4.0 Chapter Introduction

Noncompetitive Contract Negotiations (FAR 15.306(d)(1)). Noncompetitive contract negotiations are exchanges that take place between the Government and a single contractor. They may take place before or after contract award.

The pattern of negotiations can vary significantly depending on the number, magnitude, and complexity of the issues involved, as well as the personalities of the negotiators. For example,

- The time required to complete negotiations can vary from a few minutes to several months.
- The number of negotiation sessions can vary from one to twenty or more.
- A single negotiator may preside at every negotiation session or different negotiators may take the lead in addressing different issues.

Procedural Steps. The following flowchart outlines the information presented in this chapter:
4.1 Recognizing The Steps Of Negotiation

Principal Negotiator Responsibilities. The principal negotiator must assume Government negotiation team leadership responsibility during the negotiation conference even if the principal negotiator is not the team leader at other times. This includes:

- Actively leading the team throughout the conference;
- Opening the negotiation conference;
- Obtaining any additional facts needed to support continued proposal analysis and negotiation;
- Reviewing facts and identifying negotiation issues;
- Bargaining on the issues;
- Reaching agreements on the issues; and
- Closing the negotiation conference.
Actively Leading the Government Team. The negotiation team must be more than a group of individuals representing the Government. From the beginning of the negotiation conference, the team must function as a single entity. This requires preparation before the negotiation conference and active leadership throughout the conference.

- **Assure That Preparations Are Complete Before Opening the Negotiation Conference.** Before every negotiation session assure that all necessary preparations are complete. In particular, you should assure that the meeting room is properly set up and that team members are available and prepared to perform their assigned roles in implementing the negotiation plan.

- **Assure That Team Support Is Available When Needed.** Normally, the number of Government team members participating in any negotiation session should be as small as practical, but large enough to provide the support required.
  - Consider having the entire team present for the opening of negotiation. This permits everyone to hear the opening comments and participate in the introductions. It also visually demonstrates that the Government position is a team position, not your personal position.
  - For other sessions, you should only include team members whom you expect will actively participate in the session. If you expect to discuss direct material, why have the direct labor expert present? The direct labor expert will likely contribute little to the session, but will be unable to perform other duties while sitting at the negotiation table.

- **Control Team Member Participation.** Exercise the positive control necessary to ensure effective communications while presenting a unified position to the contractor's team.
  - Ask for support when you need it to clarify or emphasize a negotiation position.
  - Interrupt when team members enter into an uncontrolled discussion with the contractor. For example, you might say "I'm going to interrupt you because I think we're getting off the track" or "I'm a little unclear on this point myself, and I'd like to discuss this privately with the team before we continue."
Do not permit side conversations between team members and the contractor's team. The noise from side conversations interferes with the negotiation exchange. There is also a good chance that the team member involved could say things that appear to conflict with the Government position.

- **Use Caucuses to Maintain a Unified Government Position.** In negotiations, a caucus is a team meeting to review and, when appropriate, adjust the team position.
  - Use a caucus when you need to:
    - Consult with other team members either in person or by telephone.
    - Restore your control of team participation in the negotiation.
    - Divert the negotiations from sensitive issues or areas of weakness. After the caucus resume negotiations on a different subject.
    - Emphasize to team members that they should request a caucus if you appear to have missed an important point or it appears that you are not taking advantage of a negotiation opening provided by the contractor's team.
    - Hold your caucus in an area away from the contractor's team.
  - For a short caucus (e.g., 30 minutes or less):
    - Move to another room if possible.
    - If another room is not available, consider asking if the contractor's team would allow you to use the negotiation conference room in private for the caucus.
    - If necessary, caucus in the hallway or some other place where you can prevent others from listening.
  - For a longer caucus, suggest that both teams break from negotiations and return at a preset time.

- **Use Breaks to Relieve Tension and Control the Pace of Negotiations.** A break provides both teams time away from the conference table, as well as an opportunity to privately assess new information and reevaluate the team's position.
  - You may call for a break anytime. You might take a:
    - Short break to provide an opportunity to go to the rest room and get some refreshment;
o Longer break in conjunction with lunch; or
o A still longer break overnight, over a weekend, or even over several weeks.
o Consider calling a break when you want to:
o Provide relief from the stress of the negotiation;
o Give the contractor's negotiator an opportunity to reevaluate the contractor's position or consider a possible concession;
o Help restore a cordial and unemotional atmosphere after someone has made a provocative or emotional statement; or
o Calm down an individual who has become contentious.

Opening the Negotiation Conference. The opening negotiation session is critical, because it sets the stage for the rest of the negotiation conference. It can positively or negatively influence the attitudes that will prevail throughout the conference and significantly affect the probability of a win/win agreement.

- **Greet the Contractor's Team.** Extend a cordial greeting to members of the contractor's negotiation team.
  o Welcome team members as they arrive;
  o Shake hands with all team members if practical;
  o Create a cordial atmosphere by exchanging pleasantries and compliments. At the very least, express appreciation for the contractor's support in the acquisition process.

- **Take Time for Introductions.** Introductions may not be necessary if all the participants know each other. Otherwise, the few minutes required for introductions will pay dividends throughout the negotiation.
  o You may introduce each Government team member yourself or you may have team members introduce themselves. Each introduction should include full name, title or position, and the person's role in the negotiation.
  o Suggest similar contractor team introductions.
  o To help participants remember each others' names, consider providing an attendance roster or nameplates for all team members at the conference table. If the nameplates have been prepositioned on the table, allow time for the contractor's team to rearrange seating in accordance with their seating preference.
• **Help Attendees Feel More at Ease.** Casual conversation often dispels the tension present during every negotiation and helps attendees feel more at ease.

• **Briefly Review Background Information.** Facilitate mutual understanding, by reviewing information related to the contract action under negotiation. In particular, identify any unusual constraints (e.g., imminent expiration of funds) that may affect the negotiation process.

• **Emphasize the Goal of a Win/Win Outcome.** Point out the Government's interest in fairness and a win/win result. Indicate that you assume that the contractor shares that interest.

• **Review the Negotiation Agenda.** Briefly, review the negotiation agenda. When appropriate, provide a written copy for each participant. Then ask for comments from the contractor team. Specifically ask if there are any items that need to be added to the agenda.

**Reviewing Facts And Identifying Negotiation Issues.** Review contract requirements and the contractor's proposal to assure that you have identified key negotiation issues.

• **Pay Special Attention to Areas Where Issues Are Common.** Ensure that both parties have the same understanding of the:
  - Required contract effort;
  - Contract terms and conditions;
  - Exceptions to Government terms and conditions proposed by the contractor; and
  - Facts, assumptions, and judgments submitted by the contractor as part of its proposal.

• **Summarize the Results of Any Prenegotiation Exchange.** If an exchange preceded the formal negotiation conference, summarize the results of that exchange.

• **Conduct Additional Fact-Finding When Necessary.** Before proceeding with the negotiation conference ensure that both parties feel that the general facts and issues are clear.
  - If the general facts and issues are not clear, conduct additional fact-finding before opening negotiations. Fact-finding should follow the same general guidelines used for conducting prenegotiation exchanges.
• Fact-finding does not necessarily end once bargaining begins. Additional fact-finding may be necessary whenever additional issues arise.

• **Summarize Areas of Agreement and Issues for Negotiation.** Sometimes an attempt to summarize areas of agreement will identify issues not previously identified. It is better to identify them now rather than after negotiations are complete.

Bargaining on the Issues. Bargaining includes persuasion, alteration of assumptions and positions, as well as give and take on the issues including price, schedule, technical requirements, contract type, or other terms of the proposed contract. In noncompetitive negotiation, bargaining involves offers and counteroffers to define changes in the contractor or Government positions. Bargaining continues until the two parties reach agreement or one party decides that agreement cannot be achieved.

• **Follow Your Negotiation Plan.** Maintain the initiative throughout discussions by following your negotiation plan.
  o Use your agenda to address the issues.
  o Ask questions. Listen and evaluate the answers for responsiveness, truth, and consistency. Listening will minimize the probability of misunderstanding and show that you have a genuine interest in what the contractor's negotiator is saying.
  o Employ appropriate tactics and countermeasures to achieve win/win results.

• **Begin Bargaining With Issues Related to Contract Requirements.** Begin bargaining by seeking agreement on the contract requirements.
  o When addressing contract requirements, always consider potential effects on contract price. Remember that any contract requirement may significantly affect contract cost and price. Do not get boxed into a high price by "gold plating" contract requirements.
  o However, you should consider possible trade-offs between technical requirements and contract price until a final agreement. For example, a lower contract price might be possible if you increase the period of time between contract award and required delivery.
• **Bargain on Price After Agreement on Technical Issues.**

Once you have an agreement on contract requirements, you can proceed with bargaining on contract price.

  o Tailor price negotiations to the contract type. When you negotiate a firm fixed-price contract, you can limit your price agreement to total contract price. For other types of contracts, you will need to negotiate more than one contract element to define contract price. For example, when negotiating a fixed-price incentive firm contract, you must agree on target cost, target profit, share-ratio over target, share-ratio under target, and ceiling price.

  o Bargain for a fair and reasonable price. That means you should be willing to negotiate up when the proposed price is unreasonably low or negotiate down when the proposed price is unreasonably high. Remember that your pricing objective should be a price that is:

    o Fair to the buyer;
    o Fair to the seller; and
    o Reasonable considering market conditions, available alternatives, price-related factors, and non-price factors.

  o When bargaining is based on price analysis comparisons:

    o Share information on the bases that you used to develop your estimate of a fair and reasonable price unless the information is confidential or proprietary; and

    o Remember that you need to persuade the contractor's negotiator that your price is more reasonable than the contractor's.

  o When bargaining is based on cost analysis:

    o Begin by examining the contractor's work design and its affect on key elements of cost and profit/fee.

    o Typically, you should address contract costs in the following order:

      ▪ Direct costs (e.g., materials, labor, and other) of performing the work;
      ▪ Indirect costs (e.g., such as overhead and general and administrative expense; and
      ▪ Profit or fee.

    o Do not require agreement on every cost element.

    o Consider available bases for price analysis. Do not get lost in contract cost information. Your
goal should always be a price that is fair and reasonable.

Reaching Agreements on the Issues. As you bargain, remember that you need an agreement that considers all the issues, but you do not have to reach agreement on every issue. For example, you do not have to agree on every issue related to contract cost as long as you can agree on a fair and reasonable contract price.

- **Periodically Review Areas of Agreement.** Review areas of agreement before you begin bargaining and periodically throughout negotiations until you have an overall agreement. Periodic reviews tend to reinforce areas of agreement and demonstrate that the areas of agreement are more significant than the areas of disagreement.

- **Sequence the Areas of Disagreement.** There are several different approaches to sequencing bargaining on areas of disagreement. No one approach is necessarily better than another. The issues being negotiated, circumstances surrounding the negotiation, and the negotiating styles of the negotiator determine the method most likely to succeed. Moreover, predictable patterns may not even be desirable when regularly negotiating with the same party. Approaches include:
  o Negotiating the issues of greatest importance first and then addressing the secondary issues.
  o As each issue comes up, try to reach agreement.
  o If agreement cannot be reached, lay the issue aside and move on to the next.
  o Once you begin discussing issues of secondary importance, you can attempt to trade these secondary issues for the more important unresolved issues.
  o Negotiating secondary issues first and then addressing the issues of greatest importance.
  o It is often easier to reach agreement on secondary issues and success creates a climate of mutual cooperation.
  o The climate of mutual cooperation makes it easier to reach agreement on the more important issues.
  o Negotiating the contractor's demands first.
  o By first making concessions on issues important to the contractor, you create a win/win environment and are more likely to receive comparable concessions.
- This approach carries obvious risks.
  - The contractor may not be motivated by Government concessions. Why concede after your major demands have been addressed?
  - The contractor's expectations may actually increase. When all the contractor's demands are met, more may appear.
- Negotiate the Government's demands first. This is the opposite of the approach above.
- By first reaching agreement on issues important to the Government, you put yourself in a better position to make concessions and foster a win/win environment.
- This approach also carries risks. The most obvious is that the contractor will perceive unreasonable Government demands and refuse to bargain.

- **Use Mutual Problem Solving to Reach Agreements.** Your initial approach to resolving issues should be to:
  - Work with the contractor's negotiator to identify alternatives. Together, you may be able to identify alternatives that are better than any of the original positions. Brainstorming is often useful for this purpose.
  - Consider the acceptability of identified alternatives. Most alternatives will likely be unacceptable to one side or the other. However, there may be several that are acceptable.
  - Select the best alternative. Most often, you will be fortunate to find a single alternative that is acceptable to both parties. However, if there are multiple alternatives, select the one that provides the highest mutual satisfaction. For example, the Government wants the technical data available for competitive follow-on acquisitions while the contractor does not want to give competitors access to proprietary information. The seemingly unresolvable problem can often be worked out by contractual language that protects the rights of both parties.

- **Use Tradeoffs to Reach Agreements.** Some issues involve differences that do not lend themselves to resolution through problem solving. Each party feels that its position is more reasonable based on the available information. When you encounter such issues, consider attempting to reach agreement through tradeoffs.
When you make a concession, attempt to obtain a concession of at least equal importance in return. The concession may be on the same issue or a different issue. Remember that a concession that is relatively unimportant to you may be very important to the contractor.

Any offer that you make should be supportable and represent a reasonable position. Provide sufficient support to convincingly demonstrate its merits.

Be prepared to sometimes make concessions that represent real sacrifices in the interest of a win/win outcome.

- **Keep a Written Record of Offers, Counteroffers, Agreements, and Unresolved Issues.** This list can be helpful in defining current positions on resolved and unresolved issues.

- **Reach Agreement.** Do not prolong discussions any longer than necessary. Instead, seize the moment to finalize a good agreement. If the contractor's negotiator is reluctant:
  
  - Emphasize the advantages of the proposed agreement;
  
  - Offer assurances, such as, "This is a good agreement for everyone," or "I am confident that we both have a good deal;" and
  
  - Focus attention on your intent to finalize an agreement to provide the final push needed for acceptance.

**Closing the Negotiation Conference.** Close the negotiation conference as soon as possible once an agreement is reached.

- **Review Key Elements of the Agreement.** A review will protect negotiators from finding out later that they actually agreed to different things.

- **Offer a Handshake on the Agreement.** A handshake is a symbolic gesture of mutual agreement.

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**4.2 Recognizing Differences Between Pre- And Post-Award Negotiations**

This section will examine unique points to consider when negotiating post-award contract actions:
Different Post-Award Negotiations. Two types of post-award negotiations will be examined in this section:

- Equitable adjustment under one of several different contract clauses; and
- Settlement under one of the contract termination clauses.

Negotiation Similarities. While this section concentrates on negotiation differences, remember that there are more similarities than differences. Whether you are negotiating before or after contract award, you must:

- Strive for win/win results;
- Conduct exchanges with the contractor prior to contract negotiations when necessary to establish the facts and issues related to the negotiation;
- Prepare effectively for the negotiation including development and, if necessary, approval of a negotiation plan; and
- Use the negotiation plan and your negotiation skills to obtain a mutually satisfactory result.

4.2.1 Recognizing Special Considerations For Equitable Adjustments

Clauses Providing for Equitable Adjustment (FAR 52.236-2, 52.242-14, 52.242-15, 52.242-17, 52.243, 52.245-2, and 52.245-4).

You may need to negotiate an equitable adjustment under one of several different contract clauses that provide for an equitable adjustment in certain situations. These include the:

- Changes clause;
- Government Property clause;
- Suspension of Work clause;
- Government Delay of Work clause;
- Stop-Work Order clause; or
- Differing Site Conditions clause.

Unilateral and Bilateral Modifications (FAR 43.101, 43.103, 52.212-4(c), and 52.243-1).

There are two basic types of contract modifications permitted under the contract Changes clause:

- **Bilateral modifications** are signed by both the contractor and the contracting officer. You can use them to:
  - Define all aspects of the contract modification, including an equitable adjustment, at the time that the modification is made;
  - Incorporate a negotiated equitable adjustment that resulted from a unilateral contract change, or;
  - Definitize a letter contract.

- **Unilateral modifications** are signed only by the contracting officer and do not require contractor consent.
  - Unilateral modifications are not permitted under the standard FAR Contract Terms and Conditions -- Commercial Items clause. However, the clause may be tailored to provide for unilateral contract modification.
  - Unilateral modifications are permitted under the Changes clauses for all noncommercial contracts.
  - You can use a unilateral contract modification to direct the contractor to modify any of the contract elements specified in the relevant contract Changes clause.
  - The contractor is required to continue performance of the contract as changed and can request an equitable adjustment within the period prescribed in the clause.

Preference for Bilateral Modifications (FAR 43.204(b)). When time permits, the contracting officer should generally modify contract requirements using a bilateral contract modification for three reasons:

- Only one contract document is required.
  - If you make a bilateral contract modification, you can use a single document to modify the contract requirements and incorporate any necessary equitable adjustment.
If you make a unilateral contract modification, you must use one document to make the contract modification and a second document to incorporate any necessary equitable adjustment.

- The equitable adjustment is established before work begins. When you use a unilateral contract modification, the contractor must continue to perform the modified contract.
- While continuing to perform, the contractor incurs actual costs related to the change. As a result the contractor's proposal for an equitable adjustment must include a combination of actual and estimated costs. Each day work is completed so actual costs change and the estimated cost for uncompleted work changes. Negotiations are like trying to hit a constantly moving target.
- Each day of contractor performance reduces the possibility that you can further influence how the contractor will interpret the modified contract requirements.

Contracting officers must definitize unilateral modifications within the shortest practicable time. Contracting officers commonly perceive this requirement as additional pressure for timely settlement on them but not on the contractor.

Other Reasons for Equitable Adjustments. An equitable adjustment may also be necessary when:

- Either the Government or the contractor fails to meet its contract obligations. (e.g., the Government fails to deliver Government furnished property when and where required); or
- There is a change in the contracting situation (e.g., a differing site condition on a construction contract).

Equitable Adjustment Objective. As the term implies, your objective should be an "equitable" adjustment. FAR does not define the term "equitable." Instead the Government relies on the judgment of the contracting officer and precedents established by the Courts and Boards of Contract Appeals. In general, an equitable adjustment is one that is fair to all concerned. Many define it as leaving the contracting parties in a position no better or worse than before the action or inaction that necessitated the adjustment.
**Equitable Adjustment Elements.** An equitable price adjustment should consider changes in contract price and other terms affected (e.g., schedule).

- Price changes should consider the reasonable cost of completing the contract before the act that necessitated the adjustment and the reasonable cost of performing the contract after it.
- Contract terms (e.g., schedule) should consider the effect of the act on contract performance. For example, production must stop because parts that meet new requirements will not be available at any price for six months, but parts that met the original requirements were in stock.
- Elements of the adjustment can be traded off. For example, when contract requirements increase, the contractor might request a higher price to make the change and meet the required delivery schedule. However, the contractor might accept a lower price increase if you extend the delivery schedule.

**Special Problems in Equitable Adjustment Negotiation.** An equitable adjustment negotiation often presents special negotiation problems. The biggest problems are usually related to adjusting contract price. As stated above, the objective is a fair adjustment that leaves the contracting parties in a position no better or worse than before the action or inaction that necessitated the adjustment.

The preferred method of pricing the adjustment is by negotiating the difference between the reasonable cost of performing the contract before the action or inaction that necessitated the adjustment and the reasonable cost after. Depending on the type of equitable adjustment profit may or may not also be adjusted.

The main problem is deciding what costs are reasonable:

- The same rules on cost allowability that apply to new contract negotiations also apply to equitable adjustments. Unfortunately, many contractors not familiar with cost negotiations often do not understand that they cannot recoup such unallowable costs as interest expense.
- You may have to rely on the opinions of experts concerning actual costs incurred by the contractor.
This is particularly likely when the contractor does not have an adequate cost accounting system.

- You may have to rely on the opinions of experts concerning work actually completed. This is particularly likely when the contractor does not have a well documented system for managing contract performance. This is a special problem if the contractor overestimates the work completed to support an unreasonably low estimate of the cost of work deleted and not performed.
- Most contractors are very reluctant to accept estimates showing that the costs for work deleted would have been more than estimated at the time of contract award. Some look at equitable adjustments as an opportunity to recoup losses associated with unrealistically low cost estimates at the time of contract award.

Contractor Advantages in Equitable Adjustment Negotiation.
An equitable adjustment negotiation may provide the contractor with negotiation advantages not present before contract award.

- Negotiations are noncompetitive. Pricing alternatives on the original contract may have been limited by competition.
- Contracting officers have time limits to complete definitization of unilateral contract modifications. Those limits increase pressure on the contracting officer to complete negotiations. However, they do not directly increase pressure on the contractor.
- While performing under a unilateral modification, the contractor is incurring actual costs. The fact that the costs have already been incurred provides strong support for the position that the costs are reasonable.

Government Advantages in Equitable Adjustment Negotiation (FAR 31.201-3(a)). An equitable adjustment negotiation may also provide the Government with negotiation advantages that it did not have in the original contract award.

- The contractor performance must continue, so the Government is not faced with a lack of progress in meeting its needs.
- Payment for affected items delivered may be withheld until unit prices have been adjusted as part of the
equitable adjustment, increasing pressure on the contractor to negotiate.

- The contractor is incurring actual costs, but you are precluded from paying any cost that is not reasonable (actual cost or not). Until the adjustment is consummated, the contractor assumes the risk that its actual costs will be accepted as reasonable. As this actual cost increases, so does the pressure to negotiate.
- The clauses that provide for equitable adjustment also provide for a unilateral contracting officer decision if no agreement can be reached. Of course, the contractor can dispute the decision, but the process is expensive and long. Most importantly, there is no guarantee that the dispute will be successful, particularly when the contracting officer's final decision is reasonable.

**Win/Win Benefits of Negotiated Adjustments.** A negotiated agreement is generally a better deal for both sides because:

- A unilateral contracting officer's decision may give the impression of being win/lose no matter how reasonable it is.
- Disputes are long and expensive for both parties involved.
  - If the Government wins, the contracting officer's decision may still appear one-sided to the contractor.
  - If the contractor wins, it appears that the Government adopted a win/lose position and lost.

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**4.2.2 Recognizing Special Considerations For Termination Settlements**

Contract Terminations ([FAR 49.101](https://www.acq.osd.mil/far/part49appA.html)). There are two general types of contract terminations.

- **Termination for Convenience.** The contract termination for convenience clause gives the Government the right to terminate the contract when it is in the Government's best interest to do so. Specific provisions for settlement will depend on the
commercial or noncommercial nature of the product and the contract type.

- **Termination for Default or Cause.** The contract termination for default clause or termination for cause clause gives the Government the right to terminate the contract when the contractor fails to meet its obligations under the contract. Specific Government rights depend on the commercial or noncommercial nature of the product and the contract type.

*Termination Settlement Negotiation (FAR 52.212-4, 52.249-1, 52.249-2, 52.249-6, and 52.249-8).*

Noncommercial fixed-price termination for convenience settlements typically require more and more complex negotiations than any other type of termination settlement.

- Commercial contract termination for convenience settlements center on determining the percentage of contract work performed prior to the notice of termination and reasonableness of charges related to the termination. The termination settlement is calculated by multiplying the contract price by the percentage of work performed and adding the reasonable charges related to the termination.
- Cost-reimbursement contract terminations for convenience require little negotiation because the contractor is entitled to receive all allowable costs and any related fee.
- Settlements for terminations for default or cause normally require little negotiation because the general requirements for settlement are described in the clause. In fact, most negotiations related to terminations for default or cause involve contractor efforts to convince the Government that there are factors that justify converting the termination for default or cause into a termination for convenience.

*Noncommercial Fixed-Price Termination for Convenience Settlement Objective (FAR 49.201(a) and 49.201(b)).*

For a noncommercial fixed-price contract termination for convenience, your objective should be a settlement that compensates the contractor *fairly* for the work done and the preparations made for the terminated portions of the contract including a reasonable allowance for profit.
Fair compensation is a matter of judgment and cannot be measured exactly.

Various methods may be equally appropriate for arriving at fair compensation.

The use of business judgment, as distinguished from strict adherence to accounting principles, is the heart of settlement.

The parties may agree upon a total amount to be paid to the contractor without agreeing on or segregating the particular elements of cost or profit comprising that total.

Noncommercial Fixed-Price Termination for Convenience Guides for Settlement (FAR 49.201 and 49.207).

The primary objective is to negotiate a settlement by agreement.

Cost and accounting information provide guides for negotiating a fair settlement, but they are not a rigid measure.
- In appropriate cases, costs may be estimated, differences compromised, and doubtful questions settled by agreement.
- Other types of data, criteria, or standards may furnish equally reliable guides for fair compensation.

The amount payable under a settlement (not including settlement costs) must not exceed the contract price less payments otherwise made under the contract. From that amount you must deduct any disposal or other credits.

Special Problems in Fixed-Price Terminations for Convenience Settlement Negotiation. A fixed-price contract termination for convenience settlement negotiation may also present special problems.

The biggest problem is often the atmosphere surrounding the termination process. While the atmosphere surrounding a new contract negotiation is one of hope and a new beginning, the atmosphere surrounding a termination is one of lost opportunities. Many times it is an atmosphere of distrust and resentment. You must not allow this atmosphere to drag you into a win/lose negotiation.
• Contractors are required to submit final settlement proposals within one year of the contract termination but the period for submission can be extended by the termination contracting officer. The long period of time between the termination and settlement negotiation can affect the availability of information and your ability to verify the facts surrounding the termination. Work in process inventory, special tooling, special test equipment, or important records may be lost during this extended period of time. Costs incurred after the termination may be mixed with costs incurred before the termination.
• The same rules on cost allowability that apply to new contract negotiations and equitable adjustments also apply to termination settlements. Unfortunately, many contractors not familiar with cost negotiations often do not understand that they cannot recoup unallowable costs.
• You may have to rely on the opinions of experts concerning actual costs incurred by the contractor. This is particularly likely when the contractor does not have an adequate cost accounting system.
• In a partial termination settlement, the contractor may propose increased costs in the continued portion of the contract related to the termination. Never consider these costs as part of the termination settlement. However, you may consider the need for a separate equitable adjustment.

Contractor Advantages in Fixed-Price Termination for Convenience Settlement Negotiation. A fixed-price contract termination for convenience settlement negotiation may provide the contractor with negotiation advantages not present before contract award.

• Negotiations are noncompetitive. Pricing alternatives on the original contract may have been limited by competition.
• When the contractor's accounting system permits cost identification and tracking, actual costs should be available. There should be few cost estimates.

Government Advantages in Fixed-Price Termination for Convenience Settlement Negotiation (FAR 52.249-2(g)).

A fixed-price contract termination for convenience settlement negotiation may also provide the Government with
negotiation advantages that it does not have in the original contract award.

- Normally, the Government will owe the contractor additional funds when the settlement is reached. This should increase the contractor's desire to reach an agreement.
- The fixed-price termination for convenience clause permits the contracting officer to unilaterally settle the termination by paying the amounts determined reasonable. Of course, the contractor can dispute the determination, but the process is expensive and long. Most importantly, there is no guarantee that the dispute will be successful, particularly when the contracting officer's determination is reasonable.

Win/Win Benefits of Negotiated Settlements. A negotiated agreement is generally a better deal for both sides.

- A unilateral contracting officer settlement determination gives the impression of being win/lose no matter how reasonable it is.
- Disputes are long and expensive for both parties involved.
  - If the Government wins, the contracting officer's determination may still appear one-sided to the contractor.
  - If the contractor wins, it appears that the Government adopted a win/lose position and lost.

4.3 Identifying Documentation Requirements

Need for Documentation. Documentation must identify the significant facts and issues that affected the negotiated contract price. As a minimum, it should include:

- The proposal and any related information submitted by the contractor;
- The Price Negotiation Memorandum (PNM);
- Copies or references to the location of any technical or audit analysis reports considered during the negotiation; and
- A record of any request for additional contractor information to support the proposal and the contractor's response.
Price Negotiation Memorandum (FAR 15.406-3). At the close of each negotiation, you must promptly prepare a PNM outlining the principle elements of the contract negotiation and include a copy in the contract file. Formats vary, but the PNM must include the following information:

- Purpose of the negotiation (new contract, final pricing, etc.)
- Description of the acquisition, including appropriate identifying numbers (e.g., RFP number).
- Name, position, and organization of each person representing the contractor and the Government in negotiations.
- The current status of any contractor systems (e.g., purchasing, estimating, accounting, or compensation) to the extent that they affected and were considered in the negotiation.
- If the offeror was not required to submit cost or pricing data to support any price negotiation over the cost or pricing data threshold, the exception used (e.g. acquisition of a commercial item) and the basis for using it.
- If the offeror was required to submit cost or pricing data, the extent to which the contracting officer:
  - Relied on the cost or pricing data submitted and used in negotiating price;
  - Recognized any cost or pricing data submitted as inaccurate, incomplete, or noncurrent:
  - The action taken by the contracting officer as a result of that recognition;
  - The action taken by the contractor as a result of that recognition; and
  - The effect of the defective data on the price negotiated; or
  - Determined that an exception applied after the data were submitted and, therefore, did not consider the submission to be cost or pricing data.
- A summary of the contractor's proposal, any field pricing assistance recommendations, including the reasons for any pertinent variances from them, the Government's negotiation objective, and the negotiated position.
  - When the determination of price reasonableness is based on cost analysis, the summary must address each major cost element.
When determination of price reasonableness is based on price analysis, the summary must include the source and type of data used to support the determination.

- The most significant facts or considerations controlling the establishment of the prenegotiation objectives and the negotiated agreement including an explanation of any significant differences between the two positions.
- To the extent such direction has a significant effect on the action, a discussion and quantification of the impact of direction given by Congress, other agencies, and higher-level officials (i.e., officials who would not normally exercise authority during the award and review process for the instant contract action).
- The basis for the profit/fee prenegotiation objective and the profit/fee negotiated.
- Documentation that the negotiated price is fair and reasonable.

**PNM Cost Element Summary.** When you use cost analysis, your cost element summary should address the offeror's estimating rationale, the Government's objective, and the amount considered negotiated. Commonly, this summary begins with a tabular presentation similar to the following:

<table>
<thead>
<tr>
<th>Cost Element</th>
<th>Proposed</th>
<th>Objective</th>
<th>Considered Negotiated</th>
<th>Reference</th>
</tr>
</thead>
<tbody>
<tr>
<td>Engineering Direct Labor</td>
<td>$1,000,000</td>
<td>$900,000</td>
<td>$925,000</td>
<td>See Para A</td>
</tr>
<tr>
<td>Engineering Overhead</td>
<td>$2,500,000</td>
<td>$2,025,000</td>
<td>$2,127,500</td>
<td>See Para B</td>
</tr>
<tr>
<td>Subtotal</td>
<td>$3,500,000</td>
<td>$2,925,000</td>
<td>$3,052,500</td>
<td></td>
</tr>
<tr>
<td>G&amp;A</td>
<td>$350,000</td>
<td>$292,500</td>
<td>$305,250</td>
<td>See Para C</td>
</tr>
<tr>
<td><strong>Total Cost</strong></td>
<td>$3,850,000</td>
<td>$3,217,500</td>
<td>$3,357,750</td>
<td></td>
</tr>
</tbody>
</table>

Using this type of tabular cost element summary, you can identify the areas and degree of differences and provide a general format more detailed analysis.

- In Paragraph A, summarize:
  - The rationale used by the offeror in developing the proposal.
Focus on any differences between the proposal and the recommendations.

The reasons for any differences between technical or audit recommendations and the Government objective.

The reasons for any differences between the Government objective and the amount considered negotiated. (Note: You and the contractor will likely not agree on each element of cost so the amount considered negotiated is your analysis of the cost used to arrive at a reasonable price.)

In Paragraphs B and C, address the same subjects covered in Paragraph A with one major addition. Since dollars are calculated using overhead and G&A rates, you need to address whether the dollar differences are the result of differences in the application base, the rates themselves, or both.

<table>
<thead>
<tr>
<th>PNM Cost Element Summary (cont)</th>
<th>Engineering Overhead Calculations</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>In the example above, the differences in engineering overhead dollars result from differences in both the base and the rate.</td>
</tr>
<tr>
<td>Engineering Overhead</td>
<td>Calculations</td>
</tr>
<tr>
<td>Proposed</td>
<td>$1,000,000 \times 250% = $2,500,000</td>
</tr>
<tr>
<td>Objective</td>
<td>$900,000 \times 225% = $2,025,000</td>
</tr>
<tr>
<td>Considered Negotiated</td>
<td>$925,000 \times 230% = $2,127,500</td>
</tr>
</tbody>
</table>

- The differences in G&A expense dollars relate only to differences in the base. The rate is the same for all three positions.

<table>
<thead>
<tr>
<th>G&amp;A Expense</th>
<th>Calculations</th>
</tr>
</thead>
<tbody>
<tr>
<td>Proposed</td>
<td>$3,500,000 \times 10% = $350,000</td>
</tr>
<tr>
<td>Objective</td>
<td>$2,925,000 \times 10% =</td>
</tr>
<tr>
<td>Item</td>
<td>Proposed</td>
</tr>
<tr>
<td>--------</td>
<td>----------</td>
</tr>
<tr>
<td>0001</td>
<td>$15,000</td>
</tr>
<tr>
<td>0002</td>
<td>$10,000</td>
</tr>
<tr>
<td>0003</td>
<td>$4,500</td>
</tr>
</tbody>
</table>

- If the same rationale applies to all items, a single explanatory paragraph should be enough.
- If different rationales apply to different items, you may need to provide several explanatory paragraphs.

**PNM Analysis of Facts or Considerations Affecting Price.** As you document the significant facts or considerations affecting the proposal, your objective, and the amount negotiated, consider the effect of the following:

- Items or services being purchased;
- Quantities being purchased;
- Place of contract performance;
- Delivery schedule or period of performance;
- Any difference(s) between the proposed delivery schedule, the objective schedule, and the negotiated schedule;
- Any previous buys of similar products including:
  - When,
  - How many,
  - Schedule/production rate,
  - Contract type, and
  - Unit prices or total prices, including both target and final prices, if applicable;
- Any Government-furnished material that will be provided as a result of the contract; and
- Any unique aspects of the contract action.
PNM Distribution (FAR 15.406-3(b)). Whenever you obtain field pricing assistance to support your negotiation, you must forward a copy of the PNM to the office(s) providing field pricing assistance. When appropriate, you should also forward recommendations on how field pricing assistance can be made more effective.

Technical and Audit Reports. Technical and audit reports provide key insights into the rationale that you used in developing your prenegotiation objectives. Normally, you should include a copy of each relevant report in the contract file. However, if the report is large or only available electronically, it may not be practical to include a copy in the contract file. In such situations, you must at least include information on where the full report can be found.

Record of Any Additional Information. The contract file should also include a record of any request(s) that you submitted to the contractor for additional information along with the contractor's response.