Department of Energy
Acquisition Regulation

No. AL-2014-02
Date October 29, 2013

ACQUISITION LETTER

This Acquisition Letter is issued under the authority of the Senior Procurement Executives of DOE and NNSA. It is intended for use by procurement professions of DOE and NNSA, primarily Contracting Officers, and other officials of DOE and NNSA that are involved in the acquisition process. Other parties are welcome to its information, but definitive interpretations of its effect on contracts, and related procedures, if any, may only be made by DOE and NNSA Contracting Officers.

Subject: Provisional Payment of Fee

References:

FAR Part 16	Types of Contracts
FAR Subpart 16.4	Incentive Contracts
FAR Part 32	Contract Financing

When Is this Acquisition Letter (AL) Effective?

This AL is effective immediately upon issuance.

When Does this AL Expire?

This AL remains in effect until superseded or canceled.

Who Is the Intended Audience For this AL?

Department of Energy (DOE) Contracting Officers who are considering providing for provisional payment of fee under their non management and operating (M&O) contracts are the audience for this AL.

Who Is the Point of Contact For this AL?

Contact Michael Righi of the Contracts and Financial Assistance Policy Division, Office of Policy, Office of Acquisition and Project Management at (202) 287-1337 or at Michael.Righi@hq.doe.gov.

Need More Information on ALs?

Visit the website at http://energy.gov/management/office-management/operational-management/procurement-and-acquisition/guidance-procurement for information on Acquisition Letters and other policy issues.

What Is the Purpose Of this AL?

The purpose of this AL is to provide guidance on provisional payment of fee.

What Types of Contracts Are Affected by this AL?

This AL applies to non M&O contracts that provide for provisional payment of fee.

What Is the Background Of this AL?

DEFINITIONS

Issuing effective guidance on provisional payment of fee requires establishing definitions and concepts. They are listed below (all definitions are consistent with the Federal Acquisition Regulation (FAR) and DOE fee policy and constructs):
(1) *Price* means cost plus any fee or profit applicable to the contract.
(2) The terms *profit* and *fee* are synonymous.
(3) *Incentive* means a term or condition (used only when a firm-fixed-price arrangement is not appropriate) whose purpose is to motivate the Contractor to provide supplies or services at lower costs and, in certain instances, with improved delivery or technical performance, by relating the amount of profit or fee earned to the Contractor's performance.
(4) *Earned fee* for an incentive means the fee due the Contractor by virtue of its meeting the contract's requirements entitling it to fee. Earned fee does not occur until the Contractor has met <u>all</u> conditions stated in the contract for earning fee.
(5) *Available fee* for an incentive means fee the Contractor might earn but has not yet earned.
(6) *Provisional payment of fee* for an incentive means the Government's paying available fee to the Contractor for making progress towards meeting the performance measures for the incentive before the Contractor has earned the available fee. As "an authorized Government disbursement of monies to a contractor prior to acceptance of supplies and services by the Government," a provisional payment of fee falls under the category of a contract financing payment as stated in the Definitions section of FAR Part 32.
(7) The Government's determination that the Contractor has met the requirements for the provisional payment of fee for an incentive has no implications for the Government's eventual determination that the Contractor has or has not earned the associated available fee for the incentive. Provisional payment of fee is a separate and distinct concept from earned fee. A contractor could in some instances, for example, receive 100% of possible provisional fee payments yet not earn any fee (the contractor would be required to return all of the provisional fee payments). A contractor could in other instances, for example, receive 0% of possible provisional fee payments yet earn the entire amount of available fee (it would not receive any fee payments until the Government's determination that the Contractor had earned the associated available fee for the incentive).

(8) *Clause* means a term or condition used in a contract.

EARNED FEE

Articulating clearly in a contract what constitutes the Contractor's meeting the contract's requirements entitling it to fee for an incentive (how and when the Contractor earns fee) is a key aspect of contract formation. Under the FAR's contract formation and pricing construct and congruent with DOE fee policy, the concept of earned fee (similar to the concept of an incentive) does not fit in perfectly with firm-fixed-price contracting. A firm-fixed-price contract for one item (the simplest form of a fixed-price type contract) calls for the Contractor to deliver one item and for the Government to pay (the price) the Contractor once, upon performance, which occurs at contract completion. If the Contractor doesn't perform, the Government pays nothing (the Contractor works under the ultimate "incentive," receiving neither cost reimbursement nor fee if it does not perform).

DOE's policy is to first consider the use of a fixed-price contract. This contract type is most appropriate when supplies or services can be objectively defined in a statement of work and the risks involved can be estimated with an acceptable degree of certainty. Of all contract types, this contract type best matches DOE's two primary principles for aligning contract incentives, that is, it provides a contract that is structured so that the Contractor is not rewarded if the taxpayers are not well served and it results in the Contractor bearing responsibility for its actions.

If use of a fixed-price contract is not appropriate and a cost-reimbursement contract is selected, DOE policy mandates the Contracting Officer use objective performance measures as much as possible and only use subjective performance measures if objective measures are not feasible. DOE policy also mandates the Contracting Officer link all of, or a substantial portion of, the fee to the achievement of final outcomes rather than interim accomplishments. Ideally, the Contractor will not earn fee for any incentive until it has completed the contract (or portion of the contract that provides value to the taxpayer, such as completion of all of the requirements for a performance based incentive). At the end of a major project, for example, if the contractor has not met the objective of the contract for that project, it should not receive fee for its performance on that project.

In all cases a contract's price, incentives included in its price, and all other terms should reflect the Government's and the Contractor's agreement to link, to the maximum extent practical, the Contractor's earning of fee to its achievement of final outcomes rather than interim accomplishments.

It is a fundamental requirement of DOE policy that if a contract includes an incentive it must specify unambiguously the requirements the Contractor must meet to earn the fee for the incentive.

PROVISIONAL PAYMENT OF FEE

As stated above, ideally, Contractors will not earn fee for any incentive until they have completed their contracts. It is evident, of course, that delaying Contractors' earning of fee will influence Contractors' toward proposing higher fees—because they will face greater uncertainly and bear higher financing costs. To mitigate this upward influence on fees due to the delayed earning of fees, Contracting Officers may sometimes determine it in the Government's interest to provide some provisional payment of fees. In some cases it may be appropriate to provide a mix of incentives in the contract with different types of fee payments associated with different incentives. A contract might appropriately be structured, for example, to allow some fee to be paid and earned as progress is made, some fee to be paid provisionally (but not earned) until contract completion, and other fee only to be earned and paid at contract completion.

Before a contract may provide for provisional payment of fee for an incentive, it must first specify unambiguously the requirements the Contractor must meet to earn the fee for the incentive. After that requirement is met, if a contract provides for provisional payment of fee for an incentive, the contract must stipulate the requirements the Contractor must meet before the Government is obligated to pay fee, provisionally, to the Contractor for that incentive and for the Contractor to have any right to retain the provisionally paid fee.

Regarding the requirements for provisional payment of fee and the calculation of each provisional fee payment for an incentive, the contract must also state:
(1) the Contracting Officer, at his/her sole discretion, determines if the Contractor has met the requirements;
(2) the Contracting Officer's calculation of the amount of <u>each</u> provisional fee payment—
(i) will never be a set percentage, a fixed amount, or any other constant value and will be directly and expressly linked to continued performance, that is, to continued progress towards eventually earning the available fee for the incentive;
(ii) will be accomplished per explicit procedures expressed in the contract; and
(iii) with each successive payment, if any, will reflect the Contractor's cumulative performance to date.
(3) if the Contracting Officer determines the Contractor has not met the requirements to retain any provisionally paid fee and notifies the Contractor, the Contractor must return that provisionally paid fee to the Government within 30 days and --
(i) the Contactor's obligation to return the provisional paid fee is independent of its intent to dispute or its disputing the Contracting Officer's determination; and
(ii) if the Contractor fails to return the provisionally paid fee within 30 days of the Contracting Officer's determination, the Government, in addition to all other rights that accrue to the Government and all other consequences for the Contractor due to the Contractor's failure, may deduct the amount of the provisionally paid fee from: amounts it owes under invoices; amounts it would otherwise authorize the Contractor

to draw down under a Letter of Credit; or any other amount it owes the Contractor for payment, financing, or other obligation.

What Guidance Included in this AL?

1. What's new for Contracting Officers?

Before providing for provisional payment for an incentive in a contract, Contracting Officers must first specify unambiguously in the contract the requirements the Contractor must meet to earn the fee for the incentive. After that requirement is met, if a contract provides for provisional payment of fee it must include the attached clause. Contracting Officers must also ensure all parts of the contract are congruent with the clause's requirements.

2. What's new for Other Officials Involved in the Acquisition Process?

This AL requires nothing new from other officials involved in the acquisition process.

3. Who has what responsibility for implementing this AL's guidance?

The Contracting Officer has the responsibility of implementing this AL.

4. *What changes implemented by this AL's guidance affect current contracts, future contracts, or both?*

This AL's guidance requires the Contracting Officer, before providing for provisional payment of fee for an incentive in a contract, to specify unambiguously in the contract the requirements the Contractor must meet to earn the fee for the incentive. After that requirement is met, if a contract provides for provisional payment of fee it must include the attached clause and the other parts of the contract must be congruent with the clause's requirements. This AL's guidance applies to all future contracts and, to the extent they do not already obligate the Government to provide for provisional payment of fee, to current contracts.

Attachment

PROVISIONAL PAYMENT OF FEE

(a) Notwithstanding any other term or condition of this contract to the contrary, this clause applies to and has precedence over all other terms and conditions of this contract that provide for provisional payment of fee.

(b) The Contractor must notify the Contracting Officer immediately if it believes any incongruence exists between this clause and any other term or condition of this contract that provides for provisional payment of fee. If a term or condition of this contract provides for provisional payment of fee but fails to include all of the requirements of this clause, that term or condition will be considered to include the omitted requirements.

(c) This clause conforms to the Federal Acquisition Regulation and Department of Energy fee policy and constructs. The following definitions and concepts apply.
(1) *Price* means cost plus any fee or profit applicable to the contract.
(2) The terms *profit* and *fee* are synonymous.
(3) *Incentive* means a term or condition whose purpose is to motivate the Contractor to provide supplies or services at lower costs, and in certain instances with improved delivery or technical performance, by relating the amount of profit or fee earned to the Contractor's performance.
(4) *Earned fee* for an incentive means fee due the Contractor by virtue of its meeting the contract's requirements entitling it to fee. Earned fee does not occur until the Contractor has met <u>all</u> conditions stated in the contract for earning fee.
(5) *Available fee* for an incentive means the fee the Contractor might earn but has not yet earned.
(6) *Provisional payment of fee* for an incentive means the Government's paying available fee for an incentive to the Contractor for making progress towards meeting the performance measures for the incentive before the Contractor has earned the available fee.
(7) Provisional payment of fee has no implications for the Government's eventual determination that the Contractor has or has not earned the associated available fee. Provisional payment of fee is a separate and distinct concept from earned fee. The Contractor could, for example, receive 100% of possible provisional fee payments yet not earn any fee (the Contractor would be required to return all of the provisional fee payments). The Contractor could, for example, receive 0% of possible provisional fee payments yet earn the entire amount of available fee (it would not receive any fee payments until the Government's determination that the Contractor had earned the associated available fee for the incentive).
(8) *Clause* means a term or condition used in this contract.

(d) This contract's price, incentives included in its price, and all other terms and conditions reflect the Government's and the Contractor's agreement to link, to the maximum extent practical, the Contractor's earning of fee to its achievement of final outcomes rather than interim accomplishments.

(e) Certain terms and conditions of this contract provide for provisional payment of fee for certain incentives. Other terms and conditions of this contract provide for each such incentive the requirements the Contractor must meet to earn the fee linked to the incentive. The terms and conditions of this contract that provide for provisional payment of fee for certain incentives include for each such incentive the requirements the Contractor must meet before the Government is obligated to pay fee, provisionally, to the Contractor and for the Contractor to have any right to retain the provisionally paid fee.

(f) The Contracting Officer, at his/her sole discretion, will determine if the Contractor has met the requirements under which the Government will be obligated to pay fee, provisionally, to the Contractor and for the Contractor to have any right to retain the provisionally paid fee.

(g) If the Contracting Officer determines the Contractor has not met the requirements to retain any provisionally paid fee and notifies the Contractor, the Contractor must return that provisionally paid fee to the Government within 30 days:
(i) the Contactor's obligation to return the provisional paid fee is independent of its intent to dispute or its disputing the Contracting Officer's determination; and
(ii) if the Contractor fails to return the provisionally paid fee within 30 days of the Contracting Officer's determination, the Government, in addition to all other rights that accrue to the Government and all other consequences for the Contractor due to the Contractor's failure, may deduct the amount of the provisionally paid fee from: amounts it owes under invoices; amounts it would otherwise authorize the Contractor to draw down under a Letter of Credit; or any other amount it owes the Contractor for payment, financing, or other obligation.

(h) If the Contractor has earned fee associated with an incentive in an amount greater than the provisional fee the Government paid to the Contractor for the incentive, the Contractor will be entitled to retain the provisional fee and the Government will pay it the difference between the earned fee and the provisional fee.