Recently we **wrote** about commercial items in support of the notion that when the government enters the marketplace it must buy those commercial items in the manner in which the marketplace offers them for sale. The government contracting officer (or prime contract buyer or higher-tier subcontractor buyer) must acquire commercial items via use of “customary commercial practices.” The customary commercial practices must be determined by adequate market research; and market research involves more than simply looking at how other government agencies acquired such services.

Similarly, sales to government entities—whether foreign or domestic—do not support the determination that an item meets the FAR 2.101 definition of a “commercial item.” Those wishing to have their items determined to be “commercial items” must demonstrate several things, including (but not limited to):

-

The item is “of a type” that is “customarily used by the general public” or by “non-governmental entities”

-

The item is used for “purposes other than governmental purposes”

-

The item has been “sold, leased, or licensed to the general public” or “has been offered for sale, lease, or license to the general public”

Having a service determined to be a commercial item is even harder. Without going into detail, the fundamental requirement is that, to be determined to be commercial, the services must be “of a type offered and sold competitively in substantial quantities in the commercial marketplace based on established catalog or market prices for specific tasks performed or specific outcomes to be achieved and under standard commercial terms and conditions.”

As we noted in our prior article (link in first sentence), when a contractor seeks to have its items (or services) determined to be commercial items, the contractor bears the burden of providing sufficient information to enable the contracting officer (or buyer) to make the determination of commerciality. It is not the contracting officer’s job (or the buyer’s job) to ensure sufficient information has been provided; it is the responsibility of the entity who desires to have the commerciality determination made.

But for some reason many entities are reluctant to provide that information. They don’t want to tell anybody else who else has purchased the items or services, and under what conditions. They want a determination of commerciality, but they don’t want to provide the necessary support to enable it to be made.

Obviously, looking at the bulleted points we listed above, anybody seeking a determination of commerciality should be prepared to identify—at a minimum—the non-governmental entities that have purchased the items in the past and for what purpose they were acquired. If no sales have yet taken place, there needs to be sufficient information to show that the items have been offered for sale. If you can’t at least muster that information, you should not expect to get the determination you say you want. Yet many entities seem to think providing such information in an intrusion into their private business.

No doubt some of that perception stems from the lack of experience with governmental sales. If you’ve never sold to the Federal government, you may not fully appreciate just how intrusive the experience can be. Indeed, having your transaction with the Federal government conducted under FAR Part 12 procedures—as compared to Part 15 procedures—significantly reduces the intrusions. But in order to get to Part 12 you have to first get that coveted

determination of commerciality—which means you've got to provide the necessary information.

It is also possible—perhaps even likely—that companies that have not sold to the Federal government before have not collected the information or organized it in the necessary format to support that determination of commerciality. They may not actually know their customers to the level of detail necessary to stratify them into governmental versus non-governmental. But if you can't get organized to that extent, you probably shouldn't be thinking about selling to the Federal government.

Even if the commerciality determination is made and Part 12 procedures are used for the acquisition, the contracting officer must still made another determination that the price being paid is "fair and reasonable." And that's a *whole 'nother* challenge.

In order for the buyer to determine that the price is fair and reasonable, more information is necessary. If your company is involved in a competitive acquisition, it is likely the buyer will use price analysis to determine if your price is fair and reasonable. That means your price (and terms) will be compared to the other bidders. But in a sole-source acquisition—one in which there are no other bidders—that comparison is not possible, and so the buyer will be asking for "information other than cost or pricing data"—which is likely to be the prices (and terms) at which your items have been sold previously to the public. That may well be a difficult challenge for companies selling commercial items.

Many companies consider their prices to be proprietary information, not to be disclosed outside the company. They may (reluctantly) provide pricing information to a government official, for official use only. But they will tend to resist providing that information to another commercial entity (such as a higher-tier subcontractor or the prime)—especially if that other commercial entity is a competitor in the same or adjacent market.

Circling the wagons and protecting that information by calling it "proprietary" is your privilege; but it also means you are not likely to get what you want. And if you think supporting the determinations under Part 12 procedures is invasive—just wait for the cost and pricing data requirements under Part 15.

Companies selling commercial items actually may not know the historical prices paid for their

items, especially if there are complex discounting strategies in play. It may be labor-intensive and overly expensive to mine the data and conduct interviews and prepare the necessary information for submission to the buyer who has requested it.

But as noted above, if you are not willing to do the work involved, you probably aren't going to be happy with the result.

What happens if the government buys commercial items without competition, and without obtaining the necessary information to support a determination that the price being paid is fair and reasonable? Well the DoD Inspector General **recently issued** an audit report that discussed just such a situation.

Because the DoD OIG audit report was "for official use only" our information is limited to the summary it published. There are no details. But the summary is sufficient for our purposes.

According to the audit report, the Defense Logistics Agency (DLA) issued a contract with a maximum value of $1 billion to CFM International for the purchase of spare parts for the F108 engine. According to Wikipedia, the F108 engine is a "high-bypass turbofan aircraft engine." Interestingly, CFM International (CFMI) is only the distributor of the engines. The engines are actually manufactured by GE Aviation and SNECMA (an French company). Some components are made by Avio (an Italian company). According to Wikipedia: "The engines are assembled by GE in Evendale, Ohio, and SNECMA in Villaroche in France. The completed engines are marketed by CFMI." Wikipedia says that CFMI is "a 50/50 joint-owned company" of GE and SNECMA.

Wikipedia also states that the F108 (aka CFM56) "is now one of the most common turbofan aircraft engines in the world, with more than 20,000 having been built in four major variants." The engine is used by both commercial and military aircraft; it is used by both Airbus and Boeing. Accordingly, it should have been relatively easy for CFMI to support the DLA determination of commerciality. However (according to the DoD IG), "the contracting officer did not question the commercial off-the-shelf classification for parts with no commercial sales."

You'd think that parts that have been in continuous production since 1974, and which have been sold worldwide to companies that include both Airbus and Boeing, and which have been

used in commercial aircraft such as the Boeing 737 and the Airbus 320, would obviously be commercial items. But you'd be wrong—at least, according to the DoD Inspector General. Apparently, although some of the parts sold to DLA were "of a type" that were also sold commercially, in fact the exact parts being acquired had no commercial sales. (We assume this; the summary doesn't really say so.) Our position on the matter is that "of a type" is right there in the commercial item definition in FAR 2.101, and that should have been sufficient for the contracting officer and the Inspector General auditors.

On the other hand, determining that the prices being paid were "fair and reasonable" is a *whole 'nother* problem—especially because the acquisition was on a sole source basis. (Which makes sense, because CFMI is the only company that sells the engines and the spare parts for them.) The DoD IG report summary stated—

The DLA Aviation contracting officer did not appropriately determine fair and reasonable prices for sole-source commercial spare parts purchased from CFM International. This occurred because the contracting officer did not conduct a sufficient price analysis. Specifically, the contracting officer:

- relied on sales data that did not include customer names;
- did not review commercial sales quantities; and
- accepted prices for sole-source commercial parts with no commercial sales.

It seems that CFMI was unwilling to provide the names of its customers when the DLA contracting officer requested that information. This put the CO in a bind, because CFMI was the only game in town. Unlike most transactions where the Federal government is the big gorilla in the room, in this transaction CFMI was the big gorilla.

"*You want our parts? Fine. Here are the prices. You want support? No. Shop somewhere else."*

The above imaginary monologue illustrates the attitude of many commercial entities seeking to do business with the Federal government. In this case, the entity had the negotiating position to carry it off—but note that the transaction resulted in an adverse Inspector General audit report which carried a recommendation that the DLA Director should "take administrative action

[regarding the contracting officer] … for not following the Federal Acquisition Regulation and defense acquisition guidance."

This story is not really about CFM International and that particular transaction. It's intended to be about entities that want to have their items or services determined to be commercial items, and their prices for those items/services determined to be fair and reasonable. If you want to make that happen, you need to be prepared to give the individual making those determinations sufficient information. If you don't give sufficient information, you are not likely to get what you want. And if, by some lucky happenstance, you do get what you want without providing the required information, then you need to be prepared for downstream consequences, such as an adverse Inspector General audit report.