

Performance-Based Payments: Final DFARS Rule

Written by Nick Sanders

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It's all COVID-19, all the time. Except when it's not.

In between the pandemic panic¹ the wheels of acquisition rule-making continue to grind, albeit with the rapidity of a downhill skier racing through gravel. In fact, on April 8, several DFARS final rules were issued, along with several proposed rules. By and large, there isn't much in the regulatory revisions that is worth reporting—though note proposed dollar threshold changes to several DFARS regulations/clauses found in [this](#) proposed rule.

But the one thing that caught our eye was the [final DFARS rule](#) on performance-based payments (PBPs).

Readers know this one because we've [commented](#) on it before on this blog site, and even [submitted](#) a comment into the rule-making process. The “current state” DFARS rules were so bad that the DOD [issued](#) a Class Deviation to help contracting officers get it right.

Remember, PBPs are not progress payments. Progress payments are contract financing payments based on a percentage of costs incurred. PBPs are contract financing payments that are fixed amounts tied to accomplishment of significant program or technical events. We discussed the differences in [this article](#) .

Anyway, the final rule gets it mostly right. The impacted DFARS clauses have been revised “to specifically state that it is not necessary to have a Government-unique cost accounting system in order to report incurred costs under the clause”—which was our major gripe with them. In addition, “the procedures at DFARS 232.1004 are modified to eliminate the requirement to first agree on price using customary progress payments and then require consideration if performance-based payments are subsequently negotiated.” Those are good things, and we applaud the DAR Council for listening to public input. (Historically, that has not always been the case.)

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In the final rule, the DAR Council makes it clear that some type of “job cost accounting” is still required when PBPs are used. In response to public comments on the issue, they wrote “It would be highly unlikely for a fiscally sound company to have no means of identifying the costs of performing a contract. Furthermore, the rule does not require any particular accounting system; rather, the rule states that ‘incurred cost is determined by the Contractor’s accounting books and records.’”

Further despite respondents (including us!) pointing out that the government shouldn’t need to use incurred costs as the basis for negotiating future costs, the requirement was retained in the final rule. The DAR Council wrote “... aside from the value to Government negotiators of being able to evaluate current proposals for PBP milestone values against past experience, it remains important for the Government to know the risk it is incurring when it makes payments that may be disproportionate to the contractor’s investment in contract performance.”

Regardless, the final rule represents a significant improvement over the current state that existed before the regulatory revision. One suspects that the DOD Class Deviation is no longer needed.

In the midst of COVID-19 thoughts and decisions and actions, consider the DAR Council, who is still grinding through open cases. We wish them well.

¹ “Pandemic Panic” is the name of my new deathmetal band. I’m calling it now.