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OFFICE OF MANAGEMENT AND BUDGET
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OFFICE OF FEDERAL
PROCUREMENT POLICY

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MEMORANDUM FOR CHIEF ACQUISITION OFFICERS
SENIOR PROCUREMENT EXECUTIVES

FROM: Lesley A. Field
Deputy Administrator

SUBJECT: Increasing Competition and Structuring Contracts for the Best Results

The President's March 4, 2009, Memorandum on Government Contracting calls on federal agencies to examine their use of noncompetitive and cost-reimbursement contracting as one of several key actions to improve results achieved from government contractors. Each of these contracting authorities carries significant potential risk of overspending taxpayer resources. Noncompetitive contracts place agencies in the position of having to negotiate contracts without the benefit of a direct market mechanism to help establish pricing. Competitions that yield only one offer in response to a solicitation deprive agencies of the ability to consider alternative solutions in a reasoned and structured manner. Cost-reimbursement contracts, as well as time-and-materials and labor-hour (T&M/LH) contracts, provide limited direct incentive to control costs. Reports from the Government Accountability Office (GAO), agency inspectors general, and agency management point to a general overuse of these authorities and significant lost opportunities for savings and performance efficiencies.

To address these concerns, the Office of Management and Budget (OMB) instructed agencies to take immediate action. In accordance with OMB Memorandum M-09-25, *Improving Government Acquisition* (July 29, 2009), agencies must reduce by at least 10 percent the combined share of dollars obligated through new contracts in FY 2010 that are: (1) awarded non-competitively and/or receive only one bid in response to a solicitation or a request for quote, (2) cost-reimbursement contracts, or (3) T&M/LH contracts.

The President's Memorandum also called upon OMB to issue guidance: (1) to govern the appropriate use and oversight of sole-source and other types of noncompetitive contracts and to maximize the use of full and open competition and other competitive procurement processes; and (2) to govern the appropriate use and oversight of all contract types, in full consideration of the agency's needs, and to minimize risk and maximize the value of Government contracts generally.

In response to the President's charge, the Office of Federal Procurement Policy (OFPP) has established initial guidelines to help Chief Acquisition Officers (CAOs) and Senior Procurement Executives (SPEs) evaluate the effectiveness of their agency's competition practices and processes for selecting contract types. The guidelines focus around three key questions:

(1) How is the agency maximizing the effective use of competition and choosing the best contract type for the acquisition?

(2) How is the agency mitigating risk when noncompetitive, cost-reimbursement, or T&M/LH contracts are used?

(3) How is the agency creating opportunities to transition to more competitive and lower risk contracts?

OFPP's guidelines include a set of considerations to help CAOs and SPEs address each of these questions. They are intended to help agencies identify specific areas in need of greater management attention, training, and workforce development. Accordingly, CAOs and SPEs should use the considerations to evaluate progress against their high risk contracting reduction targets. These evaluations may be included as part the competition advocate's annual assessment of agency accomplishments and planned actions. The evaluations may also be coordinated with reviews performed pursuant to OFPP's *Guidelines for Assessing the Acquisition Function*[1], which integrate acquisition reviews with the internal control procedures outlined in OMB Circular A-123. OFPP will review progress against the targets on a semiannual basis in FY 2010 and require corrective action plans, where necessary. OFPP will set new targets for FY 2011 and beyond and work with agencies to identify best practices, new techniques and strategies, areas in need of additional guidance or policy, and measures and benchmarks.

To achieve sustained improvement, OFPP will work with CAOs, SPEs, and competition advocates to identify and share best practices, new techniques and strategies, areas in need of additional guidance or policy, measures and benchmarks. These efforts will include review and refinement, as appropriate, of the initial considerations to enhance their value as a tool for identifying opportunities for improvement.

Achieving good results from contracting tools is directly linked to the skills, judgment, and capacity of the acquisition workforce. These skills and judgments must be especially well honed to meet the heightened challenges associated with high-risk contracting. OFPP is working with the Defense Acquisition University (DAU) and the Federal Acquisition Institute (FAI) to identify areas in need of targeted training and opportunities for rapidly communicating with the affected community as new rules and policies are developed. CAOs and SPEs should actively identify training needs within their community and aggressively leverage the available training resources of DAU and FAI. Agencies should also review OFPP's Acquisition Workforce Development Strategic Plan[2] to consider their workforce needs.

OFPP appreciates the attention your agency is giving to the President's Memorandum. We look forward to working with your staff and sharing the best practices they develop to increase savings, reduce high-risk contracting, and improve the value our taxpayers receive from federal contracts. Questions regarding this memorandum may be directed to Mathew Blum at (202) 395-4953 or mblum@omb.eop.gov.

Attachment

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[1] See OFPP Memorandum, *Guidelines for Assessing the Acquisition Function* (May 21, 2008), available at http://www.whitehouse.gov/omb/assets/omb/procurement/memo/a123_guidelines.pdf.

[2] See OFPP Memorandum, *Acquisition Workforce Development Strategic Plan for Civilian Agencies* – FYs 2010-2014.

Attachment

Guidelines for Increasing Competition and Structuring Contracts for the Best Results

The President's March 4, 2009, Memorandum on Government Contracting directs agencies to strengthen their use of competition and improve how contracts are structured. The Memorandum states, in particular, that agencies must strive for a process that is "open and competitive" when awarding government contracts. Competition lies at the heart of the federal acquisition system. It drives down costs, motivates better contractor performance, helps to curb fraud and waste, and promotes innovation.

The President's Memorandum further states that government contracts should be structured to "minimize risk and maximize value" for the taxpayer. In most cases, fixed-price contracts will be best suited for achieving this goal because they provide the contractor with the greatest incentive for efficient and economical performance. In circumstances where there is considerable uncertainty regarding the requirements, however, cost-reimbursement contracts or, in more limited circumstances, time-and-materials or labor-hour (T&M/LH) contracts may provide for a more effective allocation of risk between the government and the contractor.

OFPP has established initial guidelines to help Chief Acquisition Officers (CAOs) and Senior Procurement Executives evaluate the effectiveness of their competition practices and processes for selecting contract types. The guidelines should be used to help agencies achieve their targets for reducing the use of high risk contracting authorities. OFPP will review progress against the targets on a semiannual basis in FY 2010 and require corrective action plans, where necessary. OFPP will set new targets for FY 2011 and beyond and work with agencies to identify best practices, new techniques and strategies, areas in need of additional guidance or policy, and measures and benchmarks.

The guidelines consist of *three key questions* and a set of *considerations* for addressing each question. The purpose of the considerations, many of which have been drawn from basic tenets of acquisition policy, is to help identify specific areas in need of greater management attention, training, and workforce development. OFPP will consider refinements to the guidelines based on agency experience.

Key Question #1

How is the agency maximizing the effective use of competition and choosing the best contract type for the acquisition?

Initial considerations

A. Maximizing the effective use of competition

1. **Focus on requirements development and outreach to potential vendors**. Poorly developed requirements that are either vague or unduly restrictive are detrimental to meaningful competition. To promote competition effectively, agencies must provide sufficient information in the statement of work and sufficient time for response. These steps will allow offerors to make informed business decisions on whether to respond to a solicitation and work with end users to perform the due diligence necessary to propose the best solutions. Agencies should take appropriate steps to ensure contracting and program offices are working together and applying their respective skill sets to understand the market for the types of products or services they need, including how industry is structured (e.g., how distribution channels function), potential cost drivers (e.g., how services are provided), and its competitive state. These collaborative efforts would include:

   - inviting potential offerors, through a request for information or an industry day that provides a general description of the scope or purpose of the acquisition, to submit information or have discussions on marketplace capabilities;

   - taking advantage of the full range of market research tools to understand marketplace capabilities and identify all reasonable potential solutions; and

   - engaging potential suppliers, whenever practicable, in an advisory process, especially for complex needs, such as major systems, that invites potential offerors, through a pre-solicitation notice, to submit information that the agency would evaluate to advise offerors of their potential to be viable competitors. An advisory process enables potential vendors to more wisely use their internal resources to perform due diligence.

   By applying both contracting and program skills on these efforts, agencies can facilitate the development of informative requirements documents with expected levels of service quality that put offerors in the best position to propose to the agency's actual needs. This, in turn, increases the probability of awarding a contract through competition that represents the best value available in, or capable of being developed by, the marketplace.

2. **Use performance based acquisitions and commercial solutions**. Performance-based acquisition (PBA) is the government's preferred approach for acquiring services. PBA principles call on agencies to focus on mission outcomes, rather than prescriptions for how work is to be performed or key personnel requirements. By emphasizing this approach, agencies can encourage meaningful competition by allowing vendors to offer more innovative solutions to meet the agency's

performance needs. PBA also allows vendors to offer market-tested commercial solutions at competitive pricing with risks that can be reasonably managed by a small or large business under a fixed-price contract.

3. **Evaluate alternative competition strategies for larger and more complex requirements**. Agencies should ensure that, as part of market research and acquisition planning processes, their contracting and program offices are working together to consider the comparative benefits of awarding a new contract using full and open competition versus placing an order under an existing contract. In making this comparison, agencies might evaluate the strength of each competition strategy in terms of its ability to (i) generate meaningful competition, (ii) meet needs in a timely manner, and (iii) allow for the negotiation of fair and reasonable pricing and terms and conditions to address the requirements at hand.

4. **Use strategic sourcing**. Agencies should actively consider the use of strategic sourcing when requirements can be satisfied through a contracting vehicle under the Federal Strategic Sourcing Initiative. These vehicles have been established to maximize the value of competition by using the government's buying leverage. If these contracting vehicles are not used and the agency chooses instead to use its own vehicle, such as an enterprise-wide vehicle, managers should ensure their agency documents in the contract file the reasons for doing so (e.g., describe the greater savings and/or the more favorable terms and conditions anticipated).[1]

5. **Ensure consistent maximization of competition at the task and delivery order level**. Reviews by agency management, the GAO, and agency IGs indicate that use of competition on task and delivery order contracts is inconsistent. At the same time, data from the Federal Procurement Data System (FPDS) shows that agency expenditures through orders under contracts has increased from just 14 percent of dollars obligated in FY 1990 to more than half of total obligated dollars in FY 2008. These shortcomings coupled with the increasing level of obligations through these vehicles warrant greater management attention by agencies to ensure agencies are achieving meaningful competition in their placement of task and delivery orders, such as by:

   - applying greater competitive rigor through the disclosure of significant factors and subfactors and their relative importance when conducting the "fair opportunity process" for orders over $5 million; and

   - using data generated by new FPDS reports to evaluate in new competitions the extent to which task and delivery order competition is being achieved.

6. **Give maximum practicable consideration to small businesses, including minority businesses, and businesses owned by women and veterans**. In order to maximize performance and minimize

[1] CFO Act agencies are strongly encouraged to prepare as part of (or supplement) their acquisition savings plan to identify (a) their estimated department annual obligations for strategically sourced products or services (e.g., express ground delivery, software and maintenance services, and plumbing and electrical services), (b) the estimated obligation amount to be strategically sourced in FY 10 and 11 and (c) reasons why a strategic sourcing vehicle was not used for all of the agency's spend for that requirement.

costs, agencies need to consider the full range of possible suppliers. Small businesses provide creativity, innovation, and technical expertise to support a wide range of agency requirements at good prices, but are sometimes overlooked as suppliers. Agencies should take appropriate steps to facilitate regular collaboration of contracting and program offices with their Offices of Small and Disadvantaged Business Utilization (OSDBU) in planning acquisitions to identify: (1) requirements that can be met effectively with the help of small businesses, and (2) the small business contracting authority that is best suited for a given requirement and will help the government meet and exceed its small business contracting goals. OSDBUs, the Small Business Administration's (SBA) District Offices, and the Department of Commerce's Minority Business Development Agency can assist agencies with market research to help identify qualified and capable small business sources for prime contracting and subcontracting, both at the national and local level. OSDBUs should actively share their strategies for facilitating access to federal business opportunities. SBA's Procurement Advisory Council serves as one forum for OSDBU exchanges.

B. Choosing the best contract type for the acquisition

1. **Determine the level of uncertainty**. Determining whether an agency should award a fixed-price, cost-reimbursement, or T&M/LH contract requires careful consideration of the level of uncertainty regarding the agency's requirements.

   Fixed-price contracts are preferred unless uncertainty in the requirement and the risk of failure cannot be managed by the contractor within economically reasonable bounds. Fixed-price contracts provide greater incentive than cost-reimbursement contracts for the contractor to control costs and perform efficiently. Many of the same practices that facilitate meaningful competition also promote fixed-price contracting. Sound requirements development and performance-based statements of work, for example, give contractors the opportunity to understand the government's needs and offer solutions, including market-tested commercial items, with an amount of risk that they can manage for a fixed price.

   Cost-reimbursement contracts are more appropriate when there is considerable uncertainty about the resources that will be necessary to achieve the government's objective. This uncertainty may be due to lack of knowledge regarding the effort needed to meet a defined requirement, including a lack of cost experience in performing the work. Alternatively, the uncertainty may be due more fundamentally to a lack of knowledge about what is possible and practical, as is often the case with research or leading-edge innovation. Similarly, T&M/LH contracts may help agencies accomplish tasks for a reasonable cost where the needed amount of labor effort cannot be specified in advance, such as for emergency repair services. In these situations, a cost reimbursement or T&M/LH contract allows the government to absorb a greater portion of the risk and avoid the costly contingencies that contractors would pass on to taxpayers if forced to offer their services on a fixed-price basis.[2]

[2] FAR changes are in process to improve policies and practices associated with the use of cost-reimbursement contracting and help to guard against their overuse. Changes will address: (1) when and under what circumstances cost-reimbursement contracts are appropriate, (2) the acquisition plan findings necessary to support a decision to use cost-reimbursement contracts, and (3) the acquisition workforce resources necessary to award and manage cost-reimbursement contracts.

Over time, experience should generally enable the agency to address these uncertainties, making it possible to convert to a fixed-price contract that creates a better incentive to provide the desired products or services within time and on budget.

2. **Use incentives to motivate lower costs with improved delivery or technical performance and to discourage contractor inefficiency and waste**. In cost-type contracting, incentives enable the government to reduce its exposure to risk by tying the payment of fees to contractor performance. During acquisition planning, agencies should consider the type of incentive that is most likely to motivate efficient and economical performance. For example, the agency should consider use of an objective incentive fee when cost and performance targets can be predetermined and a formula can be used to adjust the negotiated fee based on variations relative to objective targets. The agency might consider an award fee if it is neither feasible nor effective to devise predetermined objective incentives for cost, technical performance, or schedule.

   Incentive arrangements should be developed through close collaboration between the contracting officer, program manager, and technical requirements staff. Incentives should be considered not only to motivate good cost control but also to encourage quality on-time performance, taking into consideration factors that are within the contractor's control, such as achieving a delivery or test schedule, application of quality controls, and effective implementation of maintenance requirements.

Key Question #2

How is the agency mitigating risk when noncompetitive, cost-reimbursement, or time-and-materials / labor-hour contracts are used?

Initial considerations

A. Mitigating the risk of noncompetitive contracts

1. **Limit the length of the contract**. Noncompetitive contracts play an important role in helping agencies address requirements that can only be satisfied by one source or that rise during emergencies when time allows only limited consideration of offers. But these contracts carry risk of overspending because they have been negotiated without the benefit of a direct market mechanism. One way to mitigate risk is to limit the contract's performance period. In some cases, limitations are imposed by law and/or regulation. For example, in circumstances of unusual and compelling urgency, FAR 6.302-2 states that the total period of performance shall not exceed the minimum period necessary for meeting the unusual and compelling urgency requirements, but no longer than one year or such period as specified in law, unless a longer period for performance is approved by the head of the contracting activity. [3] Such approval is in addition to that provided as part of the initial decision to make an award using other than full and open competition.

2. **Ensure price reasonableness**. Agencies must ensure fair and reasonable pricing on all of their acquisitions. This requirement can present challenges when adequate price competition is lacking. Agencies should ensure agencies are obtaining the information and data they need, consistent with the policies established in FAR Subpart 15.4. The FAR Council is currently reviewing proposed clarifications to the pricing policies in FAR Subpart 15.4 regarding the circumstances and procedures for obtaining data or information in the absence of adequate price competition to establish the reasonableness of offered prices.

3. **Regularly assess contractor performance**. Regular assessment and reporting of the contractor's quality, timeliness, cost control, and concern for the customer will improve the agency's ability to motivate quality contractor performance during the life of a contract, including one that has been awarded noncompetitively. The contractor will be motivated by the fact that the strength of its performance on the current contract could affect its position when competing for future federal work.

[3] The Department of Homeland Security and its components are limited to a period of performance no longer than 150 days unless a longer period of performance is approved by the head of the contracting activity.

FAR Subpart 42.15 requires regular assessment of contractor performance and submission of electronic records of these assessments in the Past Performance Information Retrieval System (PPIRS) so that the information may be considered by other agencies. Beginning in February 2010, OFPP will conduct regular compliance assessments and quality reviews to make certain that agencies are submitting to PPIRS timely performance evaluations on required actions and that these evaluations provide clear, comprehensive, and constructive information that is useful for making future contract award decisions.[4]

B. Mitigating risk of cost-reimbursement and T&M/LH contracts

1. **Be forward leaning in management and oversight of cost-reimbursement and T&M/LH contracts**. The government must ensure contractor costs are reasonable and the contractor is making progress in accordance with the contract's performance schedule. In particular, agencies must:

   - determine that the contractor's accounting system is adequate for determining costs related to the contract. Determinations must be periodically updated. Periodic updates are necessitated by the organizational changes contractors make to keep pace with the dynamic demands of the marketplace.

   - have in place appropriate government surveillance to provide reasonable assurance that efficient methods and effective cost controls are in place. Agencies that rely on invoice reviews by contracting officer technical representatives (COTRs) should ensure the COTRs have the skills and capacity to perform adequate reviews before payment is made to contractors. When cost, schedule, or performance variances are identified, agencies should increase their management attention to ensure such variances are eliminated or otherwise addressed.

2. **Link payment to performance on cost-plus-award-fee contracts**. Risk associated with award fee contracts is high because they are designed for circumstances where requirements may be difficult to define with sufficient specificity to measure objectively. Recent changes to FAR Subpart 16.4 detail the steps agencies are required to take so that risk is managed effectively. These required steps include:

   - determining that an award fee contract is the appropriate contract type;

   - tying fees to cost, timeliness, and quality of the contractor's performance;

   - following prescribed standards for differentiating between levels of performance and the corresponding percentage of available award fee that can be earned; and

[4] See OFPP Memorandum, *Improving the Use of Contractor Performance Information* (July 29, 2009), available at http://www.whitehouse.gov/omb/assets/procurement/Improving_the_Use_of_Contractor_Performance_Information.pdf.

- prohibiting both the payment of award fees for unsatisfactory contractor performance and the practice of "roll over" where a contractor is given a second chance to earn fees in a subsequent performance period that were not earned initially.

3. **Determine the appropriateness of T&M/LH contracts in commercial item acquisitions**. Because commercial items have been market tested, risk can be effectively managed in most cases through the use of firm-fixed-price contracts or fixed-price contracts with economic price adjustments. In certain situations, however, such as for emergency repairs, it may not possible at the time of placing the contract to estimate accurately the extent or duration of the work or to anticipate costs with any reasonable degree of confidence. Agencies are authorized to use T&M/LH contracts in these circumstances, but must take care to ensure sufficient analysis underlies the decision, including an explanation of why a fixed-price contract is unsuitable. It is insufficient simply to assert in a D&F that a T&M/LH contract is suitable.[5]

4. **Provide for the necessary skills and capacity in the acquisition workforce to award and manage a cost-type contract**. Development, negotiation, and management of cost-type contracts generally demand more in-depth programmatic knowledge and experience, a higher level and broader range of skills (e.g., including but not limited to, finance, accounting, cost and price analysis, industrial engineering, and program management), and greater resources than are required for competitively awarded fixed-price contracts.

[5] A recent GAO review found limited use of D&Fs for commercial item contracts due, in large part, to a general unawareness of the requirement and lack of its express application to the Multiple Award Schedules (MAS) Program. See *CONTRACT MANAGEMENT: Minimal Compliance with New Safeguards for Time-and-Materials Contracts for Commercial Services and Safeguards Have Not Been Applied To GSA Schedules Program*, GAO-09-579 (June 2009). A FAR case has been opened to expressly apply the D&F requirements generally required for commercial item acquisitions to MAS acquisitions and to consider where additional regulatory or other policy guidance may be beneficial, such as in the reinforcement of requirements associated with acquisition planning.

Key Question #3

How is the agency creating opportunities to transition to more competitive or lower risk contracts?

Initial considerations

A. Transitioning to more competitive contracting

1. **Engage the marketplace to determine how barriers to competition can be removed**. Agencies should encourage their contract specialists and program offices to speak to sources, including leading competitors and sources that expressed interest in the procurement (e.g,. responded to a request for information, participated in an industry day, or contacted the agency OSDBU) but ultimately did not submit offers to understand the basis for their decision not to participate. These discussions might reveal, for example, that:

   - the requirements were not sufficiently clear;
   - sufficient time was not provided to the offerors to perform due diligence;
   - requirements were grouped inconsistent with the way services are commonly performed or provided by industry, or otherwise bundled to make it difficult for small businesses to compete.
   - insufficient reliance was placed on commercial standards;
   - criteria that were used to evaluate sources did not permit meaningful comparison and discrimination between and among competing proposals.

   Contract specialists and program officials should ask sources if future plans, such as those described in published justifications and approval documents for sole-source contracts, will be effective in encouraging competition and if other alternatives should be considered.

2. **Do a spend analysis of the agency's largest spend categories**. Spend analysis is a basic tool for agencies to evaluate the strength of their competition practices and identify opportunities for improvement. Spend analysis may be especially useful for identifying and analyzing competitions for which only one offer was received. To accomplish a spend analysis, an agency might use data in the Federal Procurement Data System (FPDS) to identify the agency's largest spending categories to analyze and compare levels of competition achieved by different organizations within the agency or by organizations similarly situated in other agencies to determine if more successful practices may exist for obtaining greater marketplace competition for a given spending category. OFPP and the Competition Working Group of the Chief Acquisition Officers Council will help agencies create competition profiles that can inform the development of goals and plans for increasing competition on a fiscal year basis.

B. Transitioning to lower risk contract types

1. **Use appropriate mechanisms, such as contract review boards, peer reviews, or contract type advocates to bring additional expertise to bear in determining the best contract type**. FAR 16.103(c) cautions contracting officers to avoid protracted use of a cost-reimbursement or T&M/LH contract after experience provides a basis for firmer pricing. The FAR explains that changing circumstances may make a different contract type appropriate in later periods than that used at the outset. Contract review boards and/or peer reviews can facilitate stronger analyses to determine the best contract type. Teams should include not only contracting experts with relevant background but other appropriate officials such as program managers, systems engineers, and other technical personnel. These reviews can produce constructive ideas and alternatives to test whether bases commonly cited to support the use of high risk contract types, such as complexity of the requirements, uncertain duration of the work, or lack of meaningful spend data, exist and, if so, whether reasonable mitigation steps have been taken. For example, a review might:

   - reveal ways in which complexity and/or uncertainty can be reduced, such as by disaggregating requirements;
   - ensure steps have been taken to differentiate certain and uncertain requirements so that fixed-price options can be used where requirements are known and not-to-exceed amounts for uncertain requirements can be replaced with fixed-price options over time as a pricing history can be established to support firm pricing; and
   - help the acquiring organization improve its use of spend data, such as by using standard methodologies for collecting information on costs, so costs incurred on similar projects or subprojects can be compared more easily to create a history that supports fixed-pricing on future procurements involving similar requirements.

   Agency analyses and associated recommendations should be documented in the contract file to help agency officials with subsequent reviews and decision making. If the agency decides that it is premature to transition to a fixed-price contract, the file should explain the rationale for the decision -- for example:

   - why it remains difficult to define requirements with a reasonable degree of certainty;
   - what spend data has been collected and analyzed, especially for ongoing work that is the subject of a contract option or renewal, and why it does not support firm-fixed pricing; and
   - for T&M/LH contracts, why no other contract type is suitable, including cost-reimbursement contracts for acquisitions of non-commercial items.

Agencies that rely on high-risk contracting to a significant extent are encouraged to consider designating a contracting official to serve as a dedicated "contract type advocate." This advocate could bring greater attention to internal contract type selection practices not only in choosing between fixed-price, cost-reimbursement, and T&M/LH contracts, but also in selecting the type of incentive that can best motivate strong performance and mitigate risk in different situations.

2. **Award contracts that allow the agency to choose between a fixed-price, cost-reimbursement, or T&M/LH basis for the payment of different contract requirements**. A hybrid contract may allow the agency to achieve a better match between the requirement and how the work is priced. Work for which there is a basis for firm pricing can be awarded for a firm-fixed price while requirements for which there remains considerable uncertainty can be acquired on a cost or T&M/LH basis.[6]

   - An agency undertaking a large-scale project with significant development could use a hybrid contract to pay for studies of early design on a cost or T&M/LH basis, later design and initial development using a cost-plus incentive fee arrangement, and initial and full scale production for a firm-fixed price. Of course, agencies should, whenever possible, employ strategies that encourage up front due diligence so that vendors can come up with lower risk solutions that can be met with fixed-price contracts at the earliest feasible point in the acquisition lifecycle, thereby limiting the need to resort to riskier contracting forms.

   - A hybrid contract might support different types of incentive fees so that an agency may use incentive fee contracts with objective performance metrics whenever requirements can be measured objectively and limit the use of award fee contracts with subjective criteria to those requirements whose outcomes cannot be effectively measured objectively.

   A hybrid contract may require additional monitoring to ensure payment is made in accordance with agreed-upon terms (e.g., overruns created by performance inefficiencies on work awarded for a firm-fixed price must not be charged to a cost-reimbursement line item).

[6] As an alternative to a hybrid contract, an agency could competitively award a series of contracts addressing smaller increments or modules of work.