



Government Contracts Advisory

October 15, 2010

New Proposed Rule for Time-and-Materials and Labor-Hour Contracts

The Civilian Agency Acquisition Council and the Defense Acquisition Regulations Council (Councils) propose to amend the FAR in an effort to ensure that agencies better understand the risks associated with time-and-materials and labor-hour contracts (T&M contracts) and follow certain safeguards regarding these types of contracts. 75 Fed. Reg. 59195, 59195, Sept. 27, 2010. The proposal comes as a response to the GAO's findings and recommendations in a June 2009 report on "Minimal Compliance with New Safeguards for Time-and-Materials Contracts for Commercial Services and Safeguards Have Not Been Applied to GSA Schedules Program." *Id.* In the report, GAO found that when purchasing off the GSA schedules program, many agencies mistakenly believed that fixed labor rates on T&M contracts made them fixed price type contracts, were not ensuring that T&M contracts are used only when no other contract type is appropriate, and failed to prepare required justifications for their use. *Id.* at 59196. Accordingly, the Councils propose to amend the FAR to further clarify and ensure that agencies follow the appropriate procedures when using T&M contracts. While purchasing practices for commercial services in GSA's federal supply schedules program were the focus of the GAO report, the proposed rule makes changes regarding T&M contracting generally to address GAO's concerns.

Under T&M contracts, the government pays contractors based on a fixed hourly labor rate as well as the cost of any materials used. Because the final price of a T&M contract is tied to the actual hours a contractor works, the government considers T&M contracts risky. Accordingly, a T&M contract is only supposed to be used when no other type of contract is suitable. In addition, existing regulations require a determination and findings (D&F) to justify its use, including market research and acquisition planning analysis, and discussion of how the agency will maximize the use of fixed-price contracts on future acquisitions. In addition, the agency must justify any subsequent changes to the ceiling price of a T&M contract. The GAO found that GSA schedule T&M purchases frequently were used without an assessment of risk or preparation of a D&F (a requirement added to the FAR two years ago).

In order to better implement these safeguards, the Councils propose to amend FAR Part 16 to make it explicitly clear that T&M contracts are *not* fixed-price type contracts. In addition, the proposal would amend the GSA schedule program rules in FAR subpart 8.4 to implement the same requirements as the commercial item purchasing rules in FAR Part 12 when using T&M contracts for GSA schedule program purchases; namely requiring a D&F to justify the T&M contract. The proposal would also amend FAR Part 12 to cross-reference this new section in FAR 8.4 and make it clear that GSA schedule T&M purchases are not to be treated differently.

Specifically, the proposal would amend or revise the following parts of the FAR:

- Amend the GSA schedule contract ordering rules in FAR § 8.405-2 to add a new paragraph (e) to establish basic ordering procedures for T&M schedule contract orders, expressly including the D&F requirement for initial orders and ceiling price increases.
- Amend the commercial item T&M rules in FAR § 12.207 to add a cross-reference to the GSA schedule contract T&M requirements in subpart 8.4.

CONTACTS

If you would like more information, please contact any of the McKenna Long & Aldridge attorneys or public policy advisors with whom you regularly work. You may also contact:

[Alison L. Doyle](#)
202.496.7604

[John Sorrenti](#)
202.496.7616

- Amend the contract type definitions in FAR § 16.201 and add a new definition provision at FAR § 16.600 to explicitly state that T&M contracts are not fixed-price contracts.

These changes will most directly affect contractors providing services to the government through the GSA schedules program, where the program abuses noted by GAO were found. However, we expect that it will lead to more restrictions on T&M contracting generally as agencies are forced to confront the price risks such contracts present.

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