THESIS

GUIDANCE FOR TRANSITIONING TO
PERFORMANCE-BASED SERVICE CONTRACTING -
A GUIDE FOR DEPARTMENT OF DEFENSE
FIELD CONTRACTING ACTIVITIES

by

Michael L. Renegar

June 2000

Thesis Advisor: David A. Smith

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**13. ABSTRACT (maximum 200 words)**
The objective of this thesis is to assess the transition from traditional service contracting to performance-based service contracting at Department of Defense Field Contracting Activities. There has been an increase in spending on services over the past decade that has forced the Federal Government to review its policy on service contracting. In 1991, the Office of Federal Procurement Policy established policy for the acquisition of services using performance-based contracting. Interviews of Government contracting personnel and review of professional literature highlight barriers to performance-based service contracting. These barriers are: management of cultural change, education and training of Government and contractor personnel, adoption of best commercial practices, writing of performance-based statements of work, and the tasks involved in contract administration. This thesis makes recommendations for overcoming these barriers and provides guidance for successful implementation of performance-based service contracting within the Department of Defense.

**14. SUBJECT TERMS** Service Contracting, Performance-Based Service Contracting (PBSC), Field Contracting Activities, Acquisition.

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GUIDANCE FOR TRANSITIONING TO
PERFORMANCE-BASED SERVICE CONTRACTING –
A GUIDE FOR DEPARTMENT OF DEFENSE
FIELD CONTRACTING ACTIVITIES

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The objective of this thesis is to assess the transition from traditional service contracting to performance-based service contracting at Department of Defense Field Contracting Activities. There has been an increase in spending on services over the past decade that has forced the Federal Government to review its policy on service contracting. In 1991, the Office of Federal Procurement Policy established policy for the acquisition of services using performance-based contracting. Interviews of Government contracting personnel and review of professional literature highlight barriers to performance-based service contracting. These barriers are: management of cultural change, education and training of Government and contractor personnel, adoption of best commercial practices, writing of performance-based statements of work, and the tasks involved in contract administration. This thesis makes recommendations for overcoming these barriers and provides guidance for successful implementation of performance-based service contracting within the Department of Defense.
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I. INTRODUCTION

A. PURPOSE

This thesis examines the management functions associated with performance-based service contracting and how they impact the administration of performance-based service contracts. This examination takes an in-depth review of the transition from traditional service contracting to performance-based service contracting and develops a model for performance-based service contracting that can be used as a guide by Department of Defense Field Contracting Activities.

B. BACKGROUND

Federal procurement spending has emphasized the acquisition of products, with services a distant runner-up. However, procurement has been plummeting in tandem with the Department of Defense's precipitously declining weapons system budget. In recent years, the Federal Government and the Department of Defense acquisition process has gone through a transition period characterized by a declining national defense budget and acquisition reform initiatives. In a report from the Office of Federal Procurement Policy
(OFPP), the Government spends about $200 billion annually through contracts. Services account for about $100 billion, or half of this total, and have steadily grown from an almost negligible amount during World War II. Historically, most of the federal statutes, policies, regulations, and attention directed at Government contracting were focused on the acquisitions of weapon systems and supplies, not services. As a result, the General Accounting Office (GAO) and agency Inspector General (IG) reports and Congressional hearings too often revealed problems surrounding service contracts. Some of the problems noted are: poor planning, inadequate definition of requirements that resulted in selection of less than optimal contract types and pricing arrangements, and lax or nonexistent contract administration that prevented the Government from obtaining best value for the money spent. Many Government agencies routinely contended with cost overruns, time extensions, and performance problems (U.S. Executive Office of the President, OFPP, May 1998).

In April 1991, OFPP issued Policy Letter 91-2 that established policy for the Government’s acquisition of services by contract. It emphasized the use of performance requirements and quality standards in defining contract requirements, source selection, and quality-assurance. This
approach provided the means to ensure that the appropriate performance quality level is achieved, and that payment is made only for services which meet contract standards.

Reforming the procurement process is one of the essential elements identified by the National Performance Review to increase the efficiency of the day-to-day operations of the Government. Contractors not only provide support to Government operations, but also are increasingly providing services directly to the public. The cost and performance of service contracts determine to a large extent how well agencies are able to fulfill their missions. Performance-Based Service Contracting (PBSC) can make a major contribution towards increasing the value of contracted services. In addition, PBSC is consistent with goals of the Government Performance and Results Act of 1993. While PBSC has been in existence for many years, it has not been widely adopted (U.S. Executive Office of the President, OFPP, May 1998).

C. THESIS OBJECTIVE

The primary objective of this research is to evaluate and analyze performance-based service contracting at Department of Defense Field Contracting Activities, and determine methodologies and trends that may lead to more
effective and efficient management of performance-based service contracts.

D. RESEARCH QUESTIONS

The primary research question is:

How can a Department of Defense Field Contracting Activity successfully implement an effective Performance-Based Service Contracting (PBSC) Program into its operational routine, given that no formal PBSC process exists while available resources will remain relatively constant?

The following are subsidiary research questions:

a. What is PBSC, and what constitutes effective PBSC?

b. What skills are necessary to conduct effective PBSC? What approaches to PBSC can be used to develop and enhance these skills?

c. What are the potential barriers that may be encountered when transitioning to PBSC?

d. What benefits can be realized as a result of implementing an effective PBSC program?

E. SCOPE OF THE THESIS

The scope of this thesis will include: (1) a review of the management of service contracts, (2) a review of
performance-based service contracting, (3) an evaluation of how to transition to performance-based service contracting, (4) discussion of the opportunities and barriers to performance-based service contracting, (5) development of a model to be used as a guide to implementing performance-based service contracting, and (6) discussion of how the Federal Government and Department of Defense can adopt commercial business practices to become more effective and efficient in performance-based service contracting.

F. METHODOLOGY

The methodology used in the thesis research will consist of the following steps:

1. Conduct a literature review of books, magazine articles, CD-ROM systems, Internet based materials, and other library information resources.

2. Conduct interviews either in person, or by telephone, with members of Government officials at Department of Defense Field Contracting Activities.

3. Review the management of performance-based service contracts, including acquisition reform initiatives, statutes, regulations, and policies.
4. Review the transition to performance-based service contracts, including acquisition strategy and plan, and contract methodology.

5. Prepare a summary and finding of fact of the advantages and barriers that impact the effective and efficient management of performance-based service contracts.

G. CHAPTERS AND CONTENTS

The thesis consists of six chapters. Chapter I is an introduction to the thesis and provides a detailed structure to the research methodology. Chapter II provides the reader with general information regarding service contracting and the administration of service contracts. Chapter II also discusses trends in service contracting and the statutes, regulations, and public policies associated with service contracting. Chapter III provides the reader with a background to performance-based service contracting (PBSC) including a discussion regarding the transitioning to PBSC and the potential barriers. Chapter IV presents the summary of interviews with Department of Defense Field Contracting Activity personnel and a review of performance-based service contracts. Chapter V provides the development of a PBSC model that may be used as a guide to PBSC. Chapter VI is
the conclusion, recommendations, answers to research questions, and areas for further research.
II. BACKGROUND ON SERVICE CONTRACTING

A. INTRODUCTION

This chapter provides the reader with background information concerning service contracting. It will provide an overview of the management and administration of service contracts. This chapter will include some basic definitions, statutes, regulations, and public policies associated with service contracting. This chapter will conclude with a discussion of current Federal Government and Department of Defense trends in service contracting.

B. DEFINITION OF SERVICE CONTRACTS

The Federal Acquisition Regulation (FAR) Part 37 provides general guidance for the acquisition and management of services by contract. The FAR defines a "service contract" as:

"...a contract that directly engages the time and effort of a contractor whose primary purpose is to perform an identifiable task rather than to furnish an end item of supply. A service contract may be either a nonpersonal or personal contract. It can also cover services performed by either professional or
nonprofessional personnel whether on an individual or organizational basis." (FAR, part 37.101)

There are a variety of different types of services acquired within the Department of Defense, from maintenance and repair services, to logistics transportation, and related services. Each of the services provided under the contract engages the contractor to expend time and effort in the performance of an identifiable task without providing a tangible end product. It should be noted that there is a clear distinction between goods and services. Goods are tangible (capable of being touched) while services are intangible (not capable of being touched).

a. Nonpersonal Service Contract

A service contract may be either a nonpersonal or personal contract. A "nonpersonal service contract" means a contract that provides for "the personnel rendering their services are not subject, either by the contract's terms or by the manner of its administration, to the supervision and control usually prevailing in relationships between the Government and its employees" (FAR, part 37.101).
**b. Personal Service Contract**

A "**personal service contract**" means a contract that "makes the contractor personnel appear, in effect, Government employees" (FAR, part 37.101).

The differences between "nonpersonal or personal" service contracts may be subtle, but Government contracting officials must clearly understand these differences. A personal service contract is characterized by the employee-employee relationship it creates between the Government and the contractor's personnel. The Government is normally required to obtain its employees by direct hire under competitive appointment or other procedures required by the civil service laws. Obtaining personal services by contract rather than by direct hire, circumvents those laws unless Congress has specifically authorized acquisition of the services by contract. Federal statute 5 U.S.C 3109 authorizes Government agencies to use personal service contracts under general contracting authority (FAR, part 37.104).

**C. CLASSIFICATION OF SERVICE CONTRACTS**

Classification is defined as "...the ordering or arrangement of objects into groups or sets on the basis of"
their relationships" (Sokal, 1974, p.1116). The results of these classifications facilitate a better understanding of the relationship based on observable or inferred properties of the groups or sets (Sokal, 1974, p.1116).

The Federal Government and the Department of Defense use a variety of methods for classifying goods and services. For the purpose of this research, the researcher provides an overview to the major general methodologies for generating service contract classifications.

1. Categories of Service Contracts by Order Class

Obligations for goods and services purchased by the Department of Defense are reported using the object class structure specified in Office of Management and Budget (OMB) Circular A-11. There are five major groupings of object classes in the circular: (1) personal services and benefits, (2) contractual services and supplies, (3) acquisition of assets, (4) grants and fixed charges, and (5) other. Defense contract services, as defined in the 1999 Defense Authorization Act, are a subset of the contractual services and supplies category (U.S. Executive Office of the President, (OMB), 1999). Specifically, contract services are those contracts included in the other contractual services object class – object class 25 (U.S. Executive
Office of the President, OMB Circular A-11, 1995). There are eight categories included under contract services. Table 1 provides a brief summary of the categories that classify which object class is used for accounting and tracking obligations for each procured contract service.

Table 1. Categories of Service Contracts

<table>
<thead>
<tr>
<th>Category of Service</th>
<th>Object Class</th>
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<tbody>
<tr>
<td>Advisory and assistance services</td>
<td>25.1</td>
</tr>
<tr>
<td>Other services (often called miscellaneous services)</td>
<td>25.2</td>
</tr>
<tr>
<td>Purchase of goods and services from Government accounts</td>
<td>25.3</td>
</tr>
<tr>
<td>Operation and maintenance of facilities</td>
<td>25.4</td>
</tr>
<tr>
<td>Research and development contracts</td>
<td>25.5</td>
</tr>
<tr>
<td>Medical care</td>
<td>25.6</td>
</tr>
<tr>
<td>Operation and maintenance of equipment</td>
<td>25.7</td>
</tr>
<tr>
<td>Subsistence and support of persons</td>
<td>25.8</td>
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</table>

Source: Office of Management and Budget Circular A-11

The object classes and categories listed in Table 1 provide a general description of the type of contract services procured by the Department of Defense. It is
intuitive that the Department of Defense contracts for better-defined services than those outlined by the broad categories of services by OMB Circular A-11. The eight categories of services acquired by the Department of Defense are more descriptively defined in the following summary (U.S. Executive Office of the President, OMB Circular A-11):

- Advisory and assistance services (object class 25.1). Services acquired by contract from nongovernmental sources to provide management and professional support; studies, analyses and evaluations; or engineering and technical services.

- Other services (often called miscellaneous services) (object class 25.2). Services not otherwise classified as either advisory and assistance services or any of the other service categories included under contract services.

- Purchases of goods and services from Government accounts (object class 25.3). Purchases from other Government agencies or accounts that are not otherwise classified. Includes rental payments to agencies other than the General Services Administration and interagency agreements from contractual services. Excludes, among other things, advisory and assistance services obtained through interagency contracts.

- Operation and maintenance of facilities (object class 25.4). Includes the operation and maintenance of facilities, when done by contract.

- Research and development contracts (object class 25.5). Includes contractor services for conducting basic and applied research and development.
Excludes research and development reported as advisory and assistance services for operation and maintenance of research and development facilities.

- Medical care (object class 25.6). Payments to contractors to perform medical care.
- Operation and maintenance of equipment (object class 25.7). Contractor services for operation, maintenance, repair, and storage of equipment, when done by contract. Includes storage and care of vehicles, storage of household goods, and operation and maintenance of information technology systems.
- Subsistence and support of persons (object class 25.8). Contractual services with the public sector or another Federal Government agency for board, lodging, and care of persons, including prisoners.

The classification of service contracts into eight broad categories allows the Department of Defense to plan for future budgetary requirements and provides a method for the type of service acquired to be measured against performance requirements.

a. Assignment of Costs to Service Contract Object Class

The question can be postulated, "Why is there a need to accurately assign costs associated with service contracts to the appropriate object class?" Congress has expressed significant concerns regarding the accurate assignment of obligated costs to the appropriate service
contract object class. In fiscal year 1998, the Department of Defense reported contract service costs totaling $90 billion. In that same year, Congress imposed a statutory limit on the percentage of total contract service costs that could be reported in the other services category (object class 25.2). This limit was set at 30 percent of the total contract service costs in fiscal year 2000 and at 15 percent in 2001 and thereafter (GAO/NSIAD-00-29). Figure 1 provides a detailed breakdown of the contract services costs reported by the Department of Defense in the object class 25 series during fiscal year 1998.
Figure 1. DOD's Reported Contract Services in Fiscal Year 1998

$26.9 billion
(object class: 25.3)

$17.1 billion
(includes object class: 25.4, 25.6, 25.7, 25.8)

$3.2 billion
(object class; 25.1)

$15.4 billion
(object class: 25.2)

$27.9 billion
(object class: 25.5)

Source: Federal Budget, fiscal year 2000

The descriptive classification of service contracts into the applicable object class provides Congress with insight to future allocation of budgetary funds within the Department of Defense. Figure 1 clearly shows $15.4
billion of costs were allocated and obligated to the Other Services (better known as miscellaneous services) object class 25.2.

In November 1998, the Department of Defense Comptroller provided guidance to the military services and Defense agencies on identifying and reporting contract service costs. This guidance provided specific directions as to the proper category (object class) in which these services should be reported (GAO/NSIAD-00-29).

2. Federal Acquisition Regulation

The Federal Acquisition Regulation (FAR) provides a general listing of some of the areas where service contracts may be used to acquire "nonpersonal or personal" services. The listing of FAR categories annotated below is intended to group services according to Federal statutes and regulations (FAR, 1999, parts 35-37, 39, 47):

(a) Maintenance, overhaul, repair, servicing, rehabilitation, salvage, modernization, or modernization of supplies, systems, or equipment.
(b) Routine recurring maintenance of real property.
(c) Housekeeping and base services.
(d) Advisory and assistance services.
(e) Operation of Government-Owned equipment, facilities, and systems.
(f) Communications services.
(g) Architect-Engineering.
(h) Transportation and related services.
(i) Research and Development.

These categories of service contracts represent a broad spectrum of services procured by the Federal Government as outlined by the FAR. Additionally, the FAR should by no means be the only regulating factor for categorization of service contracts, because it does not have jurisdiction over all aspects of Government contracting.

3. OMB Circular A-76

OMB Circular A-76 set forth guidance and procedures for determining whether commercial activities should be performed under contract with commercial sources or in-house using Government facilities and personnel. Certain functions are inherently Governmental in nature, being so intimately related to the public interest as to mandate performance only by Federal employees. It has been and continues to be the general policy of the Government to rely on competitive private industry to supply the products and services it needs. There are numerous services performed by
Federal employees that could be provided from a commercial source in the private industry. The following are examples of services performed by Federal employees that could be contracted from the private industry (U.S. Executive Office of the President, OMB Circular A-76, 1983, p. 7-10):

- Audiovisual Services
- Advisory and Assistance Services
- Automatic Data Processing
- Food Services
- Health Services
- Industrial Services
- Maintenance, Overhaul, Repair, and Testing
- Management Support Services
- Operation of Government-owned equipment, facilities, and systems
- Housekeeping and Other Services
- Printing and Reproduction
- Guard and Protective Services
- Special Studies and Analyses
- Transportation

This list of services should not be considered exhaustive, but includes examples of commercial activities currently contracted or operated in-house by Federal agencies. Contracts for research and development services are not covered under OMB Circular A-76.
4. Federal Supply Classification

The Federal Government categorizes listings for the classification of occupational services using the Federal Supply Classification (FSC). The FSC is a commodity classification that categorizes goods into groups and classes established by currently known items in the supply systems of the Federal Government. Presently there are 78 groups that are subdivided into approximately 700 classes. The primary basis for inclusion into one of the classes is the good's physical or performance characteristics. Items that are usually requisitioned or issued together or make up a related grouping for supply management purposes are included in the same class (DIOR/P07-95).

Table 2 represents categories of service contracts according to the appropriate FSC code and description (DIOR/P07-95):

Table 2. Summary of Service Codes

<table>
<thead>
<tr>
<th>Service Code</th>
<th>Description</th>
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<tr>
<td>B</td>
<td>Special Studies and Analyses - Not R&amp;D</td>
</tr>
<tr>
<td>C</td>
<td>Architect and Engineering Services</td>
</tr>
<tr>
<td>D</td>
<td>Automatic Data Processing and Tele Services</td>
</tr>
<tr>
<td>Code</td>
<td>Description</td>
</tr>
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<td>------</td>
<td>--------------------------------------------------</td>
</tr>
<tr>
<td>E</td>
<td>Purchase of Structures and Facilities</td>
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<td>F</td>
<td>Natural Resources and Conservation Services</td>
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<td>G</td>
<td>Social Services</td>
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<tr>
<td>H</td>
<td>Quality Control, Testing and Inspection Services</td>
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<tr>
<td>J</td>
<td>Maintenance, Repair, and Rebuilding of Equipment</td>
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<tr>
<td>K</td>
<td>Modification of Equipment</td>
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<tr>
<td>L</td>
<td>Technical Representative Services</td>
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<tr>
<td>M</td>
<td>Operation of Government-Owned Services</td>
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<td>N</td>
<td>Installation of Equipment</td>
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<td>P</td>
<td>Salvage Services</td>
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<td>Q</td>
<td>Medical Services</td>
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<td>R</td>
<td>Professional, Admin and Management Services</td>
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<td>S</td>
<td>Utilities and Housekeeping Services</td>
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<td>T</td>
<td>Photographic, Mapping, Printing and Publication</td>
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<td>U</td>
<td>Education and Training Services</td>
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<td>V</td>
<td>Transportation, Travel, and Relocation Services</td>
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<td>W</td>
<td>Lease or Rental of Equipment</td>
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<tr>
<td>X</td>
<td>Lease or Rental of Facilities</td>
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<tr>
<td>Y</td>
<td>Construction of Structures and Facilities</td>
</tr>
<tr>
<td>Z</td>
<td>Maintenance, Repair or Alteration of Real Property</td>
</tr>
</tbody>
</table>

Source: Directorate for Information Operations and Reports (DIOR/P07-95)
5. Standard Industrial Classification

The Standard Industrial Classification (SIC) methodology focuses on classifying products or goods according to the structure of the U.S. economy with each unit classified within a SIC representing a particular business establishment in the economy. The major purpose of the SIC was to provide a means for collecting, tabulating, and presenting statistical data related to the various business establishments (U.S. Executive Office of the President, OMB, 1987, p.11).

In the researcher’s opinion the SIC classifies business establishments based on the principal activity engaged and then appropriately places business units within these establishments at different manufacturing levels. The SIC provides a detailed listing to the principal products manufactured by U.S. industries.

D. ADMINISTRATION OF SERVICE CONTRACTS

Contract administration includes all relationships between the Government and the contractor that arise out of contract performance. It encompasses all dealings between the parties from the time the contract is awarded until the work has been completed, accepted, payment has been made,
and disputes have been resolved. As such, contract administration constitutes a large part of the activity in the Government process (Cibinic and Nash, 1995).

A comprehensive list of contract administration functions (see Appendix A) is provided in the Federal Acquisition Regulation (FAR) part 42.3. The FAR identifies over sixty normal contract administration functions, but it provides relatively little information regarding actual performance of work.

Stanley Sherman, Contract Management: Post Award, identified six broad categories of contract administration functions. Under each category, the functions are grouped according to the principal management objectives. Field contract administration offices normally perform some functions, while others are normally retained by the procuring activity awarding the contract. For example, adequately staffed Government procuring offices awarding contracts which are performed locally or which are highly specialized, may not assign any contract administration functions to a field contract administration office. Conversely, procuring offices with limited staff and a location remote from contract performance and administration may assign contract administration functions to a field contract management office that has the requisite skills and
resources to properly manage the performance of the contract (Sherman, 1987, p. 142).

The six broad categories of contract management responsibilities are as follows (Sherman, 1987, p. 142-143):

1. Monitoring and surveillance functions
2. Reports and services to procuring office and contractor
3. Reviews and audits of contractor internal management systems
4. Formal decisions and actions affecting contractors
5. Direction, negotiations, and agreements
6. Program-sensitive contract management functions

Contract management responsibilities in the Government are split between centralized procurement office and decentralized field contracting administration offices. Each of the contract management responsibilities, as they relate to service contracting, will be discussed below.

1. Monitoring and Surveillance Functions

Monitoring and surveillance functions for a service contract use the statement of work (SOW), called a performance work statement (PWS) in PBSC, and a quality assurance surveillance plan (QASP) that is developed before the contract was awarded. The SOW and QASP specify the
requirements for the contractor and set forth the internal procedures for Government technical surveillance of contractor performance. They are interdependent and must be tailored to meet the requirements of the Government as well as the surveillance and administrative capabilities for the service contract (Air Force Manual 64-108, 1994).

Contract managers at field contracting offices are called upon to perform a variety of monitoring and surveillance functions. The essence of the field administration job is to ensure that the contractor is performing the services in accordance with the contract (Sherman, 1987). A Contracting Officer's Technical Representative (COTR) and Quality Assurance Evaluator (QAE) assist the Contracting Officer with the administrative oversight related to subsequent monitoring and surveillance functions of the contractor's performance. The COTR and QAE are technically knowledgeable and professionally competent in the service for which they are responsible. They have experience in the area to be monitored that is sufficient to permit them to observe contractor performance and to determine whether the service does or does not satisfy the requirements of the contract.
The specific duties of a COTR are (Lesson Plan for COTR, 1979,):

- Ensure that services performed by the contractor remain nonpersonal in nature.
- Ensure that the contractor does not exceed the defined statement of work set forth in the contract. The contractor can perform those tasks only within the number of hours or time and dollars set forth for the performance of work.
- Monitor contract performance and to report all problems related to the contract to the Contracting Officer of record.
- Provide the Contracting Officer with a monthly report concerning contractor performance.
- Notify the Contracting Officer of any anticipated overrun of the estimated or ceiling price placed under the basic contract.
- Accomplish on-site surveillance and status reporting of performance of services in accordance with terms and conditions of the contract.
- Perform inspections and to certify or have certified acceptance or nonacceptance of work performed by the contractor.
- Monitor the use of Government-Furnished Material (GFM) and Equipment (GFE) by the contractor.

The duties and responsibilities of the QAE are synonymous with the COTR. The COTR and QAE are technical experts in the area of the service being provided and provide valuable insight to the monitoring and surveillance of the performance of the contractor.
2. Reports and Services to Procuring Office and Contractor

Field contract administrators are chartered to perform a number of services to support procurement activities and contractors. A principal duty is to conduct pre-award surveys, at the facilities, of contractors who are being considered for award of a Government prime contract. Full scale pre-award surveys require on-site visits at the prospective contractor’s plant or offices. An on-site visit may not be required if the contractor has recently been surveyed in connection with prior award competitions. The main purpose of this activity is to verify that the contractor has the necessary management, technical expertise, requisite facilities, and financial strength to perform the contract (Sherman, 1987, p. 150).

Field contracting offices administer the procedures for making payments that may vary depending upon the location of the payment office and the type of contract involved. The roles of the contract administration offices (CAO) and the contract auditor should be coordinated and efficient because actual payment depends upon their verification and authorization. The Prompt Payment Act, 31 U.S.C. 3901 requires (Cibinic and Nash, 1995):
Government payment of interest for delays in payment for a complete delivered item of property or service...the required payment date is stated to be the date of payment specified in the contract or thirty days after receipt of a proper invoice...if a specific date on which payment is due is not established by contract.

The basis for payments could be progress payments under fixed-price contracts, interim payments on cost-reimbursable contracts, payment of a contractual fixed rate in time-and-material and labor-hour contracts, liquidation of progress payments upon receipt of contract deliveries, final payments on fixed-price or cost-reimbursable contracts, and other methods of payments. A substantial part of the CAO's responsibility in the payments process is to withhold or reject a payment request if necessary.

One of the most active areas of financial and price management work of the CAOs is to evaluate the contractor's proposal. The field administration offices support new procurement actions as well as evaluate contract modifications and price analysis on contract proposals. CAOs need to have a certain level of technical expertise to conduct proper cost and pricing analysis to support the needs of management personnel at the procuring activity. CAOs are regularly called upon to review and evaluate prime contractors' proposed subcontracting plans for small
businesses and small disadvantaged businesses (Sherman, 1987, p. 151-153).

3. Reviews and Audits of Contractor Internal Management Systems

The reviews and audits of contractor internal management systems are comprehensive on large contractors that provide construction and equipment services. Field contracting offices want to verify and certify the contractor's cost/schedule control systems and their ability to effectively manage the process while performing the contract. Since many service contractors are small businesses and small disadvantaged businesses, the reviews and audits of the contractor internal management system may not be as comprehensive. Small businesses providing contract for services are still subject to periodic reviews and audits by the field contracting office. This is done to ensure that the Government obtains the needed work on time and that the contractor receives proper compensation in the performance of the contract (Sherman, 1987, p. 154-155).

4. Formal Decisions and Actions Affecting Contractors

The most important contract administration action affecting the rights of the parties is the contract change
notice. There are two classifications of changes. The administrative change is employed to bring about contractual updates or corrections, which have no substantial impact on the contractual rights of the parties. The field CAO or the procuring contract office (PCO) may issue administrative changes. Ordinary formal change orders are different. They have an impact on the contractor’s technical performance plus other elements of the contract such as pricing, and are usually not issued by field contract offices.

When disputes arise, internal coordination with all of the affected management personnel is essential. If the indicated action is a final decision of the contracting officer, the CAO must support making timely findings of fact and convey the decision to the contractor for acceptance or appeal at the contractor’s discretion.

Establishing billing rates and final rates for indirect costs is a requisite part of the administration of all contracts requiring determination of costs. Similarly, understanding of forward pricing rates for overhead is necessary for pricing agreements on all types of contracts. Under the FAR part 42.8, the contracting officer is authorized to disallow specific costs incurred or planned by a contractor. Actions in this area result directly from the CAOs monitoring the contractor’s cost of performance.
Contract administrative offices have been delegated the responsibility for implementing certain aspects of the Government’s cost accounting standards policy. First, the CAO determines the adequacy of the contractor’s disclosure statements to ensure that the accounting system is in compliance with the statement. Secondly, the CAO determines whether the statement is in compliance with the cost accounting policy.

Contract administrative offices play a major role in the decision-making for approval or disapproval of progress payment requests. This action is important to the capital position of the contractor. The CAO also has the contractual responsibilities for inspection and acceptance of services provided by the contractor (Sherman, 1987, p.155-158).

5. Directions, Negotiations, and Agreements

The procuring office ordinarily issues contract changes, but changes can be issued by CAOs with prior agreement and authorization from the procuring office. Issuing a change notice is the most significant action of a Government contract administrative official. Such notices alter agreements in a substantial manner and may involve sizeable cost changes and schedule adjustments.
Post-award negotiations focus on the major issues that tend to divide the contractor and the Government procuring activity. One purpose of post-award negotiations is to reach an agreement on contract price adjustments. Other post-award negotiation objectives include: forward pricing rate agreements, rate of expenditure and funding issues, and final pricing of incentives. Preparation for post-award negotiations is extensive and is a major workload factor at field contracting offices (Sherman, 1987, p. 158-159).

6. Program-Sensitive Contract Management Actions

Special attention must be given to those aspects of post-award management, which impact contract progress, cost, and success. The areas of greatest significance are: change orders or modifications, schedule adjustments, termination actions, acceptance of products or services, and adjustment of price or cost (Sherman, 1987, p. 160).

Contract changes or modifications are covered in the changes clause of the contract. This clause allows the Government to unilaterally make changes to the contract without consent from the contractor. The contractor is obligated to perform the change and will be provided an equitable adjustment for any additional incurred costs. FAR part 52.243 lists the types of modifications or changes
allowed to contracts that provide "nonprofessional and professional" services (FAR, Part 52.243).

E. STATUTES AND REGULATIONS

The Federal Government's ability to acquire supplies and services relies upon statutes, regulations and directives. These same statutes, regulations and directives also place constraints on the ability for the Federal Government to acquire supplies and services. There are literally hundreds of statutes and numerous pages of regulations and directives that control or affect the contracting process for acquiring supplies and services. The focus of this research is to concentrate on the acquiring of services and service related efforts.

1. U.S. Constitution

The Constitution of the United States is the supreme law of the land. It does not, however, specifically address whether the Government has the right to enter into contracts (Miller, 1999). The U.S. Constitution, Article I, Section 8, Clause 1, states (Bednar & Jones, 1987):

"1. The Congress shall have Power to lay and collect Taxes, Duties, Imposts and Excises, to pay the Debts and provide for the common Defense and general welfare of the United States."
Other clauses in Article I, Section 8 that provide statutory authority for the legal basis by which the Federal Government has the right to enter into contracts follow (Bednar & Jones, 1987):

"12. ...raise and support Armies..."
"13. ...provide and maintain a Navy,..."
"14. ...make Rules for the government and Regulation of the land and naval Forces;..."
"18. ...make all laws which shall be necessary and proper for carrying into Execution the foregoing Powers, and all other Powers vested by the Constitution in the Government of the United States, or in any Department or Officer thereof."

It was not until 1831 that the Supreme Court, in a "landmark" decision, United States v. Tingey, declared that the Federal Government has inherent power, based on sovereignty, to enter into contracts. Additionally, the Court decision declared that the Federal Government has implied powers, as necessary, for the proper performance of its duties (Federal Acquisition Institute, 1999).

2. Minimum Wages, Benefits, and Working Conditions

The Walsh-Healey Public Contracts Act prescribes minimum wage, hours, age, and working conditions for supply
contracts. The Walsh-Healey Act covers any contract entered into by any executive department of the Federal Government for the manufacture or furnishing of materials, supplies, articles, and equipment in any amount exceeding $10,000. Under the Walsh-Healey Act, all persons employed by the contractor in the manufacture or furnishing of the materials, supplies, articles, or equipment used in the performance of the contract will be paid no less than the prevailing minimum wages for persons employed on similar work of contractors currently operating in the locality in which the contract is to be performed (USC Title 41, Section 35).

The Davis-Bacon Act prescribes minimum wages, benefits, and working conditions of federal construction contracts in excess of $2,000. It requires a provision stating the minimum wages to be paid will be determined by the corresponding class and skill-level of the employee. These minimum wages will be based on the prevailing wage rates of employees on construction projects of a similar character being performed in the locality of the contract (USC Title 40, Section 276a).

The McNamara-O'Hara Service Contract Act of 1965 provides minimum wages, fringe benefits, and working conditions for service contracts for blue collar and some
white collar employees. Every contract entered into by the Federal Government in excess of $2,500 where the principal purpose is to furnish services through the use of service employees shall contain the following provisions (USC Title 41, 351):

- A provision specifying the minimum monetary wages to be paid the various classes of service employees...with prevailing rates for such employees in the locality, or, where a collective-bargaining agreement covers any such service employees...in no case shall such wages be lower than the minimum specified...

- A provision specifying the fringe benefits to be furnished in the various classes of service employees, engaged in the performance of the contract...fringe benefits shall include medical or hospital care, pensions on retirement or death, compensation for injuries or illness, life insurance, vacation and holiday pay, and other bona fide fringe benefits...

- A provision that no part of the services covered by the Act will be performed in buildings or surroundings or under working conditions...which are unsanitary or hazardous or dangerous to the health or safety of service employees engaged to furnish the services...

The Walsh-Healey Public Contracts Act and Davis-Bacon Act provided rate of wages, benefits, and working conditions
to protect the supply and construction employees. It was not until Congress passed and adopted the McNamara-O’Hara Service Contract Act of 1965 that service employees received similar protection.

3. OMB Circular (A-76) – Acquiring Services from Commercial Activities

In the process of governing, the Government should not compete with the private sector. The competitive enterprise system, characterized by individual freedom and initiative, is the primary source of national economic strength. In recognition of this principle, it has been and continues to be the general policy of the Government to rely on commercial sources to provide products and services to satisfy Government needs. Office of Management and Budget (OMB) Circular A-76 establishes Federal policy regarding the performance of commercial activities. The Circular sets forth procedures for determining whether commercial activities should be performed under contract with commercial sources or in-house using Government facilities and personnel (U.S. Executive Office of the President, OMB, 1983, p.1). Federal agencies have been encouraged to obtain commercially available goods and services from the private sector, if doing so is cost-effective.
Under OMB Circular A-76, it is the policy of the Federal Government to (U.S. Executive Office of the President, OMB, 1983, p.2-3):

- **Achieve Economy and Enhance Productivity.** Competition enhances quality, economy, and productivity. Whenever commercial sector performance of a Government operated commercial activity is permissible, comparison of the cost of contracting and the cost of in-house performance shall be performed to determine who will do the work.

- **Retain Governmental Functions In-House.** Certain functions are inherently Governmental in nature, being so intimately related to the public interest as to mandate performance only by Federal employees. These functions are not in competition with the commercial sector. Therefore, Government employees shall perform these functions.

- **Rely on the Commercial Sector.** The Federal Government shall rely on commercially available sources to provide commercial products and services. In accordance with the provisions of this Circular, the Government shall not start or carry on any activity to provide a commercial product or service if the product or service can be procured more economically from a commercial source.

A service contract is a contract that directly engages the time and effort of a contractor whose primary purpose is to perform an identifiable task rather than to furnish an
end item of supply or tangible product. A service contract may be either a nonpersonal or personal contract and may be performed by either professional or nonprofessional personnel, whether on an individual or organizational basis. Federal policy is to rely on the private sector for commercial services consistent with the Office of Management and Budget (OMB) Circular A-76 (Procurement Guide, 1998).

F. TRENDS IN SERVICE CONTRACTING

The trend towards the increased use of innovative service contracts in not the result of a single factor or overarching policy. Instead, it is the result of a political mandate for more efficient, scaled-down Government operations. On 1 April 1998, Secretary of Defense William Cohen submitted a report to Congress, “Actions to Accelerate the Movement of the New Workforce Vision.” The report identified several new initiatives, including one to increase acquisition workforce education. It stated,

“As the Department of Defense moves into the 21st century, the amount of goods DoD buys will be reduced. DoD will increasingly adopt the commercial practice of purchasing services instead of things. This will require the Department to change significantly the way it thinks about, and actually acquires, services. To implement effectively these changes, DoD will need to train the entire acquisition workforce, and those who establish requirements, on this new focus. DoD will also have to develop tools to facilitate the change in behavior, and the structuring of the acquisitions themselves.”
In that report, the Secretary directed formation of a team to develop training and tools, which focus on acquiring services. The training and tools will include guidance on purchasing services to meet needs (DoD, AF903T1, 1999, p.1).

The environment in which the Department of Defense acquires goods and services is the result of fiscal constraints that demand ever more efficient use of resources to adequately support the warfighter. It is the result of initiatives to increase civil-military integration by relying more effectively on the commercial sector to provide operational support to the Department of Defense. Most important, it is the result of security considerations that demand the maximum support of our warfighters through the best practices and the best technology available. All of these factors contribute to the increased use of innovative service contracting that allows the commercial marketplace to meet the Department of Defense needs. The overall trend can be characterized as having two major components - an increase in volume and complexity, and a shift in emphasis to performance-based methods (DoD, AF903T1, 1999, p. 11).

G. CHAPTER SUMMARY

The primary mission of the Federal acquisition system is to meet warfighter (customer's) needs. The vision of
meeting the customer's needs is paramount. The Department of Defense will be the world's smartest buyer, continuously reinventing the acquisition process while taking maximum advantage of emerging technologies that enable business process reengineering. The Department of Defense will procure best value goods and services by buying from world class suppliers in the commercial marketplace using commercial best business practices. Since the Department of Defense is buying on behalf of the U.S. taxpayer, acquisition strategies and methods will be fair, open, efficient, protect the public trust, supportive of the nation's socio-economic policies and composed of globally competitive U.S. suppliers.

The researcher provided a broad and descriptive background on service contracting. This chapter emphasizes how the Department of Defense is transitioning from spending large dollar figures on major weapon systems to spending more dollars acquiring services. Recent trends in contracting for services indicate a significant move towards performance-based service contracting. The Federal Government is shifting from telling the contractor "what service is required" and "how to provide the service" to identifying a required service and allowing the contractor
the latitude to decide the best commercial practice that can be used to perform the service.
III. PERFORMANCE-BASED SERVICE CONTRACTING (PBSC) -
NEW APPROACH TO CONTRACTING FOR SERVICES

A. INTRODUCTION

This chapter provides insight to the methodology of performance-based service contracting within the Federal Government and Department of Defense. It will provide an overview to the management and administration of performance-based service contracts. The chapter will include some basic definitions, statutes, regulations, and public policies associated with performance-based service contracting. The conclusion of this chapter is a discussion of current Federal Government and Department of Defense contracts for services using the performance-based methodology.

B. PERFORMANCE-BASED SERVICE CONTRACTING

Each year the Government contracts for a significant amount of services. Such services range from the routine maintenance of facilities or equipment to highly sophisticated technical and management assistance such as the design, development and furnishing of weapons systems, or expert assistance for management and program activities.
Attempts to apply contracting methods which are inappropriate to the services being acquired have often resulted in unsatisfactory performance and contract administration problems, as reflected in several internal agency investigations and evaluations, General Accounting Office (GAO) Reports, and Office of Federal Procurement Policy (OFPP) studies. Several of these reports criticized unnecessarily vague statements of work, and the inadequacy of quality assurance surveillance. In addition, there is concern that the Government underemphasizes "quality vs. price" in the acquisition of services (U.S. Executive Office of the President, OFPP, 1991).

In April 1991, the OFPP signed the effective service contracting policy that emphasized the use of performance requirements and quality standards. OFPP Policy Letter 91-2 is provided as Appendix B. Performance-based service contracting (PBSC) can be defined as "a contracting strategy for recurring services that emphasizes that the work to be performed should be defined in mission-related output terms, focusing on what needs to be done rather than how to provide the service" (U.S. Department of Transportation, Office of the Secretary, 1999). This contracting strategy significantly differs from the traditional service contracting method of telling the contractor what service
needs to be provided and providing a detailed method on how the contractor should provide the service to the procuring activity.


C. STATUTES, REGULATIONS, AND POLICIES EFFECTING PBSC

The statutes, regulations, and policies governing service contracting discussed in chapter two are applicable to performance-based service contracting. However, in the 1990s, the use of performance-based contracting for services has gained momentum in both the private and public sector. Additional statutes, regulations, and policies have been approved that have fostered a new acquisition method for providing best value to the customer using best commercial practices.

This law came into effect because of the downsizing initiative of the Federal workforce in the early 1990s. Public perception was that agencies were replacing lost employees with service contract workers. The Federal Workforce Restructuring Act states that "the President shall take appropriate action to ensure that there is no increase in the procurement of service contracts by reason of the enactment of this Act, except in cases in which a cost comparison demonstrates such contracts would be to the financial advantage of the Federal Government" (National Performance Review Report, 1996).

2. OFPP Policy Letter 92-1 on Inherently Governmental Functions

This policy letter establishes policy relating to service contracting and inherently Governmental functions. Its purpose is to assist Federal Departments and agencies in avoiding an unacceptable transfer of official responsibility to Government contractors.

Contractors, when properly used, provide a wide variety of useful services that play an important part in helping
agencies to accomplish their missions. Agencies use service contracts to acquire special knowledge and skills not available in the Government, obtain cost effect services, or obtain temporary or intermittent services.

Contractors may not perform all functions. It is clear that certain functions such as infantry and combat troops are inherently Governmental and may not be contracted. On the other hand, it is also clear that certain functions such as building maintenance, food service operations, and secretarial services are not inherently Governmental and may be contracted. The difficulty is in determining which of these services are or are not inherently Governmental (U.S. Executive Office of the President, OFPP, 1992).

3. OFPP Policy Letter 93-1 on Management Oversight of Service Contracting

OFPP issued Policy Letter 93-1 that established Government-wide policy, assigned responsibilities, and provided guiding principles for Executive Departments and agencies in managing the acquisition and use of services. One way to achieve excellence in contractor performance is to improve the acquisition, management, and administration of service contracts. This policy letter provides agencies with a more results-oriented approach to managing and
administering service contracts through the “best practices” concept (U.S. Executive Office of the President, OFPP, 1993).

4. OFPP Policy Letter 99-1 on Small Business

Procurement Goals

OFPP issued Policy Letter 99-1 which contains guidance on implementing government-wide goals for procurement contracts awarded to small businesses, HUBZone small businesses, small disadvantaged businesses, and women-owned small businesses. The goals for each of these small business categories are stated as a percentage of overall Federal procurement dollars. The policy letter also provides guidance on reporting requirements that will help the Small Business Administration (SBA) determine whether Executive Agencies are reaching these goals. This policy letter supersedes OFPP Policy Letter 91-1, “Government-Wide Small Business and Small Disadvantaged Business Goals for Procurement Contracts.”

1997 increases the annual Government-wide goal for prime contract awards to small businesses from, not less than 20 percent, to not less than 23 percent (U.S. Executive Office of the President, OFPP, 1999).

5. Federal Acquisition Regulation (FAR) part 37.6 -

Performance-Based Contracting

Federal Acquisition Regulation (FAR) part 37.6 prescribes policies and procedures for use of performance-based contracting. These methods are intended to ensure that required performance quality levels are achieved and that total payment is related to the degree that services performed satisfy the contract standards. Performance-based contracts - (FAR, part 37.6)

(a) Describe the requirements in terms of results required rather than the methods of performance of work;

(b) Use measurable performance standards (i.e., terms of quality, timeliness, quantity, etc) and quality assurance surveillance plans;

(c) Specify procedures for reductions of fee or for reductions to the price of a fixed-price contract when services are not performed or do not meet contract requirements; and
(d) Include performance incentives where appropriate.

D. TRANSITIONING TO PERFORMANCE-BASED SERVICE CONTRACTING

Reform of defense management and acquisition has a long history. Department of Defense began its current efforts to reform acquisition in 1993 through the application of the Federal Acquisition Streamlining Act (FASA). It focused its initial attention on making Department of Defense's largest acquisitions - the design, development, and production of weapon systems - more performance based. In the next couple of years, it turned to improving the acquisition of support services for major weapon systems. By 1998, the Department of Defense turned its attention to performance-based acquisitions for base installation support services (DoD, AF903T1, 1999, p.17).

The trend towards the increased use of innovative service contracts is not the result of a single factor or overarching policy. Instead, it is the realization of economies of scale by aggregating services that were previously contracted out individually. Historically, commercial and Department of Defense practice relied on a simple, arm's-length approach to acquire services. The
customer would specify exactly what it wanted in a detailed statement of work (SOW), often including instructions on how the work would be performed. The customer would then hold a competition and select a source based almost entirely on the relative costs of offerors. It would then pick the low-cost provider that demonstrated a threshold level of technical capability and then would rely on close oversight to ensure delivery of the services needed. This "outtasking" approach to acquiring services often led to a "bid-and-bash" acquisition regime, dominated by driving cost down and then bashing the supplier to demand delivery.

During the last two decades, a growing number of commercial firms have discovered that they can get better, faster, and cheaper performance by developing longer term relationships with providers. These partnerships use an entirely different acquisition approach. Customers determine strategically that an outside supplier is better than they at satisfying their needs in a particular service area. These customers then seek a supplier who can satisfy these needs. The customers focus on their strategic needs in a particular service area and the supplier determines how to provide the service (DoD, AF903T1, 1999, p. 11-16).
The use of a performance-based approach to service contracting requires the customer and supplier to critically analyze three important factors (DoD, AF903T1, 1999, p. 16):

1. **Defining the service the customer wants performed.**
   The customer and potential suppliers work together to define the performance relevant to the customer's needs. This requires an initial discussion and then follow-on discussion of how to measure performance to ensure the supplier knows what the customer wants performed.

2. **Selection of a supplier for the service required.**
   The customer seeks performance measures it can use to choose a supplier who is likely to make a sound business partner over the long term. It uses a source selection process focused on past performance rather than on current or historical cost. Suppliers maintain performance data that they expect potential customers will value in source selection to distinguish themselves from other suppliers.

3. **Incentivize the supplier to improve its performance relative to the customer's needs.**
   After source selection, the customer and supplier work together to measure their joint performance
and allocate between themselves the gains that come from improvements over time. Many things can help motivate a good supplier. The customer rewards performance by extending the length of a contract or reducing Government oversight on the performance of the contract. Both of the methods reduce the customer's and the supplier's administrative costs. The customer may also expand the activities that a supplier provides.

The use of best commercial practices can enhance the delivery and effectiveness of services acquired through performance-based contracting. Performance-based contracts for services that maintain quality at fair and reasonable prices are one technique that the Department of Defense can use to integrate and leverage best commercial practices. The benefits of performance-based contracting have been demonstrated in the private sector. On the contrary, it is too early to document the actual effects of the Department of Defense's efforts to use performance-based service contracting (DoD, AF903T1, 1999. p. 20-21).
E. POTENTIAL BARRIERS TO PERFORMANCE-BASED SERVICE CONTRACTING

Performance-based service contracting requires a fundamental shift in how the acquisition and requirement communities manage the acquisition process. Rather than focusing on how a supplier performs the service, the procuring activity needs to think of what the customer values in the services. Then the Department of Defense must state the values in clear, documentable performance terminology. The procuring activity should pay more attention to the customer’s actual service requirements than spending valuable time studying the details of a traditional service requirement. A performance-based approach to contracting for services is different from the Department of Defense’s traditional approach. It is tailored to the circumstances at hand to give the customer what is desired. It often requires finding ways to review inherently subjective requirements in objective performance measures. As the Department of Defense moves in this direction, its acquisition workforce will benefit in changing the culture and developing a new mindset.

Through a review of professional literature, the researcher identified barriers that the Department of
Defense has to overcome as it transitions from traditional service contracting to performance-based service contracting. As previously stated in the above paragraph, the Department of Defense acquisition workforce needs to develop and adopt a new cultural mindset. The old way of doing business needs to change and the acquisition workforce needs to understand and accept the new performance-based acquisition approach to service contracting.

Other barriers to the successful transition to performance-based service contracting are (DoD, AF903T1, 1999, p.40):

- Identify Skills/Resources Required for Performance-Based Acquisitions
- Adoption of Best Commercial Practices
- Writing of Performance-Based Statements of Work
- Contract Administration

The acquisition workforce needs to think about the skills relevant to service acquisitions. The acquisition workforce must become less inward-looking and more outward-looking. Individuals must think less about complying with the specific regulations or procedures maintained by their functional specialties and more about improving the performance of their ultimate customers. They can no longer
be content with acquisition practices that worked in the past. They must constantly seek new ideas from other parts of the Department of Defense and the commercial industry. They must increasingly identify ways to entice the best commercial firms to sell services to the Government (DoD, AF903T1, 1999).

The adoption of best commercial practices must be overcome to successfully transition to performance-based service contracting. The Department of Defense is working to capture the best the commercial industry has to offer and fully apply it to meeting military needs. The Department of Defense is achieving this by breaking down barriers to the use of common processes and facilities, by encouraging the maximum use of commercial items, subsystems, and components in defense systems, and by incorporating the use of best commercial practices in all defense operations (DoD, AF903T1, 1999).

The performance-based statement of work (SOW) is the foundation of performance-based service contracting. A performance-based SOW describes the required outcomes of the services sought and provides criteria for measuring and verifying performance, but it does not dictate the specific methods that must be used to achieve those outcomes. The key aspects of a performance-based SOW include:
• A description of the expected output or outcomes.
• A statement expressing the performance characteristics.
• A definition of the environment in which the services are to be performed.
• Measurement criteria that permit both contractual parties to gauge actual versus expected performance.

The performance-based SOW specifies measurable performance outcomes (outputs) that are derived from a thorough job analysis. This analysis requires the customer to identify and analyze the job output task by task. From these outputs, the customer develops measurable performance outcomes that include appropriate quality levels (DOD, AF903T1, 1999).

The key to contract administration is to develop an acquisition strategy that mitigates risk and states the contract requirements in performance terms. A Quality Assurance Plan (QAP) is the embodiment of this strategy. The QAP outlines the roles and responsibilities of the parties involved to guarantee that service delivery proceeds in accordance with the performance outcomes designated in the performance-based SOW. In effect, the QAP is a roadmap to ensure that the Government receives quality services as
specified in the contract and pays only for services rendered at or above the acceptable level (DOD, AF903T1, 1999).

The identified barriers cover the entire spectrum of performance-based service contracting from "cradle to the grave." The success of overcoming these barriers should accomplish the field contracting activity's main mission of providing quality support and services to the warfighters better, faster, and cheaper.

F. CHAPTER SUMMARY

In the last decade, the Department of Defense has made a significant move from the traditional service contracting method of telling the contractor "what" and "how" to provide the service to a performance-based contracting method. Current Federal Government policy, OFPP 91-2, suggests that (1) agencies use performance-based contracting methods to the maximum extent when acquiring services, and (2) agencies carefully select acquisition and contract administration strategies, methods, and techniques that best accommodate the requirements.

The researcher identified barriers from the literature review that must be managed to successfully transition from traditional service contracting to performance-based service
contracting. It is too early in the transition period to quantitatively measure the effects of performance-based service contracting. Department of Defense agencies have been reluctant to change and have been slow to implement performance-based acquisition policy.
IV. PERFORMANCE-BASED SERVICE CONTRACTING (PBSC) AT FIELD CONTRACTING ACTIVITIES

A. INTRODUCTION

This chapter presents data gathered from interviews which have been conducted face-to-face, by telephone, and through electronic mail. These interviews have been conducted with military and civilian personnel involved in the area of performance-based service contracting at various Department of Defense Field Contracting Activities located in the San Diego region, including Hawaii and Washington State. The researcher, prior to conducting the interviews, informed the interviewees of the purpose of the interview and that their responses would not be subject to attribution.

The interviewees were given a list of questions (Appendix C) in advance to allow time for preparation and to gather information, if needed. The interview questions were based upon the literature review conducted in Chapters II and III. The face-to-face interview sessions were conducted at the interviewee’s respective activity, either one-on-one or in a roundtable discussion. Telephone and electronic mail interviews were conducted when the Government
acquisition person and the researcher were unable to schedule face-to-face interviews. Some Government acquisition professionals were located at activities outside of the San Diego region. A total of 27 interviews were conducted. The views and opinions of these interviews are presented in this chapter as responses to the questions related to performance-based service contracting. The researcher follows-up each response with an analysis of the responses collected.

B. RESPONSES AND ANALYSIS

1. Question One

What are the potential barriers that may be encountered with the administration of PBSC? What procedures and practices have you implemented to overcome barriers associated with PBSC?

a. Interview Results and Discussion. This question was designed to determine what barriers exist with the administration of performance-based service contracts. It also looked for "best practices" that were being implemented by contracting activities to overcome these barriers. The following is a list of barriers identified by the respondents in performance-based service contract administration:
1. The lack of training and skills in the Government workforce.

2. The inability to write performance-based Statements of Work (SOWs); SOWs are vague and poorly written.

3. The need to change the cultural mindset on how to acquire services within the Department of Defense.

4. The lack of control due to consolidation and regionalization efforts.

5. The adoption of best commercial practices.

6. Small businesses require a significant amount of Government oversight.

7. The lack of planned requirements requires more personnel for surveillance.

Some typical responses received are paraphrased below:

The number one barrier is training. This means training for the customer, contracting personnel, and private contractors.

There is not a clear, understanding of the true definition of performance-based service contracting. If one looks closely, the majority of service contracts have significant Government oversight and payments are based on service rendered (performed).

Effective contract oversight is a major barrier to performance-based contracts. The notion of allowing the contractor to provide the service with little oversight is not a true statement.

The responsibility for inspection is seldom a full-time position. This is directly related to the downsizing of the Government workforce. Many Government employees perform two or more job functions within their activity.

Changing the culture is probably the most difficult task of management. It is easier to just do it the way
it was before this new policy was drafted. Why change if it is not broken?

Contract administration in PBSC requires a significant amount of documentation. If the contractor is performing in accordance with the contract, then there is no problem. It is when performance is subpar that contract administration becomes a nightmare.

Many of the service type contracts are 8-A set-asides for small businesses which usually require more guidance and direction from the Government.

Government and contractor personnel do not have the skills and resources to properly administer performance-based contracts.

It is difficult to identify service requirements with discrete measurable performance objectives. Statements of Work (SOWs) are vague and poorly written.

Quality Assurance Evaluators (QAEs) still want to instruct the contractor on how to perform the service. Several of the respondents stated that many of the contractors also wanted to be instructed on how to do the job.

To determine how the interviewers are responding to these barriers, the researcher asked “what procedures and practices have you implemented to overcome barriers associated with PBSC?” Several of the respondents stated that they have not implemented any procedures to overcome the barriers associated with performance-based service contracting. The main reason is because contracting for services using the performance-based method is a relatively new acquisition approach. Other responses received are paraphrased below:
We use the TEAMING approach to identifying the tasks, writing the performance-based SOW, and outcomes for measuring performance.

The contracting activity submits a draft request for proposal (RFP) as a market research tool to determine how the service will be performed.

The contractor submits a Quality Control Plan where the Government activity validates and approves the contractor's processes.

b. Analysis. The interviews with Government contracting personnel identified many barriers and concerns with the administration of service contracts using the performance-based approach. The most common barriers identified by the majority of the respondents were:

- the lack of skills and training to administer performance-based service contracts
- inability to write measurable performance work statements
- the need to change the cultural mindset of the individuals involved in the process.

These barriers are addressed in greater detail in the following paragraphs.

The acquisition reform initiatives in the past decade have drastically changed the way Government acquires services. The personnel interviewed for this study are extremely professional and knowledgeable in Government contracting with a wide breadth of experience. The
professionalism, knowledge, and experience are warranted attributes of the Government acquisition workforce. These contracting professionals understand the barriers which they must overcome in order to successfully implement policies established to streamline the acquisition process. The researcher believes that the Government acquisition workforce has not received the proper training, nor has the resonant skills to adequately implement performance-based service contracting. The tendency within Government is to establish a policy before properly training the workforce in the implementation of the policy. Based on the literature review, training courses need to be developed specifically for the successful implementation of performance-based service contracting. The following course outline was designed in a Department of Defense report (DoD, AF903T1, 1999):

1. Overview of Performance-Based Services
2. Gathering Market Data
3. Benchmarking Best Commercial Practices
4. Developing Performance Standards
5. Reconciling Customer Needs with DoD Regulations
6. Writing a Performance-Based Statement of Work and Quality Assurance Plan
7. Identifying Potential Problems
8. Managing a Partnership under Normal Conditions
9. Reacting to a Significant, Unanticipated Problem
10. Closing Discussion and Summary

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The researcher believes there should be a greater emphasis placed on providing the acquisition workforce with the skills and resources that will enable them to perform their jobs more efficiently and effectively.

There appears to be an inability to properly write performance-based service requirements. The customers know what type of services they want performed, but have difficulty writing the requirements so that the contractor’s performance can be measured. The researcher expected this barrier since the majority of the literature reviewed on service contracting discussed procedures on how to write effective performance statements of work.

There is a need for training the personnel involved in the acquisition of performance-based services. One of the focuses should be on accurately identifying the requirements and applying measurable performance outcomes that can be monitored.

The ability to change the cultural mindset of the individuals involved in the acquisition workforce is a shift necessary to manage performance-based service contracting. Changing cultures is easier said than done. Most organizational cultures have long-standing histories and resist change. In the opinion of the researcher, the
individuals interviewed understand the need for cultural change and know that change takes time.

The contracting personnel interviewed may not have enough experience in performance-based service contracting to effectively develop and implement practices which may overcome the barriers to performance-based service contracting. This may also be a reflection of adopting commercial "best practices". Change is sometimes difficult and it takes time to understand the new performance-based service acquisition approach. The practices being implemented to overcome the barriers to performance-based service contracting follow sound business decisions used within the Department of Defense. The TEAMING approach to acquiring service can be thought of as an integrated performance team (IPT). All members of the TEAM have a vested interest in acquiring quality services. If the tasks and outcomes are identified accurately, then administration oversight may be reduced.

Several of the contracting activities have adopted best commercial practices by allowing the contractor to submit in the draft request for proposal (RFP) how they will perform the service. Additionally, the Government is allowing the contractor to submit their own Quality Control Plan. Both of these practices foster innovation and creativity by the
contractor. In return, the customer may receive quality services using the most advanced technology with minimal oversight from the Government.

c. Question Summary. The most common barriers identified by the majority of the respondents were:

- the lack of skills and training to administer performance-based service contracts
- inability to write measurable performance work statements
- the need to change the cultural mindset of the individuals involved in the process.

The stated practices being implemented to overcome these barriers are:

- use of integrated performance teams (IPTs)
- submit a draft request for proposal (RFP) and use it as a market research tool
- request the contractor submit a Quality Control Plan.

In order to fully implement a successful performance-based service contracting program, all parties involved in the acquisition need to understand how the process works. Based on the literature review and information collected during the interviews, the following areas should be
covered: develop a performance-based acquisition strategy, develop a teaming arrangement, a clear understanding of the service requirement, the ability to measure the performance objectives, a quality control plan for surveillance, an acquisition strategy, and a contract administration plan. The researcher believes that the guidance for implementing performance-based service contracting outlined above should provide a solid foundation for building a successful program.

2. Question Two

What benefits can be realized as a result of implementing an effective PBSC program?

a. Interview Results and Discussion. This question was developed to determine where field contracting activities have benefited from implementing performance-based contracting. Most of the respondents stated that performance-based contracting has allowed for the adoption of best commercial practices. This was noted as a barrier in question 1, however, many respondents felt that the contractor knows the service business better than the Government. Several respondents stated that adopting commercial "best practices" for service contracting promotes innovation and creativity from the contractor and provides
better quality services to the customer for a fair and reasonable price. Respondents stated that the following benefits could be realized through the effective implementation of performance-based service contracting:

- Receive better quality services performed at a lower price
- Learn commercial industry standards for performance of services
- Reduced Government oversight during contract administration.

Paraphrased comments from respondents are presented below:

In an effective PBSC program, you open the door for the most up-to-date processes available in industry rather than tying yourself to "the way we always did it."

Too often in Government, we are not sufficiently educated on what is going on in private industry.

By dictating the method of performance, and not knowing if this is the current technology, the Government could actually be spending more for services and receiving subpar quality.

Contractors stay on top of current technology through trade associations. Achieving a competitive advantage is a major asset in private industry.

Performance-based contracting allows for supplies and services to be acquired cheaper (at a better price) and faster.

Too early in the ballgame, only a few contracts have been awarded using the performance-based approach.
Socio-economic goals are more easily achieved as small businesses enter into the competition for service contracts.

b. Analysis. There is no single ideal approach for performance-based service contracting. Each Government agency must design each contract around how best to satisfy the Government’s needs for each acquisition.

In many cases, the contractor knows the service business better than the Government. Performance-based service contracting allows the contractor the latitude to be creative and innovative in how to perform the acquired service. The researcher believes that the majority of contractors want to be efficient and effective in the services performed. This suggests service contractors will always be looking to improve the processes used and seek new technology that can benefit all parties involved. The incentive is two-fold: the contractors improve the quality of performance and the Government obtains services based on the most current process and technology available. The creation of a “win-win partnership” between the customer, the contracting activity, and the contractor is paramount to an effective performance-based service contracting program.

Several of the respondents stated that the Federal Acquisition Streamlining Act of 1994 (FASA) initiated the change that provided flexibility and innovation to how the
Federal Government acquires services. This Act promotes the acquisition of commercial items and services. From this Act, three parts of the Federal Acquisition Regulation (FAR) were revised to implement the preference for the acquisition of commercial items and services. The revised parts are: Parts 10, Market Research; 11, Describing Agency Needs; and 12, Acquisition of Commercial Items. The researcher's summation of the revised parts is that contracting activities need to conduct extensive market research to determine if a commercial service is available to fulfill the requirement. If the service is available commercially, then the activity must acquire the service using commercial terms and conditions. This supports the adoption of best commercial practices.

c. Question Summary. The following benefits could be realized through the effective implementation of performance-based service contracting:

- Receive better quality services performed at a lower price
- Learn commercial industry standards for performance of services
- Reduced Government oversight during contract administration.
3. Question Three

Can you explain what contract types are best suited for PBSC? Why?

a. Interview Results and Discussion. The purpose of this question was to determine if a particular contract type provided the Government and the contractor with a more successful outcome in performance-based contracting. The majority of the respondents believed that the selection of the appropriate contract type would influence performance-based service contracting. However, these same respondents also stated there is a direct relationship between the selection of contract type and the performance of the contractor. The firm-fixed price (FFP) contract type received the most positive responses. Additional comments are paraphrased below:

Only issue fixed price contracts. This places the risk on the contractor to perform in accordance with the contract. If the contractor knows the business well, then he should be rewarded.

Over 90% of the contract actions are firm-fixed price.

Use a variety of contract types, it depends on the complexity of the requirement and the risk to the contractor.

Depending on the nature of the requirement, the normal contracting method is with a firm-fixed price contract. However, there have been requirements that justified using a cost reimbursable contract with an award fee (CPAF).
On one complex service contract, some of the requirements were difficult to identify and provide measurable standards. To support PBSC, we used a hybrid contract, part FFP and part CPAF.

Multiple Award Service Contracts (MASC) are in the infancy mode. More fact-finding needs to be conducted.

b. Analysis. Selection of the appropriate contract type during the acquisition phase can mitigate the risk to both the Government and the contractor. Most respondents selected the firm-fixed price (FFP) contract when the requirement could be accurately defined in performance objectives. This should come as no surprise since the majority of the literature reviewed advocated the use of FFP contracts for performance-based contracting. Firm-fixed price contracts are used for performance-based contracting because the majority of services acquired at the Government activities are not complex and commercial in nature.

The performance-based services acquired using a FFP contract are usually for a base year plus option years. The majority of the time the option years are exercised because of the time and effort it takes to go through the acquisition process. Selection of the right contractor and the appropriate contract type should improve contractor performance and mitigate contract risk.
Many of the performance-based contracts are for services such as: janitorial, lawncare, maintenance, food service, sanitation, etc. The requirements are easy to identify and quality performance outcomes can be objectively measured in accordance with the contract surveillance plan. The opinion of the researcher views the FFP contract as a commonsense business decision for developing a trusting and honorable relationship with the contractor while maintaining an arm's length relationship. This promotes quality performance and profit incentives for performance-based service contracting.

FFP contracts should not be the only contract type used in performance-based contracting. Depending on the nature of the requirement, it may be best to select a contract type that will mitigate the risk associated with the performance-based requirement. A small percentage of the respondents stated that cost-reimbursable (CR) type contracts were used when the customer could not accurately match the performance statement of work with applicable measures of performance. The researcher believes that the contract type should be associated with the risk involved in the acquisition. In order to reward the contractor for accepting greater risk, an incentive could be added to the contract. This incentive could reward the contractor for
completion of services ahead of schedule, sustained superior performance, or sharing savings incurred by using more efficient processes to perform the service.

Several of the respondents discuss the use of indefinite quantity type contracts. These contract types were selected when the customer knew the requirement was going to happen but did not know the frequency. A good example for this type of contract would be for a change of command or a visit from a high ranking official or diplomat. The services would be required on short notice and the frequency would be highly uncertain.

One respondent discussed the use of Multiple Award Service Contracts (MASC) for the performance of services in a geographical area. The contracting activity may make multiple awards for similar services to two or more services. The researcher believes that these types of contracts are similar to bundled contracts or consortium type purchasing arrangements. These types of purchasing arrangements provide incentives that promote the acquisition of larger quantities, improved contractor performance through competition, and commercial marketplace will establish the prices for the services being acquired.

There are a variety of contract types that can be used for performance-based contracting. The best contract type
to select is the one that will ensure successful performance in the completion of the contract. A win-win situation between the contracting activity and the contractor most certainly enhances the success of the acquisition process.

c. Question Summary. Selection of the appropriate contract during the early stages of performance-based service contracting may mitigate risks during the performance of the contract. The following are possible contract types for performance-based service contracting:

- Firm-fixed price (FFP)
- Cost reimbursable (CR) with incentives (CPIF and CPAF)
- Multiple Award Service Contract (MASC)
- Indefinite Delivery/Indefinite Quantity
- Hybrid type (a mix of FFP and CR)

4. Question Four

What improvements (laws, regulations, and policies) would you like to see added/changed that would make PBSC administration more effective and efficient?

a. Interview Results and Discussion. The laws, regulations, and policies that govern Federal Government contracting continue to grow and change every year. The purpose of this question was to identify particular laws,
regulations, and policies associated with performance-based service contracting administration that were a hindrance or positive influence on performance-based service contracting. All respondents stated that the laws and regulations governing the acquisition process protect all parties involved, and no improvements/additions would significantly impact performance-based service contracting.

A few of the respondents did comment that the policies pertaining to the socio-economic and small business goals need to be re-evaluated. Many of contracts for services have small business set-asides that require the contracting activity to notify Small Business Administration (SBA) when the service is up for solicitation and award.

b. Analysis. Performance-based service contracting is achievable in light of no significant legal or regulatory barriers. The respondents did comment on two important issues that effect the administration of performance-based service contracts. These are: socio-economic and small business goals. Several of the respondents stated that service contracts predominately are awarded to small businesses, small women-owned businesses, and small disadvantaged businesses.

Also, National Industries for the Blind (NIB) and National Industries for the Severely Handicapped (NISH)
impact the ability to manage performance-based service contracts. Laws mandating that Government agencies acquire services that support the socio-economic goals of the elected Government officials have created an artificial inefficient process in the acquisition system. The overall performance of these contractors may be effective and the customer is satisfied, but the negative aspect of these goals may be that the Government pays a premium price for acquired services. Additionally, the quality may be satisfactory but the contractor may not be using the most current process and technology available.

c. Question Summary. The current laws and regulations do not impede the implementation of performance-based service contracting.

5. Question Five

What skills/training requirements are necessary to effectively transition to PBSC? Have resources been made available to satisfy these requirements in the implementation of PBSC?

a. Interview Results and Discussion. The Government acquisition workforce has a mandate that each acquisition professional must receive 80-hours of training in a two-year period. The training may or may not be related to the acquisition field in which the Government employee is
associated. The purpose of this question was to stimulate responses from the personnel interviewed regarding specific training requirements that would enhance the transition to performance-based service contracting. A basic response from all respondents was “contracting officials have not had enough training.”

The majority of the respondents identified the need for training on the writing of performance statements of work. The customer knows the type of service needed but fails to accurately communicate the requirement in the performance statements of work. Specific skills and training requirements noted during interviews with the acquisition workforce are:

- contract administration - monitoring and surveillance of the contractor.
- teamwork - developing integrated performance teams (IPTs).
- negotiations - creating “win-win” situations for all parties involved in the acquisition process.
- quality assurance plan - identifying measurable performance objectives.
• market research - searching and identifying commercial "best practices" for providing the services.
• communications - creating open channels to communicate the needs of the customer to the contractor.

Respondent comments are paraphrased below:

The most important skills are the ability to write and communicate effectively. For the most part, we struggle through this problem.

In many cases, the individual’s ability to interpret the contract and apply it to the situation is lacking.

Workforce has decreased and the workload has increased. There is a need to understand fully the best practices to contracting. This means continuous training.

The responsibility for oversight of a contract is an additional duty. Training for a secondary job function does not exist.

Government contracting personnel, customers, and contractors need training on how to write performance work statements.

The end-user needs to be able to relate the required outcomes to measurable performance objectives.

B. Analysis. The use of contracts for services has steadily increased over the past decade. Acquisition reform initiatives have changed the way Government contracting activities acquire services. The commercial sector strives to improve the processes used in performing the service as technology continues to advance. The researcher believes
that the acquisition workforce needs to have acquisition refresher training sessions each year. These acquisition refresher-training sessions should reinforce the acquisition principles and guidance that creates more effective and efficient acquisition personnel at each contracting activity.

Based on the literature review, several reports noted problems in training for acquisition professionals. The major theme suggested in these reports was that training is available, but not every acquisition professionals has received the training. The researcher expected and received similar responses during the interviews. Many of the respondents noted Defense Acquisition Workforce Improvement Act (DAWIA), which requires certification at different levels in each acquisition field. However, these same respondents stated that once DAWIA certification was received, the training process predominantly ceased to exist. This appears to be common across the acquisition workforce.

The researcher believes the significant downsizing of the acquisition workforce has created a hollow acquisition environment at the middle paygrade levels (GS-9/11). Upper-level management has made a conscious decision to do more with less and not provide the sustained training to include
additional skills needed to award and administer performance-based contracts for services.

The tendency within Government is to establish requirements policy before properly training the workforce in the implementation of the policy. Based on the literature review, training courses need to be developed specifically for the successful implementation of performance-based service contracting. The direction of Government acquisition is to follow best commercial practices. Therefore, Government officials need to look at private industry and adopt commercial practices that are appropriate for acquiring supplies and services for the Government.

c. Question Summary. Specific skills and training requirements needed to improve the knowledge and understanding of performance-based service contracting within the acquisition workforce are:

* contract administration - writing of performance-based statements of work (SOWs), monitoring and surveillance of the contractor.

* teamwork - developing integrated performance teams (IPTs).

* negotiations - creating “win-win” situations for all parties involved in the acquisition process.
• quality assurance plan - identifying measurable performance objectives relating to the performance-based SOW.

• market research - searching and identifying commercial "best practices" for providing the services.

• communications - creating open channels to communicate the needs of the customer to the contractor and dealing with customer complaints.

6. Question Six

How do you measure the performance of the contractor under a performance-based service contract? Can you explain the effectiveness of the Quality Assurance Plan (QAP) or Surveillance Plan?

a. Interview Results and Discussion. The intent of this question was to determine how contracting activities measure performance of the contractor under a performance-based service contract. Additionally, the question solicited comments on effective quality assurance plans (QAP) which have been used on performance-based service contracts. The majority of the respondents use Contracting Officer Representatives/Contracting Officer technical Representatives (COR/COTR) for monitoring and measuring the
performance of the contractor in accordance with the performance objectives outlined in the contract. A few respondents use Quality Assurance Evaluators (QAEs). COR/COTRs and QAEs perform similar job functions monitoring the performance of the contractor and documenting surveillance in periodic reports by following the surveillance plan as outlined in the contract. Additional respondent comments are paraphrased below:

Service contracts include a performance requirement summary that outlines the Government’s inspection program.

The quality assurance plan can be a problem if it is not properly written. It is only as effective as the people using it are.

The use of the Contractor Periodic and Reporting System (CPARS) system for service contracts allows annual evaluations to be documented on past performance.

Technical experience in the performance area being evaluated is sometimes not adequate. This leads to inadequate performance evaluations, which put a strain on the Government/contractor relationship.

The surveillance methods most frequently used by the COTR are random sampling, scheduled sampling, and customer complaints.

The customers need to be educated on whom to respond to when they need to file a complaint.

b. Analysis. Performance is a key evaluation factor for selection of the contractor who can provide quality services at a fair and reasonable price. Performance-based
statements of work make the evaluation of past performance much easier. A contractor’s performance is measured against established performance standards in the contract and the quality assurance plan. The effectiveness of the quality assurance plan depends on how well the measurable performance objectives correlate to the performance-based statement of work. The researcher believes that the effectiveness of the measured performance objectives by various surveillance methods indicates that the requirements were well-defined. Well-defined requirements usually facilitate accurately written performance statements of work, which are clear and understandable. A few surveillance methods used at field contracting activities are: 100 percent, random sampling, periodic review, and customer complaints.

Methods of surveillance can change after contract award based on the acceptance of a contractor quality control plan. One respondent discussed how the Government could request a quality control plan in the request for proposal (RFP). This allows Government officials ample time to evaluate the quality control plan submitted by the contractor. It is the opinion of the researcher that Government officials are adopting best commercial practices.
by validating and approving the processes used to ensure quality control. Performance-based service contracting specifies the performance objectives that the contractor will be measured against in the quality assurance plan. Performance-based service contracts which maintain quality at reasonable prices using best commercial practices, produce quality results with little Government oversight.

From the literature review, the researcher noted problems in the area of quality control not identified during the interviews due to the inexperience and training of the acquisition workforce. Inadequate surveillance was performed on numerous service contracts. Government officials did not maintain up-to-date surveillance records or prepare surveillance reports. Without documentation, evaluators were unable to show that a review of contractors' actual work was performed. During payment periods, the Contracting Officer used contractor prepared status reports as evidence of surveillance and determined the payment based on how well the contractor evaluated its own performance. The researcher believes that the reduced acquisition workforce and increase in workload has caused some contract administrative functions to not be completely documented by the quality control plan.
c. Question Summary. A contractor's performance is measured against established performance standards in the contract and the quality assurance plan. The effectiveness of the quality assurance plan depends on how well the measurable performance objectives correlate to the performance-based statement of work. A few surveillance methods used at field contracting activities are: 100 percent, random sampling, periodic review, and customer complaints.

7. Question Seven

What are the procedures and practices used to ensure that service requirements are correctly identified in a Performance-Work Statement or Statement of Objectives? What are some problems with improperly defined service requirements?

a. Interview Results and Discussion. The purpose of this question was to solicit opinions concerning how to correctly identify performance-based service requirements. In addition, this question requested respondents to identify problems associated with poorly defined service requirements. The majority of the respondents indicated that the customers did not know how to write accurate performance-based work statements. The customers knew the service requirements needed but were unable to write measurable performance objectives in the performance-based
work statement. Several of the respondents suggested that the problem with an improperly defined service requirement is that the contract has to be modified, which could be very costly depending on the severity of the error. Additional comments are paraphrased below:

The preparation of a performance work statement has to be a team effort between the customer and the contracting office.

Generally, the performance work statements received from the customer are more of an outline of the service requirements needed.

The basic process used is to take the initial performance work statement provided by the customer. Sit down with the customer and fill in the holes. The customer is the technical expert.

Teaming arrangements work well for identifying the requirements and then writing a performance-based work statement with measurable outcomes.

Two problems with performance-based work statements: (1) difficult to describe how to measure discrete performance requirements and (2) customers need training on writing effective performance-based work statements.

Performance-based work statements need the customer to use "action words" in defining specific functions to be performed.

Ambiguity in the performance work statement creates a challenge for the contractor to efficiently and effectively perform the contract.

The performance-based statement of work must be related to the measurable performance requirement outlined in the quality control plan.
b. Analysis. Writing well-defined performance-based statements of work helps to mitigate the risks associated with measuring the performance objectives outlined in the contract. Several of the respondents indicated that by forming team-type arrangements (similar to Integrated Product Teams used in the public and private sectors), communication barriers were removed and creative minds could produce better defined requirements. The researcher believes that early involvement by potential offerors is key to awarding an understandable and workable performance-based statement of work. Based on the literature review, contracting policy is now reflecting the preference toward draft solicitations to assist in refining statements of work. Before issuance of the formal RFP, the Government contracting team should invite interested offerors to one last meeting. At this meeting, the contractors should communicate back to the Government the proposal requirements as they understand them. The results of upfront planning and communication between the Government and potential offerors should be: few questions during the formal period, negotiations should be minimized, reduction in procurement administration lead-time (PALT), and postaward misunderstandings should be minimized.
The use of "action words" helps to describe the performance-based service requirements more objectively. The more objective the service requirements are, the more performance risk can be transferred to the contractor.

The FAR part 37 holds the Contracting Officer responsible for accurately describing requirements before contracting for services. Contractors must define the specific need or problems to be resolved in a manner that ensures full understanding and responsive performance. Part 37 also requires agencies to use performance-based contracting methods to the maximum extent practicable for the acquisition of services. Performance-based service contracting requires structuring all aspects of an acquisition around the purpose of the work to be performed, as opposed to how the work is to be performed.

c. Question Summary. Writing well-defined performance-based statements of work helps to mitigate the risks associated with measuring the performance objectives outlined in the contract. The use of teams and early involvement by all parties involved in the acquisition process is key to awarding an understandable and successful performance-based statement of work. An improperly written
performance-based statement of work can possibly have the following negative impacts on the contract:

- increase procurement administration lead time

- require contract modifications/changes which usually increase contract price

- require more Government oversight due to poor performance.

C. CHAPTER SUMMARY

This chapter presented the views and opinions gathered from interviews of Government acquisition professionals on how efficient and effective performance-based service contracting is being implemented at field contracting activities. The acquisition professionals indicated there are barriers that have to be overcome before performance-based service contracting is truly implemented. The question/answer period during the interviews provided for in-depth discussions on the strong need for continuous training of the acquisition workforce. The following chapter develops a model for performance-based service contracting and provides general guidance for successful implementation of performance-based service contracting.
V. GUIDANCE TO IMPLEMENTATION OF PERFORMANCE-BASED SERVICE CONTRACTING (PBSC)

A. INTRODUCTION

This chapter starts with a model developed by the researcher to compare traditional service contracting to performance-based service contracting. Second, the researcher strives to incorporate the information gathered from a thorough review of literature, Government reports, policies, regulations, and interviews with Government contracting personnel into a guide for implementing performance-based service contracting within the Department of Defense and Federal agencies.

B. PERFORMANCE-BASED SERVICE CONTRACTING MODEL

The transition from traditional service contracting to performance-based service contracting has been mandated by Federal policy and documented in governing Federal and Department of Defense regulations. The transition process started in 1991 with OFPP Policy Letter 91-2, Service Contracting. In order to fully understand performance-based service contracting, the researcher compared traditional service contracting to performance-based service
contracting, Table 3, to illustrate the differences in the acquisition process.

Table 3. Comparison of Service Contracting

<table>
<thead>
<tr>
<th>ACQUISITION ELEMENT</th>
<th>TRADITIONAL</th>
<th>PERFORMANCE-BASED</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>DETERMINATION OF REQUIREMENTS</strong></td>
<td>Customer develops a detailed specification and process to be used</td>
<td>Customer states a service objective and level of performance to be achieved</td>
</tr>
<tr>
<td><strong>STATEMENT OF WORK</strong></td>
<td>Specifications and processes provided in detailed format; Describes &quot;how&quot; the service is to be accomplished</td>
<td>Describe the service in terms of desired outcomes; Allows for flexibility from the contractor</td>
</tr>
<tr>
<td><strong>QUALITY CONTROL &amp; SURVEILLANCE</strong></td>
<td>Significant Government oversight; Inspections, audits, and reports</td>
<td>Government Insight; Performance management of the contractor</td>
</tr>
<tr>
<td><strong>CONTRACT TYPE</strong></td>
<td>Fixed-price (FP) or cost-reimbursable (CR) with little incentives or award fees</td>
<td>Fixed-price (FP) or cost-reimbursable (CR); Stronger emphasis on incentive/award type arrangements</td>
</tr>
<tr>
<td>ACQUISITION ELEMENT</td>
<td>TRADITIONAL</td>
<td>PERFORMANCE-BASED</td>
</tr>
<tr>
<td>---------------------</td>
<td>-------------</td>
<td>-------------------</td>
</tr>
<tr>
<td><strong>SOURCE SELECTION PROCEDURES</strong></td>
<td>Lowest price technically acceptable (LPTA); Satisfying the minimum requirements; written presentations</td>
<td>&quot;Best Value&quot; for quality of performance; Competitive negotiations with oral presentations</td>
</tr>
<tr>
<td><strong>CONTRACT ADMINISTRATION</strong></td>
<td>Simple when compared to performance-based; Significant Government oversight of the contractor</td>
<td>Complex due to contract incentive/award clauses; Insight to performance management of the contractor</td>
</tr>
</tbody>
</table>

Source: Developed by Researcher.

1. Determination of Requirements

The determination of requirements using traditional service contracting are identified through the use of detailed specifications. The procuring activity provides detailed specifications and direction to how the contractor should perform the service for the Government. Under performance-based service contracting, the procuring activity states the required services using performance-based specifications and objectives.
2. Statement of Work

The statement of work in traditional service contracting uses the detailed specifications generated during determination of the requirements. It is extremely difficult for the contractor to deviate from the processes and procedures agreed upon without prior consent from the Government. This approach stymies the innovation and creativity of the contractor and does not allow the contractor to use best commercial practices.

The performance-based statement of work describes the work in terms of “what” the required outcome should be rather than “how” the work should be accomplished. To the maximum extent practicable, the contractor is allowed the opportunity to use best commercial practices in the performance of the service with minimum oversight from the Government.

3. Quality Control and Surveillance

To determine if the contractor satisfies the requirements under a performance-based contract, a quality assurance plan needs to be developed. This quality assurance plan should directly correspond to the performance measures and objectives of the service contract
requirements. The procuring activity and customer should develop formal, measurable metrics to facilitate the assessment of contractor performance and use performance incentives and deduction schedules. On the contrary, traditional service contracting relied heavily on inspection and oversight programs to assess contractor performance. There is greater Government insight to contractor performance in performance-based contracting versus Government oversight in traditional service contracting.

4. Contract Type

Contracts for services should be placed competitively using fixed price type contracts. Fixed priced contracts are appropriate for services that can be objectively defined using a performance-based statement of work and where measurable performance standards and surveillance plans can be developed. Services that are routine, simple in nature and require no more than a minimal acceptable level of performance fall into this category.

Cost reimbursement contracts are appropriate for services that can only be defined in general subjective terms. Complex or unique service requirements where quality of performance is paramount fall into this category.
The type of contract used mainly depends on the understanding of the requirements and the degree of manageable performance risk by the contractor. Performance-based service contracting differs from traditional service contracting by including incentive provisions to reward the contractor providing superior performance and deductions schedules to discourage unsatisfactory performance. Performance-based contracting rewards the contractor for being innovative and creative in providing quality services and achieving high levels of performance.

5. Source Selection Procedures

Neither the procurement statutes nor the FAR specify detailed standards for source selection procedures. The statutes merely require the award to be made "to the responsible source whose proposal is most advantageous to the United States, considering only cost or price and the other factors included in the solicitation" (FAR, 1999). Procuring activities should use competitive negotiations in performance-based acquisitions where quality of performance and the minimum acceptable level thresholds correspond to cost-benefit analysis for performance above the minimum level. This approach applies to the majority of services acquired by procuring activities. In the last few years,
"Best Value" has been the goal of every acquisition. "Best Value" ensures that the selected contractor satisfies the customer's needs within cost, schedule, and performance criteria. It is not uncommon to pay a price premium to acquire quality services in "Best Value" competitive source selections. The traditional approach to service contracting does not provide for incentives/awards to the contractor for performance above the minimum acceptable level.

Procuring activities should develop evaluation criteria and selection procedures that use quality related criteria such as: technical capability, management capability, cost realism, and past performance. The more complex and less clearly defined the service requirements, the greater the emphasis on the source selection criteria. The desired relative importance among the source selection criteria should be annotated in the contract solicitations. Potential offerors understanding of the requirements should be reviewed with the cost proposal to ensure application of cost realism. Technical leveling and technical transfusion discourage offerors from proposing innovative methods of performance that use the most up-to-date technology and capability available in the commercial marketplace. The potential for technical leveling and technical transfusion
should be significantly reduced by limited the opportunity for discussions and revisions by the offerors.

6. Contract Administration

Contract administration planning consists of all activities involved in setting up systems and procedures to ensure compliance with the contract terms and conditions during contract performance (Defense Acquisition University, CON202 Guide, 1999). Even though contract administration starts well before the award of the contract, contract administration is generally referred to as a post-award contract management. The objective of contract management, as a discipline, is to provide a practical methodology for Government contracting personnel to establish a definable level of control over monitoring and surveillance of the contractor’s performance.

There are challenges that contract management personnel must overcome in the administration of performance-based service contracts. Performance-based contracts are more complex than traditional service contracts due to the administration of incentive/award clauses. The contractor performing the service has committed manpower, skills, energy, and managerial expertise to the successful performance of the contract and is intimately concerned with
receiving the incentives/awards placed in the contract clauses. This type of arrangement requires Government contracting personnel to provide more insight into the monitoring and surveillance of the contractor’s performance. If the Government fails to properly manage the contract, then the relationship between the Government and the contractor can be weakened. The overall goal of contract management is to ensure that contractor performance satisfies the objectives, which are definable in the measurement of cost, schedule, and performance.

7. Performance-Based Service Contracting Model

The researcher developed a model, Table 4, that illustrates the transition process from traditional service contracting to performance-based service contracting. The model identifies techniques that may be used to overcome the potential barriers. It also shows potential benefits that may be received through performance-based service contracting.
Table 4. Performance-Based Service Contracting Model

**Techniques:**
- Teaming Arrangements
- Draft Solicitations
- Performance Objectives
- Validate Quality Processes

**Benefits:**
- Open Communications
- Best Value Services
- Measurable Performance
- Reduces Government Oversight
- Higher Quality of Performance

**Statement of Work:**
Detailed specifications state "what" and "how"

**Contract Type:**
Provide little incentives to the contractor

**Quality Surveillance Plan:**
Major Government oversight

**Source Selection:**
Use sealed-bids; lowest price technically acceptable (LPTA)

**Contract Administration:**
Inspections, audits, and reports generated

**Traditional Service Contracting**
Source: Developed by Researcher.

**BARRIERS**
- Writing effective performance-based statements of work
- Training and skills of the acquisition workforce
- Oversight versus Insight
- Paying more for better quality
- Doing more with less; decreasing budgets and workforce downsizing
- Communication between all parties
- Changing the cultural mindset

**Statement of Work:**
Accurately defined performance objectives

**Contract Type:**
Provide incentives and rewards to the contractor

**Quality Surveillance Plan:**
Government insight of processes and procedures

**Source Selection:**
Use competitive negotiations; "Best Value"

**Contract Administration:**
Prior planning reduces Government oversight

**Performance-Based Service Contracting**
C. GUIDANCE FOR IMPLEMENTING PERFORMANCE-BASED SERVICE CONTRACTING (PBSC)

Performance-based service contracting (PBSC) requires structuring all aspects of an acquisition around the purpose of the service that is to be performed in clear and well defined statements of work. PBSC emphasizes quantifiable, measurable performance requirements and quality standards in developing statements of work, selection of contractors, determining contract type, incentives, and performing contract administration. The following sections of this thesis provide guidance for successful implementation of performance-based section contracting. The researcher has compiled information from interviews, literature review, Government reports, and acquisition guidance for the planning and acquisition of service requirements using the performance-based contracting approach. The purpose of this guidance is to assist Government agencies in developing procedures for implementing PBSC.

1. Development of the Performance-Based Statement of Work

The performance-based statement of work (SOW) is the foundation for PBSC. The performance-based SOW specifies
performance outputs that are derived from a thorough job analysis. Job analysis requires the customer to identify and analyze the job outputs task by task. From these outputs, the customer develops measurable performance standards that include appropriate levels of quality. Contractor compensation and financial risk are based on successfully satisfying these quality and performance standards.

Performance-based SOWs describe the required outcomes of the services desired and provide criteria for measuring and verifying performance. The key aspects of a performance-based SOW include (DoD, AF903T1, 1999, p. 40-41 and Kalman, 1998):

- A description of the expected output or outcomes.
- A statement expressing the performance characteristics.
- Clearly specified requirements to allow the Government and offerors to estimate cost of services.
- Clearly specified requirements to allow the offeror to determine levels of expertise, manpower, and other resources to accomplish the desired outcome.
• The SOW should state specific duties of the contractor so that the contractor knows what is required and can address the requirements.

• A definition of the environment in which the services are to be performed, including all internal and external organizational interfaces.

• Measurement criteria that allow both contractual parties to gauge actual versus expected performance.

• The SOW should leave no doubt as to the contractor’s obligations and should accurately reference only minimal applicable standards.

The performance-based SOW should specify in clear, understandable terms the services to be done by the contractor during the performance of work. There must be a complete understanding of the services that are needed to satisfy a particular requirement; and an ability to define what is required in quantitative terms (Kalman, 1998).

The Government’s requirements must be expressed clearly in the SOW. The requirements should be specified in terms of minimum quality oriented performance, operational effectiveness and operational efficiency. SOWs shall state management requirements in terms of results needed rather
than "how to manage" procedures for achieving those results. The SOW is the standard for measuring contractor performance. The SOW determines the Government’s and contractor’s perspective rights and obligations. The SOW must clearly define the work to be performed since the language detailing the contractor’s effort is directly related to questions concerning the scope of work. The clearer the requirement is defined, the more enforceable are the elements of the SOW (Kalman, 1998). Table 5 is a listing of "do’s" and "don’ts" when writing a performance-based SOW.

Table 5. Performance-Based Statement of Work

<table>
<thead>
<tr>
<th><strong>DO’s</strong></th>
<th><strong>DON'Ts</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td>Select an experienced SOW writing team</td>
<td>Do not specify technical proposal criteria or evaluation factors in the SOW</td>
</tr>
<tr>
<td>Use a work breakdown structure to outline the required work effort</td>
<td>Do not include a delivery schedule in the SOW</td>
</tr>
<tr>
<td>Set SOW objectives in accordance with the Acquisition Plan</td>
<td>Do not impose a Government format when a contractor format is acceptable</td>
</tr>
<tr>
<td>Keep acquisition streamlining in mind at all times</td>
<td>Do not over specify. Specify only what is required and let the contractor find out the best method to fulfill the requirement</td>
</tr>
</tbody>
</table>

Source: Kalman and Company, Inc.
2. **Quality Assurance/Surveillance Plan (QASP)**

There is a direct relationship between the development of the performance-based SOW and the Quality Assurance Surveillance Plan (QASP) (Kalman, 1998). The QASP defines what the Government must do to ensure that the contractor has performed in accordance with the SOW performance standards. This can range from a one-time inspection of a service, to periodic inspections of on-going services. It is needed to ensure that the Government is receiving the quality of services called for under the contract, and pays only for the acceptable level of services received. Since the QASP is intended to measure performance against standards in the SOW, these interdependent documents must be coordinated (U.S. Executive Office of the President, OFPP, 1998). When the two documents are both effective and efficient, the QASP provides the contractor with information on how the Government will measure the requirements in the SOW.

The QASP should include a surveillance schedule and clearly state the surveillance method(s) to be used. The QASP development establishes how resources will be used to ensure that the Government receives adequate services for payment to the contractor. The detail of surveillance in
the QASP should be consistent with the importance of the service being monitored. Selecting the most appropriate surveillance method for the effort involved is important. Government agencies should take into consideration task criticality, task lot size, surveillance period, performance requirements and standards. The availability of quality assurance evaluators (QAEs) and other resources should also be considered. QAEs must be fully qualified to meet the major responsibilities of the position: maintaining complete and accurate documentation, a good relationship with the contractor, and a thorough knowledge of the contract requirements. Experience and training are essential for effective surveillance.

Careful selection of appropriate surveillance methods enables the Government to determine the amount of resources and associated costs needed to perform the surveillance. Contractors should be briefed on surveillance requirements and responsibilities at a post-award conference. Surveillance should be comprehensive, systematic, and well documented. Reviewing and discussing the contractor’s plan for maintaining an acceptable quality level under the contract is important. When performance is deficient, the contracting officer should notify the contractor promptly and implement the Government’s system to track corrective
action. When surveillance results show good performance consistently, then the amount of surveillance should be adjusted accordingly. This saves the Government money, reduces oversight burdens on the contractor, and recognizes the contractor’s achievement of performance (U.S. Executive Office of the President, OFPP, 1998). Table 6 provides a listing of acceptable surveillance methods.

Table 6. Surveillance Methods

<table>
<thead>
<tr>
<th>Method</th>
<th>Task</th>
</tr>
</thead>
<tbody>
<tr>
<td>100 Percent Inspection</td>
<td>Most appropriate for infrequent tasks or tasks with stringent performance requirements. Performance is inspected when each task occurs. Too expensive to be used in most cases.</td>
</tr>
<tr>
<td>Random Sampling</td>
<td>Most appropriate for recurring tasks. Services are sampled to determine if the level of performance is acceptable. Works best when the number of tasks being performed is very large.</td>
</tr>
<tr>
<td>Management Information System</td>
<td>Collect information from tasks for specified periods of time. Information is compared to a contract standard. Performance can be judged on the basis of comparison.</td>
</tr>
<tr>
<td>Formal Customer Complaints</td>
<td>Customer feedback can be used as substantiating evidence for unsatisfactory performance of task.</td>
</tr>
<tr>
<td>---------------------------</td>
<td>--------------------------------------------------------------------------------------------------</td>
</tr>
<tr>
<td>Periodic Inspection</td>
<td>Appropriate for tasks that occur infrequently, and where 100 percent inspection is neither required nor practicable. Consists of the evaluation of tasks selected on other than a 100 percent or random basis.</td>
</tr>
<tr>
<td>(Planned Sampling)</td>
<td></td>
</tr>
</tbody>
</table>

Source: Developed by Researcher.

3. Contract Type

The FAR Part 16 provides guidance for selecting a contract type that best matches the acquisition of services for the Government. Selecting the contract type is generally a matter of negotiation and requires the exercise of good sound judgment. The objective is to negotiate a contract type and price (or estimated cost and fee) that will result in reasonable contractor risk, and provide the contractor with the greatest incentive for efficient and economical performance (FAR, part 16.103). The use of negotiations is considered important in the selection of the contract type because it should offer the best value for the services being acquired by the Government.
Presently the FAR requires that service contracts be awarded through sealed bidding if the requirements for this method of solicitation exist (FAR, part 37.105). Performance-based service contracting encourages the use of fixed-price contract and incentives that are most likely to motivate contractors to perform optimally (U.S. Executive Office of the President, OFPP, 1998). To the maximum extent practicable, performance incentives shall be incorporated into the contract to encourage contractors to increase efficiency and maximize performance. These incentives shall correspond to the specific performance standards in the quality assurance surveillance plan (QASP) and shall be capable of being measured objectively (FAR, part 37.602-4).

Table 7 provides a list of contract types that should be evaluated when acquiring services using performance-based contracting procedures. These contract types should not be considered the only contract types that can be used in performance-based contracting.
<table>
<thead>
<tr>
<th>Contract Type</th>
<th>When to use in PBSC</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fixed-Price</td>
<td>Appropriate for services that can be objectively defined in the solicitation and for which risk of performance is manageable.</td>
</tr>
<tr>
<td>Cost-Reimbursement</td>
<td>Appropriate for services that can only be defined in general terms or for which risk of performance is not reasonably manageable.</td>
</tr>
<tr>
<td>Time and Material/Labor Hour</td>
<td>Appropriate for services when the amount or duration of direct labor hours and materials cannot be predicted.</td>
</tr>
<tr>
<td>Indefinite Delivery/Definite Quantity</td>
<td>Appropriate to use when a definite quantity of services will be required during a specific period.</td>
</tr>
<tr>
<td>Indefinite Delivery/Requirements</td>
<td>Appropriate to use when it is difficult to determine the precise quantities of services required during a definite period of time.</td>
</tr>
<tr>
<td>Indefinite Delivery/Indefinite Quantity</td>
<td>Appropriate to use when making multiple awards of indefinite-quantity contracts under a single solicitation for the same service.</td>
</tr>
</tbody>
</table>

Source: Developed by Researcher.
4. Contract Administration

Contract administration involves those activities performed by Government officials after a contract has been awarded to determine how well the Government and the contractor performed to meet the requirements of the contract. It encompasses all dealings between the Government and the contractor from the time the contract is awarded, until the work has been completed and accepted, or the contract terminated, payment has been made, and disputes have been resolved. Contract administration constitutes that primary part of the acquisition process that assures the Government gets what it has paid for.

In contract administration for performance-based services, the focus is on obtaining the right services, standard level of quality, on time, and within the boundaries of the budget. While the legal requirements of the contract are determinative of the proper course of action by Government officials in administering the contract, the exercise of skill and judgment is often required in order to effectively protect the interest of the public.

The specific nature and extent of contract administration varies from contract to contract. It can
range from the minimum acceptance of a service and payment to the contractor, to an extensive involvement by the customer, contracting officials, and surveillance personnel throughout the life of the contract. Factors influencing the degree of contract administration include the scope of the service, the type of contract, and the experience and commitment of the personnel involved in the acquisition process. Contract administration starts with developing clear, concise performance-based statements of work to the maximum extent possible, and preparing a contract administration plan that cost effectively measures the contractor's performance and provides documentation to pay for the services performed.

Post award orientation, either by conference, letter or some other means of communication, should be the beginning of the actual process of good contract administration. This communication process can be a useful tool that helps the Government and the contractor personnel achieve a clear and mutual understanding of the contract requirements. It can also help the contractor understand the roles and the responsibilities of the Government personnel who will administer the contract. It is helpful to have a pre-meeting with contracting officials prior to the post award orientation conference. This is done so there is a clear
understanding of such things as the authority of Government personnel who will administer the contract, quality control, the specific contract performance requirements, special contract provisions, the Government's procedures for monitoring and measuring performance, contractor billing, voucher approval, and payment procedures.

Where appropriate, an alternative dispute resolution (ADR) should be discussed with the contractor to help avoid future contract administration problems. One technique used within Government contracting to prevent disputes from occurring is partnering. Partnering involves Government and contractor management personnel mutually developing a plan for success. Potential sources of conflict are identified, and the parties seek cooperative ways to resolve any disputes that may arise during contract performance. The process results in the parties developing a partnership, which serves as a roadmap for contract success (U.S. Executive Office of the President, OFPP, 1994).

Good contract administration assures that the customers are satisfied with the service being obtained under the contract. Table 8 provides a listing of activities performed during administration of the performance-based service contracts.
Table 8. Contract Administration Activities

<table>
<thead>
<tr>
<th>Development of a contract administration plan</th>
</tr>
</thead>
<tbody>
<tr>
<td>Post award orientation conference with Government and contracting personnel</td>
</tr>
<tr>
<td>Process for surveillance and monitoring contractor performance</td>
</tr>
<tr>
<td>Procedures for modifying and making changes to the contract</td>
</tr>
<tr>
<td>Define the roles and responsibilities of Government personnel involved in administering the contract</td>
</tr>
<tr>
<td>Discuss process for resolving disputes</td>
</tr>
<tr>
<td>Method of payment for services performed by the contractor</td>
</tr>
</tbody>
</table>

Source: Developed by Researcher.

D. CHAPTER SUMMARY

In this chapter, the researcher developed the Performance-Based Service Contracting Model to illustrate the differences between traditional and performance-based service contracting. The acquisition elements of the model were discussed in order to fully understand the spectrum of performance-based service contracting. Additionally, the researcher developed guidelines for implementing performance-based service contracting based on interviews, literature review, Government reports, and articles pertaining to the area being researched.
VI. CONCLUSIONS AND RECOMMENDATIONS

A. INTRODUCTION

This research effort provides an examination of the transition from traditional service contracting to performance-based service contracting. In this chapter, the researcher discusses the conclusions identified during the research and provides recommendations for successful implementation of performance-based service contracting. This chapter concludes with recommendations for areas of further research.

B. CONCLUSIONS

1. The transition from traditional service contracting to performance-based service contracting is slow to be implemented within the Government.

In 1991, the Office of Federal Procurement Policy established policy for the acquisition of services that emphasized performance-based contracting. The qualitative interview results collected by the researcher and analyzed in Chapter IV suggest that Government contracting activities have not fully embraced performance-based approach to contracting.
2. Writing well-defined performance-based statements of work is an art.

The literature review and interviews with Government acquisition professionals strongly support the notion that creating well-defined performance-based statements of work requires experience and teamwork among the acquisition team. Personnel writing performance-based statements of work overemphasized "how" the work was to be done rather than the desired outcomes. Additionally, the measurable performance objectives are directly related to the performance work statement.

3. Selecting the appropriate contract type is critical to any successful acquisition.

All personnel interviewed and information gathered from literature reviews have stated that the selection of the appropriate contract type is critical to any successful acquisition. Performance-based statements of work allow the use of fixed-price contracts because of the well-defined requirements. Contracting activities need to use good, sound business judgement in selecting the contract type. There should be a balance between quality performance, cost, and risk.
4. Education and training is needed to maintain an acquisition workforce at a certain skill level.

As discussed in Chapters III and IV, the skills and experience of the Government acquisition workforce are barriers to the successful implementation of performance-based service contracting. The interviews indicated that the Government acquisition workforce lacks adequate training in the area of service contracting.

5. Adoption of best practices should be the norm.

Most reports in the literature review suggest that the Government should adopt the best commercial practices used in the private industry. This sounds like a great idea. If someone wants to perform a given task, then it should be easier to mimic the success of someone else, than trying to start from scratch. However, the researcher believes that the Government acquisition professionals are extremely knowledgeable and adoption of best practices should come from both public and private organizations.

6. Performance-based service contracting requires a cultural change from upper-management and mindset of the acquisition workforce.

For performance-based service contracting to be fully implemented at Government contracting activities, there
needs to be a champion within upper-management that embellishes change management. All personnel interviewed indicated that cultural change is a major barrier to the successful implementation of performance-based service contracting.

C. RECOMMENDATIONS

1. Need to educate and train the acquisition workforce on PBSC techniques and processes.

The acquisition environment is always changing. The acquisition workforce needs to be continuously educated on best practices being used in public and private organizations. Success stories in performance-based service contracting need to be shared with all acquisition personnel. This will facilitate change management of the acquisition culture. Specific areas of training identified during the research are: writing of performance-based statements of work, communication and teamwork skills, and the development of quality assurance surveillance plans.

2. Develop metrics based on performance objectives for measuring the effectiveness and efficiency of performance-based service contracting.

This research effort indicated that it was too early to measure the success of performance-based service contracting because many contracting activities have not fully
implemented this contracting approach. As performance-based service contracting moves forward, a set of metrics should be developed to measure the effectiveness and efficiency of performance-based service contracting.

3. **Department of Defense should conduct a study to determine the impact performance-based service contracting will have on small businesses.**

As the Department of Defense moves forward in the implementation of performance-based service contracting, some of the socio-economic and small business goals will probably be impacted, either positively or negatively. This study would look at the implementation process and determine the impact on small businesses.

**D. ANSWERS TO RESEARCH QUESTIONS**

The following primary and subsidiary research questions were developed in Chapter I and provided direction for accomplishing this research:

1. **Primary Research Question**

How can a Department of Defense Field Contracting Activity successfully implement an effective Performance-Based Service Contracting (PBSC) Program into its operational routine, given that no formal PBSC process exists while available resources will remain relatively constant?
Performance-based service contracting (PBSC) requires structuring all aspects of an acquisition around the purpose of the service that is to be performed in broad and imprecise statements of work. PBSC emphasizes quantifiable, measurable performance requirements and quality standards in developing statements of work, selection of contractors, determining contract type, incentives, and performing contract administration.

Chapter V provides guidance for successful implementation of performance-based service contracting at Department of Defense field contracting activities. The key areas covered are: (1) Development of the Performance-Based Statement of Work; (2) Quality Assurance/Surveillance Plan (QASP); (3) Selection of the Appropriate Contract Type; and (4) Contract Administration.

2. **Subsidiary Questions**

a. Subsidiary Question #1

What is PBSC, and what constitutes effective PBSC?

Performance-based service contracting (PBSC) can be defined as "a contracting strategy for recurring services that emphasizes that the work to be performed should be defined in mission-related output terms, focusing on what needs to be done rather than how to provide the service" (U.S. Department of Transportation, Office of the Secretary,
1999). It is too early in the implementation stages to determine what constitutes effective PBSC. Based on the literature review and analysis of qualitative interviews with Government acquisition professionals, effective PBSC should provide customers with quality service at a reasonable price that requires minimal Government oversight.

b. Subsidiary Question #2

What skills are necessary to conduct effective PBSC? What approaches to PBSC can be used to develop and enhance these skills?

Specific skills and training requirements noted during interviews with the acquisition workforce and literature review are:

- statement of work - writing effective performance-based statements of work (SOWs).
- contract administration - monitoring and surveillance of the contractor.
- teamwork - developing integrated performance teams (IPTs).
- negotiations - creating "win-win" situations for all parties involved in the acquisition process.
- quality assurance plan - identifying measurable performance objectives.
• market research - searching and identifying commercial "best practices" for providing the services.

• communications - creating open channels to communicate the needs of the customer to the contractor.

The use of a performance-based approach to service contracting requires the customer and supplier to critically analyze three important factors (DoD, AF903T1, 1999, p. 16):

(1) Defining the service the customer wants performed.
The customer and potential suppliers work together to define the performance relevant to the customer's needs. This requires an initial discussion and then follow-on discussion of how to measure performance to ensure the supplier knows what the customer wants performed.

(2) Selection of a supplier for the service required.
The customer seeks performance measures it can use to choose a supplier who is likely to make a sound business partner over the long term. It uses a source selection process focused on past performance rather than on current or historical cost. Suppliers maintain performance data that they expect potential customers will value in source selection to distinguish themselves from other suppliers.
(3) Incentivize the supplier to improve its performance relative to the customer's needs. After source selection, the customer and supplier work together to measure their joint performance and allocate between themselves the gains that comes from improvements over time. Many things can help motivate a good supplier. The customer rewards performance by extending the length of a contract or reducing Government oversight on the performance of the contract. Both of the methods reduce the customer's and the supplier's administrative costs. The customer may also expand the activities that a supplier provides.

c. Subsidiary Question #3

What are the potential barriers that may be encountered when transitioning to PBSC?

Through an intensive review of professional literature, the researcher identified barriers that Department of Defense has to overcome as it transitions from traditional service contracting to performance-based service contracting. The Department of Defense acquisition workforce needs to develop and adopt a new cultural mindset. The old way of doing business needs to change and the acquisition workforce needs to understand and accept the new performance-based acquisition approach to service contracting.
The most common barriers identified by the majority of the respondents were:

- the lack of skills and training to administer performance-based service contracts
- inability to write measurable performance work statements
- the need to change the cultural mindset of the individuals involved in the process.

The stated practices being implemented to overcome these barriers are:

- use of integrated performance teams (IPTs)
- submit draft request for proposal (RFP) and use it as a market research tool
- request the contractor submit a Quality Control Plan.

Other barriers to the successful transition to performance-based service contracting are (DoD, AF903T1, 1999, p.40):

- Identify Skills/Resources Required for Performance-Based Acquisitions
- Adoption of Best Commercial Practices
- Writing of Performance-Based Statements of Work
- Contract Administration.
The identified barriers cover the entire spectrum of performance-based service contracting from "cradle to the grave." The success of overcoming these barriers should accomplish the field contracting activity’s main mission of providing quality support and services to the warfighters better, faster, and cheaper.

d. Subsidiary Question #4

What benefits can be realized as a result of implementing an effective PBSC program?

Most of the respondents stated that performance-based contracting has allowed for the adoption of best commercial practices. Many respondents felt that the contractor knows the service business better than the Government, especially as technology is continuing to advance and improve. Several respondents stated that the following benefits could be realized through the effective implementation of performance-based service contracting:

- Receive better quality services performed at a lower price
- Learn commercial industry standards for performance of services
- Reduced Government oversight during contract administration.
Several respondents stated that adopting commercial practices for performance-based service contracting promotes innovation and creativity from the contractor.

E. AREAS FOR FURTHER RESEARCH

During this research, the researcher identified several areas that warrant additional research. The following topics are recommended for further research:

1. Conduct quantitative research on completed performance-based service contracts to determine the effectiveness of performance-based service contracting.

2. Examine and evaluate the issues that the Small Business Administration (SBA) has had on Government contracting for services from small businesses and small disadvantaged businesses.

3. Analyze methods to improve service contracting, such as contract bundling, consortium purchasing arrangements, and Government-wide area service contracts.

4. Research how major system commands are contracting for services and determine applicable processes and procedures that may be used by Department of Defense Field Contracting Activities.
APPENDIX A. CONTRACT ADMINISTRATION FUNCTIONS

Federal Acquisition Regulations

subpart 42.302 -- Contract Administration Functions

(a) The following contract administration functions are normally delegated to a CAO, unless the contracting officer has been designated to perform these functions by the cognizant Federal agency (see 42.001).

(1) Review the contractor's compensation structure.

(2) Review the contractor's insurance plans.

(3) Conduct post-award orientation conferences.

(4) Review and evaluate contractors' proposals under Subpart 15.4 and, when negotiation will be accomplished by the contracting officer, furnish comments and recommendations to that officer.

(5) Negotiate forward pricing rate agreements (see 15.407-3).

(6) Negotiate advance agreements applicable to treatment of costs under contracts currently assigned for administration (see 31.109).

(7) Determine the allowability of costs suspended or disapproved as required (see Subpart 42.8), direct the suspension or disapproval of costs when there is reason
to believe they should be suspended or disapproved, and approve final vouchers.

(8) Issue Notices of Intent to Disallow or not Recognize Costs (see Subpart 42.8).

(9) Establish final indirect cost rates and billing rates for those contractors meeting the criteria for contracting officer determination in Subpart 42.7.

(10) Attempt to resolve issues in controversy, using ADR procedures when appropriate (see Subpart 33.2); prepare findings of fact and issue decisions under the Disputes clause on matters in which the administrative contracting officer (ACO) has the authority to take definitive action.

(11) In connection with Cost Accounting Standards (see 48 CFR 30.601 and 48 CFR Chapter 99 (FAR Appendix)) --

(i) Determine the adequacy of the contractor's disclosure statements;

(ii) Determine whether disclosure statements are in compliance with Cost Accounting Standards and Part 31;

(iii) Determine the contractor's compliance with Cost Accounting Standards and disclosure statements, if applicable; and

(iv) Negotiate price adjustments and execute supplemental agreements under the Cost Accounting Standards clauses.
(12) Review and approve or disapprove the contractor's requests for payments under the progress payments or performance-based payments clauses.

(13) Make payments on assigned contracts when prescribed in agency acquisition regulations.

(14) Manage special bank accounts.

(15) Ensure timely notification by the contractor of any anticipated overrun or underrun of the estimated cost under cost-reimbursement contracts.

(16) Monitor the contractor's financial condition and advise the contracting officer when it jeopardizes contract performance.

(17) Analyze quarterly limitation on payments statements and recover overpayments from the contractor.

(18) Issue tax exemption forms.

(19) Ensure processing and execution of duty-free entry certificates.

(20) For classified contracts, administer those portions of the applicable industrial security program delegated to the CAO (see Subpart 4.4).

(21) Issue work requests under maintenance, overhaul, and modification contracts.
(22) Negotiate prices and execute supplemental agreements for spare parts and other items selected through provisioning procedures when prescribed by agency acquisition regulations.

(23) Negotiate and execute contractual documents for settlement of partial and complete contract terminations for convenience, except as otherwise prescribed by Part 49.

(24) Negotiate and execute contractual documents settling cancellation charges under multiyear contracts.

(25) Process and execute novation and change of name agreements under Subpart 42.12.

(26) Perform property administration (see Part 45).

(27) Approve contractor acquisition or fabrication of special test equipment under the Special Test Equipment clause.

(28) Perform necessary screening, redistribution, and disposal of contractor inventory.

(29) Issue contract modifications requiring the contractor to provide packing, crating, and handling services on excess Government property. When the ACO determines it to be in the Government's interests, the services may be secured from a contractor other than the contractor in possession of the property.
(30) In facilities contracts --

(i) Evaluate the contractor's requests for facilities and for changes to existing facilities and provide appropriate recommendations to the contracting officer;

(ii) Ensure required screening of facility items before acquisition by the contractor;

(iii) Approve use of facilities on a noninterference basis in accordance with the Use and Charges clause;

(iv) Ensure payment by the contractor of any rental due; and

(v) Ensure reporting of items no longer needed for Government production.

(31) Perform production support, surveillance, and status reporting, including timely reporting of potential and actual slippages in contract delivery schedules.

(32) Perform preaward surveys (see Subpart 9.1).

(33) Advise and assist contractors regarding their priorities and allocations responsibilities and assist contracting offices in processing requests for special assistance and for priority ratings for privately owned capital equipment.

(34) Monitor contractor industrial labor relations matters under the contract; apprise the contracting officer and, if designated by the agency, the cognizant
labor relations advisor, of actual or potential labor disputes; and coordinate the removal of urgently required material from the strikebound contractor's plant upon instruction from, and authorization of, the contracting officer.

(35) Perform traffic management services, including issuance and control of Government bills of lading and other transportation documents.

(36) Review the adequacy of the contractor's traffic operations.

(37) Review and evaluate preservation, packaging, and packing.

(38) Ensure contractor compliance with contractual quality assurance requirements (see Part 46).

(39) Ensure contractor compliance with contractual safety requirements.

(40) Perform engineering surveillance to assess compliance with contractual terms for schedule, cost, and technical performance in the areas of design, development, and production.

(41) Evaluate for adequacy and perform surveillance of contractor engineering efforts and management systems that relate to design, development, production, engineering changes, subcontractors, tests, management of engineering resources, reliability and maintainability, data control systems, configuration management, and independent research and development.
(42) Review and evaluate for technical adequacy the contractor's logistics support, maintenance, and modification programs.

(43) Report to the contracting office any inadequacies noted in specifications.

(44) Perform engineering analyses of contractor cost proposals.

(45) Review and analyze contractor-proposed engineering and design studies and submit comments and recommendations to the contracting office, as required.

(46) Review engineering change proposals for proper classification, and when required, for need, technical adequacy of design, producibility, and impact on quality, reliability, schedule, and cost; submit comments to the contracting office.

(47) Assist in evaluating and make recommendations for acceptance or rejection of waivers and deviations.

(48) Evaluate and monitor the contractor's procedures for complying with procedures regarding restrictive markings on data.

(49) Monitor the contractor's value engineering program.

(50) Review, approve or disapprove, and maintain surveillance of the contractor's purchasing system (see Part 44).
(51) Consent to the placement of subcontracts.

(52) Review, evaluate, and approve plant or division-wide small, small disadvantaged and women-owned small business master subcontracting plans.

(53) Obtain the contractor's currently approved company- or division-wide plans for small, small disadvantaged and women-owned small business subcontracting for its commercial products, or, if there is no currently approved plan, assist the contracting officer in evaluating the plans for those products.

(54) Assist the contracting officer, upon request, in evaluating an offeror's proposed small, small disadvantaged and women-owned small business subcontracting plans, including documentation of compliance with similar plans under prior contracts.

(55) By periodic surveillance, ensure the contractor's compliance with small, small disadvantaged and women-owned small business subcontracting plans and any labor surplus area contractual requirements; maintain documentation of the contractor's performance under and compliance with these plans and requirements; and provide advice and assistance to the firms involved, as appropriate.

(56) Maintain surveillance of flight operations.

(57) Assign and perform supporting contract administration.
(58) Ensure timely submission of required reports.

(59) Issue administrative changes, correcting errors or omissions in typing, contractor address, facility or activity code, remittance address, computations which do not require additional contract funds, and other such changes (see 43.101).

(60) Cause release of shipments from contractor's plants according to the shipping instructions. When applicable, the order of assigned priority shall be followed; shipments within the same priority shall be determined by date of the instruction.

(61) Obtain contractor proposals for any contract price adjustments resulting from amended shipping instructions. Review all amended shipping instructions on a periodic, consolidated basis to ensure that adjustments are timely made. Except when the ACO has settlement authority, the ACO shall forward the proposal to the contracting officer for contract modification. The ACO shall not delay shipments pending completion and formalization of negotiations of revised shipping instructions.

(62) Negotiate and/or execute supplemental agreements, as required, making changes in packaging subcontractors or contract shipping points.

(63) Cancel unilateral purchase orders when notified of nonacceptance by the contractor. The CAO shall notify the contracting officer when the purchase order is canceled.
(64) Negotiate and execute one-time supplemental agreements providing for the extension of contract delivery schedules up to 90 days on contracts with an assigned Criticality Designator of C (see 42.1105). Notification that the contract delivery schedule is being extended shall be provided to the contracting office. Subsequent extensions on any individual contract shall be authorized only upon concurrence of the contracting office.

(65) Accomplish administrative closeout procedures (see 4.804-5).

(66) Determine that the contractor has a drug-free workplace program and drug-free awareness program (see Subpart 23.5).

(67) Support the program, product, and project offices regarding program reviews, program status, program performance and actual or anticipated program problems.

(68) Evaluate the contractor's environmental practices to determine whether they adversely impact contract performance or contract cost, and ensure contractor compliance with environmental requirements specified in the contract. Contracting officer responsibilities include, but are not limited to --

(i) Ensuring compliance with specifications requiring the use of environmentally preferable and energy-efficient materials and the use of materials or delivery of end items with the specified recovered material content. This shall occur as part of the quality assurance procedures set forth in part 46.
(ii) As required in the contract, ensuring that the contractor complies with the reporting requirements relating to recovered material content utilized in contract performance.

(69) Administer commercial financing provisions and monitor contractor security to ensure its continued adequacy to cover outstanding payments, when on-site review is required.

(b) The CAO shall perform the following functions only when and to the extent specifically authorized by the contracting office:

(1) Negotiate or negotiate and execute supplemental agreements incorporating contractor proposals resulting from change orders issued under the Changes clause. Before completing negotiations, coordinate any delivery schedule change with the contracting office.

(2) Negotiate prices and execute priced exhibits for unpriced orders issued by the contracting officer under basic ordering agreements.

(3) Negotiate or negotiate and execute supplemental agreements changing contract delivery schedules.

(4) Negotiate or negotiate and execute supplemental agreements providing for the deobligation of unexpended dollar balances considered excess to known contract requirements.
(5) Issue amended shipping instructions and, when necessary, negotiate and execute supplemental agreements incorporating contractor proposals resulting from these instructions.

(6) Negotiate changes to interim billing prices.

(7) Negotiate and definitize adjustments to contract prices resulting from exercise of an economic price adjustment clause (see Subpart 16.2).

(8) Issue change orders and negotiate and execute resulting supplemental agreements under contracts for ship construction, conversion, and repair.

(9) Execute supplemental agreements on firm-fixed-price supply contracts to reduce required contract line item quantities and deobligate excess funds when notified by the contractor of an inconsequential delivery shortage, and it is determined that such action is in the best interests of the Government, notwithstanding the default provisions of the contract. Such action will be taken only upon the written request of the contractor and, in no event, shall the total downward contract price adjustment resulting from an inconsequential delivery shortage exceed $250.00 or 5 percent of the contract price, whichever is less.

(10) Execute supplemental agreements to permit a change in place of inspection at origin specified in firm-fixed-price supply contracts awarded to nonmanufacturers, as deemed necessary to protect the Government's interests.
(11) Prepare evaluations of contractor performance in accordance with Subpart 42.15.
APPENDIX B. OFFICE OF FEDERAL PROCUREMENT POLICY (OFPP)
POLICY LETTER 91-2

Executive Office of the President
Office of Management and Budget
Washington, DC 30683

April 9, 1991

POLICY LETTER 91-2

TO THE HEADS OF EXECUTIVE AGENCIES AND DEPARTMENTS

SUBJECT: Service Contracting

1. Purpose. This Policy Letter establishes policy for the
   Government's acquisition of services by contract. It
   emphasizes the use of performance requirements and
   quality standards in defining contract requirements,
   source selection, and quality-assurance. This approach
   provides the means to ensure that the appropriate
   performance quality level is achieved, and that payment
   is made only for services which meet contract
   standards.

2. Authority. This Policy Letter is issued pursuant to
   section 6(a) of the Office of Federal Procurement
   Policy (OFPP) Act, as amended, codified at 41 U.S.C.
   section 405.

3. Definitions.

   a. "Performance-based contracting" means structuring all
      aspects of an acquisition around the purpose of the
      work to be performed as opposed to either the manner by
      which the work is to be performed or broad and
      imprecise statements of Work.

   b. "Services" are defined as the performance of
      identifiable tasks rather than the delivery of an end
      item of supply. "Services" also include tasks that are
      delivered under a contract where the primary purpose is
      to provide supplies. For the purpose of this Policy
      Letter architect-engineer services acquired in
      accordance with the Brooks Act (P.L. 92-582, as
      amended) and for construction are excluded.
4. **Background.** Each year the government contracts for a significant amount of services. Such services range from the routine maintenance of facilities or equipment to highly sophisticated technical and management assistance such as the design, development and furnishing of systems, or expert assistance for management and program activities. Attempts to apply contracting methods which are inappropriate to the services being acquired have often resulted in unsatisfactory performance and contract administration problems, as reflected in several internal agency investigations and evaluations, General Accounting Office Reports, and OFPP studies. These reports criticized unnecessarily vague statements of work, insufficient use of firm pricing arrangements, the lack of quantifiable performance standards, and the inadequacy of quality assurance surveillance. In addition, there is concern that the Government underemphasizes quality vs. price in the acquisition of services. The use of performance-based service contracting methods enhances the Government's ability to acquire services of the requisite quality and to ensure adequate contractor performance.

5. **Policy.** It is the policy of the Federal Government that (1) agencies use performance-based contracting methods to the maximum extent practicable when acquiring services, and (2) agencies carefully select acquisition and contract administration strategies, methods, and techniques that best accommodate the requirements. In addition, agencies shall justify the use of other than performance-based contracting methods when acquiring services, and document affected contract files. Performance-based contracting methods consist of the following:

- **a. Statement of work.** When preparing statements of work, agencies shall, to the maximum extent practicable, describe the work in terms of "what" is to be the required output rather than "how" the work is to be accomplished. To assist in refining statements of work, consideration shall be given to issuing draft solicitations.

- **b. Quality assurance.** Agencies shall, to the maximum extent practicable, assign contractors full
responsibility for quality performance. Agencies shall develop formal, measurable (i.e., in terms of quality, timeliness, quantity, etc.) performance standards and surveillance plans to facilitate the assessment of contractor performance and the use of performance incentives and deduction schedules. Agencies shall, to the maximum extent practicable, avoid relying on cumbersome and intrusive process-oriented inspection and oversight programs to assess contractor performance.

c. Selection procedures. Agencies shall use competitive negotiations for acquisitions where the quality of performance over and above the minimum acceptable level will enhance agency mission accomplishment and be worth the corresponding increase in cost. This approach will apply to most technical and professional services. In such instances, contracting activities shall give careful consideration to developing evaluation and selection procedures that utilize quality-related factors such as: technical capability; management capability; cost realism; and past performance. These factors shall receive increased emphasis to the extent requirements are more complex and less clearly defined. The desired relative importance among these factors and between these factors and price shall be determined, and they shall be applied as stated in the solicitations. To ensure application of cost realism, cost proposals shall be reviewed to assess offerors' understanding of the requirements and consistency with their technical proposals. Special attention shall be directed to limited opportunities for technical leveling and technical transfusion. Technical leveling and technical transfusion discourages offerors from proposing innovative methods of performance and often result from repeated discussions and the submission of revised offers based on these discussions. Opportunities for discussions and revisions of offers shall be limited to the extent practicable. Sealed bidding shall be used when the goal of the acquisition is to achieve the desired service at the lowest price with minimum stated acceptable quality.

d. Contract type. Contract types most likely to motivate contractors to perform at optimal levels hall be
chosen. Fixed price contracts are appropriate for services that can be objectively defined and for which risk of performance is manageable. In most instances, services that are routine, frequently acquired, and require no more than a minimal acceptable level of performance fall into this category. For such acquisitions, performance-based statements of work and measurable performance standards and surveillance plans shall be developed and fixed price contracts shall be preferred over cost reimbursement contracts. Cost reimbursement contracts are appropriate for services that can only be defined in general terms and for which the risk of performance is not reasonably manageable. Complex or unique services for which quality of performance is paramount frequently fall into this category. Furthermore, to the maximum extent practicable, contracts shall include incentive provisions to ensure that contractors are rewarded for good performance and quality assurance deduction schedules to discourage unsatisfactory performance. These provisions shall be based on measurement against predetermined performance standards and surveillance plans.

e. Repetitive requirements. When acquiring services, which previously have been provided by contract, agencies shall rely on the experience gained from the prior contract to incorporate performance-based acquisition methods. For such follow-on requirements, statements of work shall further describe the services in terms of "what" is to be performed, and performance standards and surveillance plans shall be more definitive than those for the prior acquisition. Where appropriate, conversion from a cost reimbursement to fixed price arrangement shall be accomplished and, whenever possible, incentive provisions and quality assurance deduction schedules shall be introduced.

f. Multiyear contracting. Agencies with statutory multiyear authority shall consider the use of such authority when acquiring services. The use of such authority will increase competition by offering a more stable, long-term contracting environment. It will also encourage offerors to invest in the development and implementation of innovative and efficient methods of performance by ensuring recoupment of these investments.
6. **Responsibilities.**

   a. Federal Acquisition Regulatory Council. The Federal Acquisition Regulatory Council shall ensure that Government-wide regulations to conform to the policies established herein are promulgated in the first Federal Acquisition Circular issued 120 days after the effective date of this Policy Letter. These regulations shall include a framework for individually tailoring the source selection method, type of contract, and contract administration techniques to fit the requirement, and for agencies to document the reasons(s) for not using performance based contracting methods as prescribed by that framework.

   b. Heads of Agencies. Heads of agencies are encouraged to implement the policies established herein and initiate any necessary staff training upon the effective date of this Policy Letter.

7. **Information Contract.** For information regarding this Policy Letter contract Stanley Kaufman, Deputy Associate Administrator, Office of Federal Procurement Policy, 725 17th Street, NW, Washington, DC 20503, telephone (202) 395-6803.

8. **Effective Date.** This Policy Letter is effective 30 days after the date of issuance.

   (signed by)
   Allan V. Burman
   Administrator

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APPENDIX C. INTERVIEW QUESTIONS

To the Interviewee, (please excuse the informal greeting)

My name is LT. Michael L. Renegar and I am working towards obtaining a Masters Degree in Acquisition and Contracts Management at the Naval Postgraduate School in Monterey, California. I am using interview questions, listed below, as the basic approach to researching my thesis and would like to solicit your views based on experience and knowledge referring to the subject of performance-based service contracting (PBSC).

The title of my thesis research is "Guidance for Transitioning to Performance-Based Service Contracting - A Guide for Department of Defense Field Contracting Activities". My objective is evaluate the transition to PBSC and develop a guide to implement an effective PBSC program. Your extensive contracting background and knowledge will be invaluable to me as I analyze PBSC and develop ideas for a PBSC program. I look forward to talking with you and incorporating your expertise in an effort to more effectively and efficiently manage the process by which the Federal Government contracts for services.

If you have any questions, I can be contacted via e-mail (mlrenegar@nps.navy.mil) or phone 831-394-5386.

Sincerely,

Michael L. Renegar

**********************************************************************************************

Interview Questions to Determine the Effectiveness and Efficiency of Transitioning to Performance-Based Service Contracting (PBSC)

1. What are the potential barriers that may be encountered with the administration of PBSC? What procedures and practices have you implemented to overcome barriers associated with PBSC?
2. What benefits can be realized as a result of implementing an effective PBSC program?

3. Can you explain what contract types are best suited for PBSC? Why?

4. What improvements (laws, regulations, and policies) would you like to see added/changed that would make PBSC administration more effective and efficient?

5. What skills/training requirements are necessary to effectively transition to PBSC? Have resources been made available to satisfy these requirements in the implementation of PBSC?

6. How do you measure the performance of the contractor under a performance-based service contract? Can you explain the effectiveness of the Quality Assurance Plan (QAP) or Surveillance Plan?

7. What are the procedures and practices used to ensure that service requirements are correctly identified in a Performance-Work Statement or Statement of Objective? What are some problems with improperly defined service requirements?
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24. Kay, Bob, Deputy Director of Regional Contracts, FISC-Pearl Harbor, Pearl Harbor, HI., 18 May 2000.


27. Clemmons, Dave, Contracting Officer, FISC-Pearl Harbor, Pearl Harbor, HI., 22 May 2000.
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