

September 18, 2012

Hon. Frank Kendall
Under Secretary of Defense (Acquisition, Technology and Logistics)
3010 Defense Pentagon
Washington, DC 20301-3010

Dear Under Secretary Kendall:

On behalf of the more than 350 member companies of the Professional Services Council (PSC), I am writing to express our concerns with the Department of Defense's implementation of Section 808 of the fiscal year 2012 National Defense Authorization Act. On July 31, DoD rescinded a June 6 DFARS class deviation that improperly implemented Section 808 and superseded it with a revised DFARS class deviation. Unfortunately, the July 31 guidance also fails to appropriately implement key components of Section 808. Our member companies are already reporting instances where the law or the guidance is being misinterpreted and misapplied.

Of key concern is that Section 808 requires DoD to establish a negotiation objective of capping contractor labor and overhead rates at fiscal year 2010 levels. It also directs contracting officers to obtain written approval from the secretaries of military departments and the heads of applicable defense agencies for any fiscal year 2012 or 2013 contract or task order in excess of \$10 million that provides continuing services at an annual cost exceeding that paid by the military department or defense agency for the same or similar services in fiscal year 2010.

DoD's July 31 deviation should have been more thorough. The guidance fails to provide allowable exemptions, such as for commercial items, firm-fixed price contracts, and contracts with priced options or instances where contractors have pre-negotiated forward pricing rate agreements. The guidance does not adequately clarify instances when it is acceptable to negotiate contractor labor or overhead rates that are higher than 2010 levels. Although the guidance states that negotiation objectives should seek to hold rates to 2010 levels, unless the rates are otherwise established by law, the guidance fails to provide meaningful examples that would clarify such instances. The Service Contract Act and the Davis-Bacon Act are two such examples where the government's actions dictate escalations in contractor's labor rates. In addition, recent Cost Accounting Standards changes, particularly related to pension harmonization that were a result of the Pension Protection Act (P.L. 109-280), did not go into effect for most contractors until 2011. As a result of these changes, many contractors' overhead rates necessarily increased. The deviation issued on July 31 does not account for this dynamic and would effectively punish contractors for actions taken in response to government mandates.

Adding to the complexity is the fact that several of the military services and defense agencies have issued their own, equally misguided, supplemental interpretations. As a result, the goal of holding contractors' labor and overhead rates at 2010 levels is being received by some not as a negotiation objective but as a mandate that forbids paying higher rates. Other activities are declaring that they simply will not allow new contracts or task orders that exceed amounts paid for the same or similar services in 2010. Some activities allow the written approval of the head of the agency to be delegated

while others do not. Additionally, in some cases government acquisition personnel are dictating to contractors that they either revert to 2010 labor rates or the agency will not exercise a contract option—a rigid stance that hardly represents a “negotiation.”

In light of these early reports of misinterpretation, it is clear that revised guidance is urgently needed. Hence, we strongly urge the department to issue such guidance as quickly as possible to stem the consequences being felt by department contracting offices and by industry. As you know, Section 821 of the Senate Armed Services Committee-approved version of the fiscal year 2013 NDAA would extend all of the requirements of Section 808 to apply to fiscal year 2014 funds. PSC opposes the extension of Section 808 given that implementation of several key provisions is already proving to be problematic and that the extension prematurely assumes positive results. Thus, we also strongly encourage you to share with the Congress additional implementation problems that the department has experienced as a result of the statutory language. In any event, the prospect of this restriction being extended makes immediate action all the more imperative.

Thank you in advance for your attention to this important matter. We look forward to working with you on potential solutions. As always, please do not hesitate to contact me if you have any questions.

Sincerely,

A handwritten signature in black ink, appearing to read "Stan Soloway". The signature is stylized and cursive.

Stan Soloway
President & CEO

CC: Richard Ginman – Director, Defense Procurement and Acquisition Policy
Linda Neilson – Deputy Director, Defense Acquisition Regulations System