And then this happened …

The DFARS cost principle at 231.205-18 **was revised** to require a contractor and a DoD official to engage in an "informal technical interchange" before the contractor spends any money on its IRAD project. The contractor must document the technical interchange in its DTIC submission. (The DTIC submission was already a requirement.) If the contractor does not hold the technical interchange *prior to incurring the IRAD project cost*, or does not document that technical interchange in its DTIC submission, then its IRAD costs will not be accepted as being allowable costs for purposes of billing DoD.

We told you this was coming, **right here**.

Actually, we told you **way before** that article that this was coming. In September, 2015, we wrote—

Contractors who fail to 'brief' the unspecified and unidentified DoD technical personnel run the risk that their IR&D expenditures will be determined to be unallowable.

Among the myriad problems associated with this proposed approach is the sheer volume of individual IR&D projects that will need to be 'briefed' via technical interchange. Some of the larger contractors have literally hundreds of such projects going on at any given time. For those large contractors, the current requirement to input their project information into DTIC has become a bureaucratic process that adds no value but requires labor—labor that is charged to overhead and passed right back to the DoD buying commands via the contractors' indirect rates. This approach, if implemented, will make things worse.

For example, who pays for the labor and materials associated with the technical interchange briefings? We don't think it should be IR&D, because the IR&D effort could take place whether or not the briefings are made. We don't think the effort should be charged as a direct contract cost—even though the effort would be required by the DoD contracts that contain the new requirement. But we don't think the buying commands will want to pay for such

non-value-added labor that is neither engineering nor manufacturing. Instead, we suspect it will be good ol' overhead that pays for the briefings. And so the overhead rates will go up and up, and DoD will (once again) pay more for goods and services, because it insists on micro-managing its contractors.

All the foregoing is in addition to the basic problem, which is that DoD will be slowing down contractors, who must now wait to schedule their individual briefings before starting work. So much for agility and innovation.

If you were a reader of our blog, you would have been warned more than a year ago that this was coming. You would have seen our concerns with the approach. You could have submitted your comments to the DAR Council for consideration, parroting our comments or submitting your own concerns. You could have tried to influence the final rule, since the DAR Council is required to consider public comments in the rulemaking process.

Not that any of that would have mattered.

Apparently the DAR Council was determined to issue this revision regardless of public input expressing concerns with it.

For example:

Comment: Several respondents stated that the proposed rule will adversely impact innovative ideas. Another respondent cautioned that the rule will create a barrier to innovation and entry to the marketplace.

Response: DoD believes that this rule supports and promotes innovative ideas and technologies, and will incentivize entry into the marketplace by ensuring that IR&D performers and their potential DoD customers have sufficient awareness of each other's efforts and that DoD can provide industry with feedback on the relevance of proposed and completed IR&D work.

Thus, in the views of the DAR Council, requiring a technical interchange prior to initiating an IRAD project will “incentivize entry into the [defense] marketplace.” *Um, no.*

Another example:

Comment: A number of respondents stated that the rule will cost taxpayers more. One respondent stated that the rule will impose an administrative burden on contractors, administrative contracting officers (ACOs), and DoD personnel. Another respondent expressed concern with the significant costs associated with planning and conducting technical interchanges and the costs accrued prior to the technical interchange.

Response: While acknowledging that this rule imposes a slight administrative burden on contractors, ACOs, and DoD personnel, such burdens are overshadowed by the net benefit of ensuring that IR&D performers and their potential DoD customers have sufficient awareness of each other's efforts and that DoD can provide industry with feedback on the relevance of proposed and completed IR&D work. Moreover, the long-term priorities outlined in Better Buying Power 3.0 are a strategic imperative for DoD.

Thus, because BBP 3.0 called for this, it *must* be correct and its benefits *must* outweigh the costs. Forget public input. Forget an objective analysis of the initiative. Just do it, because it must be done. This kind of magical thinking is reminiscent of religious cults.
Please pass the Kool-aid.

Or consider this example:

Comment: A number of respondents expressed concern with DoD responsiveness to requests for technical interchanges, citing that the rule fails to outline DoD's obligations and unfairly saddles contractors with the full consequence of DoD's failure to take part in a technical interchange. One respondent is concerned that the proposed rule creates practical, time, resource, and data disclosure challenges for conducting technical interchanges, and that DoD Components will not have an adequate number of personnel designated to conduct the technical interchanges in the time mandated. Another respondent questioned the recourse

contractors will have if DoD personnel refuse to engage.

Response: To assist contractors in ensuring that technical interchanges take place in a timely manner, the rule has been revised to identify the primary DoD focal point for technical interchanges as OASD R&E. Contact information for this office is available at *http://www.acq.osd.mil/rd/contacts/*.
If a Contractor experiences difficulties scheduling a technical interchange, or does not have a point of contact for the technical interchange, the contractor may contact OASD R&E.

In other words, if you have a problem scheduling the technical interchange because DoD lacks sufficient resources to support it, please feel free to send an email expressing your concerns to the Assistant Secretary of Defense, who will immediately drop whatever else was on his plate and attend to your concerns. *Yeah, right.* Not addressed is what happens in the next Administration, when it is a very real possibility that Congress might not confirm Presidential appointments for a very long period (if at all). To whom do contractors address their concerns if that situation should arise? Guess we are all SOL.

But of course this requirement will not impede contractor IRAD projects whatsoever. *Nope.* In fact, adding this requirement makes things better! Just ask the DAR Council.

This blasé indifference to the question as to whether or not DoD has sufficient resources to actually implement the rule is quite reminiscent of the DAR Council's cavalier treatment of similar contractor concerns expressed during consideration of the Contractor Business Systems regulatory revisions. And we all know how that turned out. (Poorly.)

One final example:

Comment: Two respondents stated that the rule will require contractors to establish multiple accounting costs bases and pools.

Response: This rule does not impose new cost accounting requirements. The IR&D cost

principle at Federal Acquisition Regulation (FAR) 31.205-18(b) states, 'The requirements of 48 CFR 9904.420, Accounting for independent research and development costs and B&P costs, are incorporated in their entirety. . . .' The cost accounting standard at 48 CFR 9904.420-40, Fundamental requirement, paragraph (a) states, 'The basic unit for identification and accumulation of IR&D and B&P costs shall be the individual IR&D or B&P project.'

In this final example, the DAR Council's response is seemingly based on utter ignorance of government contract cost accounting principles. Either that or the author of the DAR Council response is being deliberately obtuse and misleading. Why do we say that? Because the new rule requires the technical interchanges to take place *prior to IRAD costs being incurred*. Ergo, the costs of supporting the technical interchange are *not IRAD costs*.

All that arm-waving about CAS 420 is simply inapposite. It is wrong because the costs in question are not IRAD costs and thus they are not subject to the requirements of 31.205-18 or CAS 420. Anybody who spent more than 15 seconds thinking about the situation would never have responded in the manner the DAR Council did.

If the costs are not IRAD costs, then what are they?

Nobody knows.

Thus the basis of the concerns expressed by two commenters. Are the costs overhead? Certainly it appears that they cannot be direct costs. If they aren't IRAD project costs then they must be vanilla G&A or overhead. But from a purely beneficial or causal relationship point of view (i.e., a CAS point of view) the costs of conducting the technical interchanges are most directly associated with the IRAD projects that form the subject of the interchanges. But they can't be IRAD costs. Therefore we all have a quandary from a cost accounting perspective.

And this matters. It matters because some of the larger defense contractors have literally hundreds of individual IRAD projects, some large and others small (in terms of costs). The cost

of supporting technical interchanges, no matter how informal, may well run into the tens (or even hundreds) of thousands of dollars. If you put that cost into G&A or overhead, it gets allocated to all active customers. If you only sell to DoD, fine. But if you sell to multiple Federal agencies, you will end up with the civilian agencies paying for this unique DoD requirement. That doesn't sound right.

Thus, we are pointed toward some type of special pooling and allocation method, to make sure that DoD pays for its poorly thought-out requirement. *That* was the basis of the comments.

But the DAR Council ignored those valid concerns and so here we are.

The good news, the silver lining in this dark cloud of bureaucracy, is that the rule only applies to "major defense contractors," and if you are not one of them you can skate on by. The majors will figure this one out, and they will figure out how to stick DoD with the bill—as they always do. The small businesses, the ones that are not positioned to handle this rule, are not subject to it. That's the best nugget of news we can offer to our readers.

Otherwise, this rule is going to be problematic for those entities that are subject to it.