

## **APPENDIX J STRUCTURED APPROACH FOR PROFIT OR FEE OBJECTIVE**

### **INTRODUCTORY REMARKS.**

DHS Form 700-17, Weighted Guidelines Profit/Fee Objective, has been automated and contracting officers can access this automated version of the form to calculate profit/fee objectives. The DHS Form 700-17 is accessible from DHSCconnect at: [http://dhsconnect.dhs.gov/forms/Documents/DHS\\_Form\\_700-17.pdf](http://dhsconnect.dhs.gov/forms/Documents/DHS_Form_700-17.pdf).

When using the DHS Form 700-17, Weighted Guidelines Profit/Fee Objective, the contracting officer must categorize the acquisition as a manufacturing, research and development (R&D) or a services effort. To determine to which category a particular acquisition belongs, the contracting officer must rely on the nature of the work to be performed. When acquisitions involving R&D and services require a significant amount of facilities for efficient contract performance (as determined by the contracting officer), the manufacturing weighted guidelines method may be appropriate. Similarly, certain contracts for the manufacture of small quantities of high technology supplies and equipment may not require a significant amount of facilities. In these cases, an R&D classification may be appropriate.

In determining profit or fee, the tax posture of the business entity is certainly recognized. A fair and reasonable management fee to a non-profit organization with a tax-exempt status is considerably lower than a profit/fee to a commercial enterprise with a taxable status.

### **Non-Profit Organizations.**

The following applies to non-profit organizations:

1. As used in this subchapter, non-profit organizations are defined as those business entities organized and operated exclusively for charitable, scientific, or educational purposes; of which no part of the net earnings accrue to the benefit of any private shareholder or individual; of which no substantial part of the activities include carrying on propaganda, or otherwise, on behalf of any candidate for public office; and which are exempt from Federal income taxation under Section 501 of the Internal Revenue Code.
2. When the Weighted Guidelines Method for arriving at a profit/fee position is used for non-profit organizations, the contracting officer must make the following adjustments:
  - a. The weight ranges for "Cost risk" (Item 14 on the DHS Form 700-17) must be replaced with -1 to 0.
  - b. The Total Profit/Fee Objective (Item 20 on the DHS Form 700-17) must be reduced by up to 1% for manufacturing type efforts and up to 3% for R&D or Services type efforts.

## **Commercial Organizations.**

For the purposes of this subchapter, DHS utilizes the description from FAR 31.103 to describe commercial organizations.

### **I. CONTRACTOR EFFORT.**

This factor takes into account what resources are necessary and what the contractor must do to meet the contract performance requirements. Evaluation of this factor and the assignment of weights on the DHS Form 700-17 requires analyzing the cost content of the proposed contract in the following areas:

#### ***A. Material acquisition (e.g., subcontracted items, purchased parts, and other material).***

1. Consider the managerial and technical efforts necessary for the prime contractor to administer subcontracts and select subcontractors, including efforts to break out subcontracts from sole sources through the introduction of competition.
2. Consider whether the contractor's purchasing program makes a substantial contribution to the performance of a contract through the use of subcontracting programs involving many sources; new complex components, systems, or subsystems; and close surveillance by the prime contractor.

#### ***B. Direct labor (e.g., engineering, service, manufacturing, and other labor).***

1. Analysis of the various items of cost must include evaluation of the comparative quality and level of the engineering talents, manufacturing and service skills, and experience to be employed. In evaluating labor for the purpose of assigning profit weights, consideration must be given to the amount of notable scientific talent, unusual or scarce engineering talent needed, in contrast to journeyman engineering effort or supporting personnel. Higher weights are normally assigned to engineering, professional, or highly technical skill levels and lower weights to semiprofessional or other skill levels.
2. The variety of engineering, manufacturing and other types of labor skills required and the contractor's manpower resources for meeting these requirements must be considered.
3. For purposes of computing the prenegotiation profit/fee objective, exclude any amount from the pre-negotiation cost objective measurement base for the purchase cost of contractor-acquired property if i, ii, and iii below apply:
  - i. The property is categorized as equipment, as defined in FAR 45.101,
  - ii. The purchase cost the equipment is to be charged directly to the contract, and
  - iii. The equipment will be retained by the contractor as government property for use by the contractor in performing government contract(s).

### ***C. Overhead and general management (general and administrative (G&A))***

When analyzing overhead and G&A, consider the makeup of these expenses and how much they contribute to contract performance. If the contractor proposes a single indirect cost rate, the contracting officer must breakout the composite rate or contact the auditor to determine what is in the overhead and G&A expense pools. This information will assist in determining the appropriate weights for overhead and G&A on the DHS Form 700-17.

### ***D. Other costs.***

Include all other direct costs associated with contractor performance under this item. This includes airfare, lodging, computer support, etc. The assignment of a weight on the DHS Form 700-17 for this factor must be based on the nature of these costs and how much they contribute to contract performance.

## **II. CONTRACTOR RISK.**

The degree of cost risk assumed by the contractor should influence the amount of profit/fee anticipated. Consider the following when determining a weight for cost risk:

### ***A. Contract type.***

The degree of cost risk is related to the selection of contract type. For example, if a portion of the risk has been shifted to the Government through cost-reimbursement, or other risk reducing measures, the weight assigned to this factor should be less than acquisitions where the contractor assumes most or all of the risk. This is particularly evident when using time-and-material and labor-hour contracts priced on a time and material basis. These contract types must be considered to be cost-plus-fixed-fee contracts for the purpose of establishing a profit weight in the evaluation of the contractor's assumption of cost risk.

### ***B. Subcontracting program.***

The contractor's subcontracting program may have a significant impact on the contractor's acceptance of risk under a particular contract type. Analysis is necessary to determine if real cost risk has been transferred to a subcontractor. If this is the case, the contract cost risk weight assigned may be below the range that would normally be assigned.

### ***C. Definitization.***

For procurement actions that involve definitization of a letter contract, unpriced change orders, etc., where partial performance has occurred, evaluate the effect on total contract cost risk. If it is determined that the total amount of cost risk has been effectively reduced as a result of the partial performance, a lower weight may be appropriate. In addition, evaluate the type of work performed (e.g., complexity) and the type of work remaining to ensure an equitable weight assignment.

### **III. FACILITIES INVESTMENT.**

DHS Form 700-18, Contract Facilities Capital and Cost of Money or a form substantially similar if authorized according to Component procedures, is used to determine the capital employed and cost of money amounts to be entered on the DHS Form 700-17, Weighted Guidelines.

#### ***A. Utilization.***

To evaluate how facilities contribute to the profit objective requires knowledge of the level of facilities utilization needed for contract performance, the source and financing of the required facilities, and the overall cost effectiveness of the facilities offered. Contractors furnishing their own facilities that significantly contribute (as determined by the contracting officer) to lower total contract costs generally receive additional profit/fee. Conversely, contractors that rely on the Government to provide or finance needed facilities normally receive a correspondingly lower profit/fee. The following factors should also be considered:

1. The productivity improvements resulting from the facilities capital investment including the economic value of the facilities capital (e.g., physical age, undepreciated value, idleness, and expected contribution to future Government needs).
2. The degree to which the capital investment has direct, identifiable, and exceptional benefits to the Government, such as: new investments in state-of-the-art technology which reduce acquisition cost or yield other tangible benefits such as improved product quality or accelerated deliveries, or investment in new equipment for R&D applications.

#### ***B. New Investment.***

To assist in evaluating *new* investment, the contracting officer should request the contractor to submit reasonable evidence that the new facilities investment will result in benefits to the Government.

### **IV. SPECIAL FACTORS.**

#### ***A. Productivity.***

The purpose of this factor is to recognize a prospective contractor's investment in modern cost-reducing facilities and other improvements in efficiency. This factor is applied when the acquisition is a follow-on manufacturing effort, actual cost data are available to establish a baseline, and changes in item configuration are not large enough to invalidate price comparability. The dollar amount inserted under the measurement base on the DHS Form 700-17 is based on the estimated cost reduction that can be attributed to productivity gains.

#### ***B. Independent development.***

The purpose of this factor is to recognize independent research and development on the part of the prospective contractor pertaining to the end item being procured. To determine the

appropriate weight to assign this factor on the DHS Form 700-17, it is important to evaluate whether the development cost was recovered directly or indirectly from Government sources. This factor is applied when the item is important to the advancement of the DHS mission and the prospective contractor demonstrates initiative in determining the need and application of the developed item.

***C. Other.***

1. *Socioeconomic programs.* This factor covers a number of special circumstances or particular acquisitions. It relates to the prospective contractor's participation in Federal socioeconomic programs. In addition to providing a reward for an unusual initiative in supporting Government socioeconomic programs, failure or unwillingness on the part of the prospective contractor to support these programs should be viewed as evidence of poor performance for the purpose of establishing this profit/fee objective factor.

2. *Performance.* The purpose of this factor is to evaluate the prospective contractor's past and present performance in such areas as: product quality, meeting specifications and contract schedules (including the administrative aspects of performance), efficiency in cost control (including the need for and reasonableness of costs incurred) especially under cost reimbursement contracts, accuracy and reliability of previous cost estimates, timely processing of changes, standards of good workmanship, history for reasonable and cooperative behavior and commitment to customer satisfaction, and the prospective contractor's business-like concern for the interest of the customer.