We can't pretend we were surprised to see this one hit the Federal Register.

Way back in September 2010, we **noted** that Under Secretary of Defense (AT&L) Dr. Ashton Carter published 23 "principal actions" he planned to take to drive "affordability" into defense programs, and among those 23 actions was to increase DOD's focus on contractor Independent Research and Development (IR&D or IRAD) spending so as "to improve the return on IRAD investments for industry and government."

At the time, we were concerned that the foregoing was code for "micromanage and reduce contractors' IR&D spending" though several colleagues thought we might be overreacting. Were we? You be the judge.

On March 2, 2011, the Federal Register **published** a proposed revision to the supplemental DFARS cost principles, that proposed to recreate the alleged "loss of linkage between funding and technological purpose" by requiring contractors with more than $50,000 in annual IR&D spending to report information to the Defense Technical Information Center. As the proposed rule states—

The reporting requirements, as mandated by 10 U.S.C. 2372, will provide in-process information from DoD-sponsored IR&D projects to increase effectiveness by providing visibility into the technical content of industry IR&D activities to meet DoD needs and promote the technical prowess of the industry. Without the collection of this information, DoD will be unable to maximize the value of the IR&D funds the Department disburses without infringing on the independence of contractors to choose which technologies to pursue in IR&D programs.

The proposed rule would revise DFARS supplemental cost principle 231.205-18 to read—

For a contractor's annual IR&D costs in excess of $50,000 to be allowable, the IR&D projects generating the costs must be reported to the Defense Technical Information Center (DTIC) using the DTIC's on-line input form and instructions. The inputs must be updated at least annually and when the project is completed. Copies of the input and updates must be made available for review by the cognizant administrative contracting officer (ACO) and the cognizant

Defense Contract Audit Agency auditor to support the allowability of the costs.

So contractors with more than $50,000 in annual IR&D costs may see those costs disallowed unless they provide DTIC with the required information at least once per year.

Looking at the cited **statute** , which allegedly enables the regulatory revision, we see a couple of interesting things.

First, we see the following—

(b) Costs Allowable as Indirect Expenses. - The regulations prescribed pursuant to subsection (a) shall provide that independent research and development and bid and proposal costs shall be allowable as indirect expenses on covered contracts to the extent that those costs are allocable, reasonable, and not otherwise unallowable by law or under the Federal Acquisition Regulation.

So the first thing we see is that the proposed regulation is establishing allowability criteria that are not sanctioned by the statute. Quite the contrary, in fact, since the statute expressly requires that allowability be established through determining (a) allocability, (b) reasonableness, and (c) compliance with the provisions of FAR cost principles.

That said, we also note that the statute does permit the Secretary of Defense to limit IR&D reimbursement by the DOD “to work which the Secretary of Defense determines is of potential interest to the Department of Defense.” In addition, the statute requires the Secretary of Defense to promulgate regulations that implement “regular methods of transmission … of information regarding progress by the contractor on the contractor's independent research and development programs.”

So to sum up, our point of view is that the statute permits (or requires) the Secretary of Defense to obtain contractor IR&D information “in a reasonable manner.” But the statute does not permit the DOD to make a contractor’s IR&D expenditures unallowable if it fails to comply.

As always, you can submit your comments to the DAR Council. The proposed rule (link above) explains how.