

## OFPP Recognizes *Bagley* Decisions as Proper Application of B&P Cost Rules to Proposal Costs Related to Teaming Arrangements

On June 16, 2006, the Office of Federal Procurement Policy ("OFPP") rejected industry's request that Federal Acquisition Regulation ("FAR") § 31.205-18 be clarified to address the holdings in *United States ex rel. Bagley v. TRW, Inc.*, 2000 WL 33400196, and *TRW, Inc.*, ASBCA No. 51530, 02-2 B.C.A. ¶ 31,944. These decisions held that teaming arrangements were "contracts" under FAR § 31.205-18, precluding the costs of proposal efforts required by such arrangements from being treated as bid and proposal ("B&P") costs. OFPP's position may result in contracting officers and auditors aggressively asserting, based on the *Bagley* cases, disallowances of costs that much of industry still classifies as B&P costs.

OFPP rejected industry's request to modify FAR § 31.205-18 to make it clear that teaming arrangements are not "contracts" for FAR § 31.205-18 purposes, finding the holdings in the *Bagley* cases "consistent with the intent of FAR § 31.205-18 . . ." OFPP, however, did not address the central issue of whether such teaming arrangements, like cooperative agreements, properly qualify as "contracts" for purposes of FAR § 31.205-18. The term "contract" is defined in FAR § 2.101 as "a mutually binding legal relationship obligating the seller to furnish the supplies or services . . . and the buyer to pay for them. It includes all types of commitments that obligate the Government to an expenditure of appropriated funds . . ." The teaming arrangements addressed in the *Bagley* cases, as well as the teaming arrangements that industry usually enters into, thus fail two tests for qualifying as a covered "contract": (1) no buyer pays for the proposal effort; and (2) no appropriated funds are expended pursuant to the terms of the teaming agreement. Thus, OFPP's position is wrong for the same reason that the *Bagley* decisions are wrong. Nevertheless, contractors now must be prepared to deal with the *Bagley* holdings.

Regarding proposal costs already incurred under teaming arrangements, contractors should maintain the position that such arrangements are not "contracts" and the costs of required proposal efforts are proper B&P costs. Regarding future teaming arrangements, and existing and prior arrangements, depending upon their terms, the recent decision in *ATK Thiokol, Inc. v. United States*, 68 Fed. Cl. 612 (2005), provides a basis to address the *Bagley* holdings, even assuming that teaming arrangements are contracts. In *ATK Thiokol*, the Court of Federal Claims held that research and development ("R&D") efforts are not required in the performance of a contract and, therefore, generate independent research and development ("IR&D") costs when: (1) the effort is not specifically required by a contract; (2) the effort is neither included nor intended to be included in the contract price or costs; and (3) the relevant Cost Accounting Standards ("CAS") Disclosure Statement permits treating the costs of such effort as indirect IR&D costs. Therefore, under *ATK Thiokol*, because proposal efforts result in B&P costs when, like R&D efforts, they are not required in the performance of a contract, careful drafting of teaming arrangements and CAS Disclosure Statements will support the allowability of proposal costs related to teaming arrangements, even if such arrangements are contracts.

Specifically, teaming arrangements that do not specifically require proposal effort and provide that each party will bear its own costs for any proposal effort should not be deemed to specifically require the effort. At most, the effort merely relates to the teaming arrangements. Under *ATK Thiokol*, however, mere relationship to a contract does not require direct charging when the relevant CAS Disclosure Statement provides that costs incurred in such circumstances are to be treated as indirect costs. Thus, contractors should ensure that teaming arrangements and CAS Disclosure Statements are drafted appropriately as a means to overcome the government's apparent embrace of the erroneous *Bagley* decisions.

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