officers shall require that contractor proposals for performance-based payments include a profile showing projected cash flow and contractor investment in the contract.

(4) Performance-based payment amounts may be established on any rational basis determined by the contracting officer, or agency procedures, which may include (but are not limited to)—

(i) Engineering estimates of stages of completion;

(ii) Engineering estimates of hours or other measures of effort to be expended in performance of an event or achievement of a performance criterion; or

(iii) The estimated projected cost of performance of particular events.

(5) When subsequent contract modifications are issued, the performance-based payment schedule shall be adjusted as necessary to reflect the actions required by those contract modifications.

(c) *Instructions for multiple appropriations.* If there is more than one appropriation account (or subaccount) funding payments on the contract, the contracting officer shall provide instructions to the Government payment office for distribution of financing payments to the respective funds accounts. Distribution instructions must be consistent with the contract's liquidation provisions.

(d) *Liquidating performance-based finance payments.* Performance-based amounts shall be liquidated by deducting a percentage or a designated dollar amount from the delivery payments. The contracting officer shall specify the liquidation rate or designated dollar amount in the contract. The method of liquidation shall ensure complete liquidation no later than final payment.

(1) If the performance-based payments are established on a delivery item basis, the liquidation amount for each line item shall be the percent of that delivery item price that was previously paid under performance-based finance payments or the designated dollar amount.

(2) If the performance-based finance payments are on a whole contract basis, liquidation shall be by predesignated liquidation amounts or liquidation percentages.

23. Section 32.1004-2 is added to read as follows:

32.1004-2 Procedures for evaluating offeror-proposed performance-based payments for competitive solicitations.

Use the following procedures when offerors are invited to propose performance-based payments:

(a) *Solicitations.* The contracting officer shall specify, in section M of the solicitation, the interest rate to be used in the evaluation of financing proposals (see paragraph (b)(4) of this section).

(b) *Evaluation of proposals.* (1) Since performance-based payment terms will vary among offerors, the contracting officer shall—

(i) Review the proposed terms to ensure they comply with 32.1004-1; and

(ii) Adjust each proposed price for evaluation purposes to reflect the cost of providing the proposed performance-based payments to determine the total cost to the Government of that particular combination of price and performance-based financing.

(2) The Government makes payments earlier when using the performance-based payments type of financing than it would if payments were not made until deliveries are accepted. In order to determine the cost to the Government of making payments earlier, the contracting officer shall compute the imputed cost of those performance-based payments and add it to the proposed price to determine the evaluated price for each offeror.

(3) The imputed cost of a single performance-based financing payment is the amount of the payment multiplied by the annual interest rate, multiplied by the number of years, including fraction thereof, between the projected performance-based payment (invoice) date and the date the amount would have been paid as a delivery payment. The imputed cost of financing is the sum of the imputed costs of each of the performance-based financing payments.

(4) The time value of offeror-proposed contract financing arrangements shall be calculated using as the interest rate the nominal discount rate specified in

Appendix C of the Office of Management and Budget (OMB) Circular A-94, "Guidelines and Discount Rates for Benefit-Cost Analysis of Federal Programs", appropriate to the period of contract financing. Where the period of proposed financing does not match the periods in the OMB Circular, the interest rate for the period closest to the finance period shall be used. Appendix C is updated yearly, and is available from the Office of Economic Policy in OMB.

24. Section 32.1005 is amended by revising the section heading and paragraph (a) to read as follows:

32.1005 Solicitation provision and contract clauses.

(a) If the contracting officer anticipates that performance-based contract financing may be provided in accordance with 32.1001, the contracting officer shall insert the clause at 52.232-32, Performance-Based Payments, in the solicitation and contract with the description of the basis for payment and liquidation as required in 32.1004. Additionally, if the procedures at 32.1004-2 are used for competitive solicitations, the solicitation provision at 52.232-XX, Invitation to Propose Performance-Based Payments, shall be included.

* * * * *

32.1006 [Removed and Reserved]

25. Section 32.1006 is removed and reserved.

PART 52—SOLICITATION PROVISIONS AND CONTRACT CLAUSES

26. Section 52.216-7 is amended by revising the date of the clause; by redesignating paragraphs (b)(1)(ii)(A) through (b)(1)(ii)(E) as (b)(1)(ii)(B) through (b)(1)(ii)(F), adding a new (b)(1)(ii)(A), and revising (b)(1)(iii), (b)(2), and (c) to read as follows:

52.216-7 Allowable Cost and Payment.

* * * * *

Allowable Cost and Payment (Date)

* * * * *

(b) * * *

(1) * * *

(ii) * * *

(A) Supplies and services purchased directly for the contract;

* * * * *

(iii) The amount of progress and other payments that have been paid by cash, check or other form of payment, or approved for current payment in the ordinary course of business, to the Contractor's subcontractors under similar cost standards.

(2) Accrued costs of Contractor contributions under employee pension plans shall be excluded until actually paid unless—

(i) The Contractor's practice is to make contributions to the retirement fund quarterly or more frequently; and

(ii) The contribution does not remain unpaid 30 days after the end of the applicable quarter or shorter payment period (any contribution remaining unpaid shall be excluded from the Contractor's indirect costs for payment purposes).

* * * * *

(c) *Small business concerns.* A small business concern may be paid more often than every 2 weeks.

* * * * *

27. Section 52.232-7 is amended by revising the date of the clause, the fourth sentence of paragraph (b)(1) and the second sentence of paragraph (b)(2) to read as follows:

52.232-7 Payments Under Time-and-Materials and Labor-Hour Contracts.

* * * * *

Payments Under Time-and-Materials and Labor-Hour Contracts (Date)

* * * * *

(b) *Materials and subcontractors.* (1) * * * The Contractor shall be reimbursed for items and services purchased directly for the contract only when payments of cash, checks, or other forms of actual payment have been made, or have been approved for current payment in the ordinary course of business, for such purchased items or services, provided the Contractor is not delinquent in paying such costs in the ordinary course of business. * * *

(2) * * * Reimbursable costs in connection with subcontracts shall be limited to the amounts paid to the subcontractor for items and services purchased directly for the contract only when payments of cash, checks, or other forms of actual payment have been made, or have been approved for current payment in the ordinary course of business, for such purchased items or services, provided the Contractor is not delinquent in paying such costs in the ordinary course of business. * * *

* * * * *

28. Section 52.232-16 is amended—

a. In paragraph (b) of the introductory text by removing “paragraph (a)(1)” and adding “paragraphs (a)(1), (a)(5), and (b)”;

b. In paragraph (c) of the introductory text by revising “(a)(4)” to read “(a)(1)”;

c. By removing paragraph (d) of the introductory text, and redesignating paragraph “(e)” as “(d)”;

d. In newly redesignated paragraph (d) by revising “(see 32.504(b))” to read “(see 32.504(c))”; and by revising “subparagraph (j)(4)” to read “subparagraph (j)(6)”;

e. By revising the date of the clause;

f. In the introductory text of the clause by adding “of \$2,500 or more” after “amounts”;

g. By revising paragraphs (a)(1) and (a)(2) of the clause, and adding a new paragraph (a)(7);

h. By revising paragraph (j) of the clause;

i. By revising Alternate I and adding Alternate III to read as follows:

52.232-16 Progress Payments.

* * * * *

Progress Payments (Date)

* * * * *

(a) *Computation of amounts.* (1) Unless the Contractor requests a smaller amount, each progress payment shall be computed as 80 percent of the Contractor's total costs incurred under this contract whether or not actually paid, plus financing payments to subcontractors (see paragraph (j) of this clause), less the sum of all previous progress payments made by the Government under this contract. Cost of money that would be allowable under 31.205-10 of the Federal Acquisition Regulation shall be deemed an incurred cost for progress payment purposes.

(2) Accrued costs of Contractor contributions under employee pension plans shall be excluded until actually paid unless—

(i) The Contractor's practice is to make contributions to the retirement fund quarterly or more frequently; and

(ii) The contribution does not remain unpaid 30 days after the end of the applicable quarter or shorter payment period (any contribution remaining unpaid shall be excluded from the Contractor's total costs for progress payments until paid).

* * * * *

(7) Notwithstanding any other terms of the contract, the Contractor agrees not to request progress payments in dollar amounts of less than \$2,500. Exceptions may be made by the Contracting Officer.

* * * * *

(j) *Financing payments to subcontractors.* The amounts mentioned in paragraph (a)(1) of this clause shall be all financing payments to subcontractors or divisions, if the following conditions are met:

(1) The amounts included are limited to—

(i) The unliquidated remainder of financing payments made; plus

(ii) Any unpaid subcontractor requests for financing payments that the Contractor has approved for current payment in the ordinary course of business.

(2) The subcontract or interdivisional order is expected to involve a minimum of approximately 6 months between the beginning of work and the first delivery; or, if the subcontractor is a small business concern, 4 months.

(3) If the financing payments are in the form of progress payments, the terms of the subcontract or interdivisional order concerning progress payments—

(i) Are substantially similar to the terms of the clause at 52.232-16, Progress Payments;

(ii) Are at least as favorable to the Government as the terms of this clause;

(iii) Are not more favorable to the subcontractor or division than the terms of this clause are to the Contractor;

(iv) Are in conformance with the requirements of 32.504(e) of the Federal Acquisition Regulation; and

(v) Subordinate all subcontractor rights concerning property to which the Government has title under the subcontract to the Government's right to require delivery of the property to the Government if—

(A) The Contractor defaults; or

(B) The subcontractor becomes bankrupt or insolvent.

(4) If the financing payments are in the form of performance-based payments, the terms of the subcontract or interdivisional order concerning payments—

(i) Are substantially similar to the Performance-Based Payments clause at 52.232-32 and meet the criteria for, and definition of, performance-based payments in part 32 of the Federal Acquisition Regulation;

(ii) Are in conformance with the requirements of 32.504(f) of the Federal Acquisition Regulation; and

(iii) Subordinate all subcontractor rights concerning property to which the Government has title under the subcontract to the Government's right to require delivery of the property to the Government if—

(A) The Contractor defaults; or

(B) The subcontractor becomes bankrupt or insolvent.

(5) If the financing payments are in the form of commercial item financing payments, the terms of the subcontract or interdivisional order concerning payments—

(i) Are constructed in accordance with 32.206(c) of the FAR and included in a subcontract for a commercial item purchase that meets the definition and standards for acquisition of commercial items in parts 2 and 12 of the Federal Acquisition Regulation;

(ii) Are in conformance with the requirements of 32.504(g) of the Federal Acquisition Regulation; and

(iii) Subordinate all subcontractor rights concerning property to which the Government has title under the subcontract to the Government's right to require delivery of the property to the Government if—

(A) The Contractor defaults; or

(B) The subcontractor becomes bankrupt or insolvent.

(6) If financing is in the form of progress payments, the progress payment rate in the subcontract is the customary rate used by the Contracting Agency, depending on whether the subcontractor is or is not a small business concern.

(7) The parties agree concerning any proceeds received by the Government for property to which title has vested in the Government under the subcontract terms, that the proceeds shall be applied to reducing any unliquidated financing payments by the Government to the Contractor under this contract.

(8) If no unliquidated financing payments to the Contractor remain, but there are unliquidated financing payments that the Contractor has made to any subcontractor, the Contractor shall be subrogated to all the rights the Government obtained through the terms required by this clause to be in any subcontract, as if all such rights had been assigned and transferred to the Contractor.

(9) The Contractor shall pay the subcontractor's financing payment request under paragraphs (j)(1) through (5) of this clause, within a reasonable time after

receiving the Government progress payment covering those amounts.

(10) To facilitate small business participation in subcontracting under this contract, the Contractor agrees to provide financing payments to small business concerns, in conformity with the standards for customary contract financing payments stated in 32.113 of the Federal Acquisition Regulation. The Contractor further agrees that the need for such financing payments shall not be considered as a handicap or adverse factor in the award of subcontracts.

* * * * *

Alternate I (Date). If the contract is with a small business concern, change each mention of the progress payment and liquidation rates excepting paragraph (k) to the customary rate of 85 percent for small business concerns (see 32.501-1).

* * * * *

Alternate III (Date). As prescribed in 32.502-4(d), add the following paragraph (l) to the basic clause. If Alternate II is also being used, redesignate the following paragraph as paragraph (n):

(l) The provisions of this clause shall not be applicable to individual orders at or below the simplified acquisition threshold.

29. Section 52.232-XX is added to read as follows:

52.232-XX Invitation to Propose Performance-Based Payments.

As prescribed in 32.1005, insert the following provision:

Invitation to Propose Performance-Based Payments (Date)

(a) The offeror is invited to propose terms under which the Government shall make performance-based contract financing payments during contract performance. The performance-based payment financing terms proposed by the offeror shall be a factor in the evaluation of the offeror's proposal. The financing terms of the successful offeror and the FAR clause at 52.232-32, Performance-Based Payments, shall be incorporated in any resulting contract.

(b) The offeror agrees that in the event of any conflict between the terms proposed by the offeror and the terms in the FAR clause at 52.232-32, Performance-Based Payments, the terms of the clause at 52.232-32 shall govern.

(c) The offeror's proposed performance-based payment financing shall not be acceptable if it does not conform to the following limitations:

(1) Delivery payments shall be made only for supplies delivered and accepted, or services rendered and accepted in accordance with the payment terms of this contract.

(2) The terms and conditions of the performance-based payments must comply with FAR 32.1004-1, be reasonable and consistent with all other technical and cost information included in the offeror's proposal, and their total shall not exceed 90 percent of the contract price if on a whole contract basis, or 90 percent of the delivery item price if on a delivery item basis.

(3) The terms and conditions of the performance-based financing must be in the best interests of the United States.

(d) The offeror's proposal of performance-based payment financing shall include the following:

(1) The proposed contractual language describing the performance-based payments (see FAR 32.1004-1 for appropriate criteria for establishing performance bases and performance-based finance payment amounts).

(2) A listing of—

(i) The projected performance-based payment dates and the projected payment amounts; and

(ii) The projected delivery date and the projected payment amount.

(3) A profile showing projected cash flow and contractor investment in the contract.

(e) Evaluation of the offeror's proposed prices and financing terms shall include the following—

(1) Whether the offeror's proposed performance-based payment events and payment amounts are reasonable and consistent with all other terms and conditions of the offeror's proposal.

(2) The cost to the United States of the proposal using the interest rate and delivery schedule specified elsewhere in this solicitation.

(End of provision)

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