National Defense Industrial Association

Industrial Committee of Ammunition Producers (ICAP)

Fixed Price vs. Fixed Price Incentive Contracts

Action 16-9

6 October 2016

FFP vs. FPI

A Firm Fixed Price contract is the optimal contract type for a mature production program. Use of a Fixed Price Incentive contract for a production program is in contradiction to the FAR and is inconsistent with the logical progression of contract type determinations by the Contracting Officer.

Where the U.S. Army has been procuring ammunition for multiple five years utilizing well-established Government generated Technical Data Packages, a Firm Fixed Price contractual vehicle should be used.

The FAR

- FAR 16.202-2 FFP contracts are suitable for acquiring supplies or services on the basis for reasonably definite functional or detailed specifications when the contracting officer can establish fair and reasonable prices at the outset. The examples given are as follows:

(a) There is adequate price competition;

(b) There are reasonable price comparisons with prior purchases of the same or similar supplies or services made on a competitive basis or supported by valid certified cost or pricing data;

(c) Available cost or pricing information permits realistic estimates of the probable cost or performance; or

(d) Performance uncertainties can be identified and reasonable estimates of their cost impact can be made, and the contractor is willing to accept a firm fixed prices representing assumption of the risks involved.

- Conversely, FAR 16.401(a) explains incentive contracts are appropriate when a firm-fixed-price contract is not appropriate and the required supplies or services can be acquired at lower costs and, in certain instances, with improved delivery or technical performance, by relating the amount of profit or fee payable under the contract to the contractor's performance.
  - In mature ammunition programs there are years' worth of price history available to the USG to make price comparisons of all of the components of the ammunition. The contractors provide the Government with detailed proposals that permit a thorough analysis by DCAA and Government price analysts and given the maturity of the Technical Data Package, there are minimal, if any, performance uncertainties, therefore a FFP contract is appropriate, and, in accordance with FAR 16.403(b)(1), FPI would not be appropriate.
- Fixed Price Award-fee provisions (FAR 16.404) may be used when the Government wishes to motivate a contractor and other incentives cannot be used because performance cannot be measured objectively. Such contracts establish a fixed price (including normal profit) for the effort, which is paid for satisfactory contract performance. The award fee earned (if any) will be paid in addition to that fixed price. An award-fee contract is suitable for use when the work to be performed is such that it is neither feasible nor effective to devise predetermined objective incentive targets applicable to cost, schedule, and technical performance. Any additional administrative effort and cost required to monitor and evaluate performance must be justified by the expected benefits.

Other Inputs

- Incentive contracts are used by the USG primarily to motivate a contractor to elevate performance in an environment where such performance is discouraged because of risks associated with cost growth. This doesn't appear to fit the mold of mature ammunition programs. An FPI contract would be more appropriate for the development of new ammunition, where the USG wishes to motivate a contractor to achieve certain performance objectives.
- A Fixed Price Incentive contract will increase administrative burden on both the USG's and the contractor's part while shifting some of the risk for contract performance from the contractor to the USG. These additional administrative efforts will come at an increased cost to the program and will have the unwanted effect of increasing the price of the ammunition.
- Frank Kendall, Under Secretary of Defense for Acquisition, Technology and Logistics, provides further clarity on selection of the correct contract type in his 2013 article discussing the intent of Better Buying Power 2.0: "Use of Fixed Price Incentive Firm (FPIF) Contracts in Development and Production". Kendall points to five areas to be evaluated when choosing a contract type: Firm Requirements, Low Technical Risk, Qualified Suppliers, Financial Capacity to Absorb Overruns, and Motivation to Continue. If a program and the contractor have the ability to answer "yes" to these criteria, then a fixed-price contract is most likely appropriate.
- In referring to Fixed-Price-Incentive contracts, Frank Kendall wrote that "We do NOT want exclusive use of these types of contracts, but instead want to reinforce that they should be used whenever appropriate and given explicit consideration and some preference over other contract types." From *Better Buying Power 3.0, White paper, Office of the Under Secretary of Defense, Acquisition, Technologies and Logistics, Honorable Frank Kendall, 19 September 2014*".

- What does the Army want from Fixed Price Incentive Contracts?
- Is there a way to Maintain Contractor Profit, Reduce Administrative Burden, and Meet the Army's Objectives?