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DEPARTMENT OF THE AIR FORCE  
HEADQUARTERS AIR FORCE MATERIEL COMMAND  
WRIGHT-PATTERSON AIR FORCE BASE, OHIO

30 MAR 1995

MEMORANDUM FOR SEE DISTRIBUTION

FROM: HQ AFMC/PKF  
4375 Chidlaw Road, Suite 6  
Wright-Patterson AFB OH 45433-5006

SUBJECT: Revised Practices in DD1547 Profit Reporting - ACTION MEMORANDUM

1. The Office of the Under Secretary of Defense, Acquisition and Technology (USDA&T, DP/CPF) is concerned about profit statistics being reported by the Air Force under Use Code 4 (DD1547, block 12). This code is intended to identify use of an alternate structured approach (ASA) in lieu of the standard or modified weighted guidelines methods. For reports submitted in FY93, the Air Force reported 38% of its dollars through use code 4 compared to 12% for the Army and 1% for the Navy. We attribute the significance of our figures to prior direction that certain actions in addition to ASAs be reported with use code 4. Specific situations include negotiations with multiple contract types, time and materials arrangements, contracts with reimbursable or other non-fee-bearing costs, and contracts where the basic contract profit rate is used to negotiate a modification.

2. We offered several suggestions to DP/CPF that could resolve their concerns, and they have concurred with some changes in reporting profit. Effective immediately, modify your reporting practices to comply with the following guidance.

a. Report only ASAs through use code 4. Remember that the Chief of the Contracting Office or the Senior Laboratory Contracting Official must approve use of an ASA, and be sure to provide a copy of the approved ASA to our office (AFMCFARS 5315.903(b)).

b. Where multiple contract types are involved in a single contract action (e.g., FFP, FPI, and CPFF line items on one contract), prepare a separate DD1547 for each contract type to determine suitable profit objectives for the different line items. Do not consolidate the negotiation summary statistics from those individual forms into a single DD1547 for reporting purposes. Instead, select the prepared DD1547 reflecting the largest negotiated total price and report only that form.

c. Use the weighted guidelines method to compute profit objectives for time and materials (T&M), labor-hour, and firm fixed-price-level-of-effort-term contracts. The reporting requirement is now linked to the existence of an initial award or order exceeding \$500,000. Continue to assign type contract U (DD1547, block 10) consistent with the profit policy requirement to use CPFF contract type risk factors; however, do not assign use code 4. Use codes 1 and 2 are likely selections depending on whether alternate or standard performance risks are assigned.

95-6D (FAR 15) Post to DFARS 215.970 and AFMCFARS 215.970 by circling the references and noting in the margins: "70-41, atch 95-6D". Then file this atch behind the sups to FAR 15.

(1) If you obtain a proposal for a specific effort to be awarded on a T&M basis, prepare a DD1547 reflecting your objective elements of cost on that proposed effort. If the negotiated value shown on the DD1547 exceeds \$500,000, submit that form for reporting.

(2) If you contemplate a contractual instrument authorizing placement of orders on a T&M basis, and you will negotiate T&M rates for inclusion in that instrument to be applicable to orders, the requirement to accomplish profit reporting depends on the initial order. The maximum estimated value that might be anticipated under the instrument is not relevant.

(a) If a firm initial order is known when the instrument will be negotiated, and you have obtained a proposal for that order, compute a profit objective for rates in the instrument using the objective position on that order. Report the DD1547 only if the negotiated value reflected on the form exceeds \$500,000.

(b) If a firm initial order is not known at the time the instrument will be negotiated, profit reporting is not required. To develop a profit objective for the T&M rates, we suggest selecting any representative or average rate and subjecting a hypothetical scenario to the weighted guidelines method (e.g., allocate cost elements against the estimated maximum value, or simply multiply the selected rate by 1000). The instrument is not considered an "action" for reporting purposes since an amount exceeding \$500,000 is not really being "awarded."

(c) With the exception of (a) above, do not report individual orders against such T&M instruments unless a new profit analysis is performed in negotiating the price of the order (and that order exceeds \$500,000).

(3) When deciding whether the \$500,000 reporting threshold is met, remember that the "materials" portion of T&M contracts is typically cost reimbursable and receives no profit or fee. The DD1547 would address the "time" portion (loaded labor rates) of the effort, and those figures determine whether the form is reported. For example, a \$600,000 T&M effort consisting of \$450,000 "time" and \$150,000 "materials" is not reportable.

d. When the total contract price involves non-fee-bearing costs (e.g., reimbursable material or travel costs, royalties, warranty costs, or state income taxes), do not include such amounts in the DD1547 calculations. The form used to compute the profit objective, absent the non-fee-bearing costs, will be submitted for reporting. It is acceptable for the DD1547 figures to differ from the dollar values cited on the face page of the contract or used for contract approval purposes.

e. When negotiating a change order that will result in a net increase exceeding \$500,000, report the action provided that a new profit analysis has been performed. (Refer to paragraph f below for situations where the basic contract rate is used.) Perform a DD1547 profit analysis on the new work being added to the contract. If work is also being deleted, you may calculate it using either the originally negotiated profit rate, the profit rate computed for new work, or a profit rate computed separately on deleted work, whichever is deemed appropriate under the circumstances. However, report only the DD1547 covering new work. Reported figures shall not represent net decreases, deleted work, net increases (added work minus deleted work), or aggregate increases (added work plus the absolute value of deleted work).

f. FAR 15.903(f) permits use of the basic contract rate for pricing changes or modifications when they involve essentially the same type and mix of work as the basic contract and are of relatively small comparative dollar value. When this exception to performing a profit analysis is used, do not prepare a DD1547 and do not report profit. Note that the exception presumes that an analysis was originally performed for the basic contract. If the basic contract was competitively awarded, the exception cannot be used and a profit analysis must be performed for the change or modification.

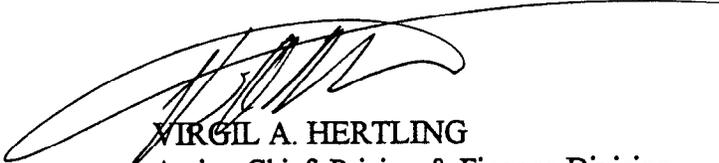
3. In addition to the revised guidance set forth above, you are reminded of the following:

a. Report indefinite-delivery contracts (FAR 16.5) if the expected value for the contract period (basic and option periods are segregated) exceeds \$500,000. Prepare the DD1547 based on the expected value (definite quantity, best estimated quantity, or maximum quantity as deemed appropriate). Do not report individual orders placed against these contracts unless you have performed a new profit analysis.

b. When negotiating contracts containing options, generally prepare a separate DD1547 covering each option. Report options exceeding \$500,000 at the time they are exercised (reference DFARS 253.215-70(b)(5) and AFMCFARS 5315.970(b)(90)(3)). However, if the basic contract profit rate was used to price an option (e.g., option line items in a larger basic effort), do not report that option.

4. Disseminate this guidance to all buying and pricing personnel within your organization to be followed for all FY95 profit reporting. Briefing charts and discussion notes are attached to facilitate training efforts. The briefing was prepared in Microsoft PowerPoint Ver. 3.0 and will be furnished via e-mail upon request. This is interim guidance pending revision of the AFMCFARS to include the reporting requirements. We solicit your comments for consideration in drafting the AFMCFARS language. If you have any questions, please call us or have your staff call our action officer, Mr. Tony Baumann, HQ AFMC/PKF, DSN 787-6861.

FOR THE COMMANDER



VIRGIL A. HERTLING  
Acting Chief, Pricing & Finance Division  
Directorate of Contracting

Attachment:  
Briefing -- Profit: Computing and  
Reporting in Selected Situations

cc:  
SAF/AQCP



**PROFIT:  
COMPUTING AND REPORTING  
IN SELECTED SITUATIONS**

**TONY BAUMANN  
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DSN 787-6861  
March 1995**

This briefing was prepared by Tony Baumann, HQ AFMC/PKF, for use in disseminating revised profit reporting requirements. It reviews several scenarios encountered by negotiators, addressing how the profit analysis should be conducted and whether the action is reportable.

Questions or comments should be directed to Mr. Baumann at:

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## BRIEFING PURPOSE

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- **BACKGROUND**
  - OSD concern about USAF statistics on DD1547 Use Code 4
  - Use Code 4 intended for Alternate Structured Approach (ASA)
  - USAF has been assigning code to other actions besides ASAs
- **REPORTING CHANGES COORDINATED WITH OSD**
  - Interim guidance reflected in briefing
  - AFMCFARS change to follow
- **BOTTOM LINE: ONLY CITE USE CODE 4 FOR ASAs!!**

3/30/95 2:45 PM

2

OSD is concerned that FY93 profit statistics recorded from DD Form 1547 submittals showed the Air Force citing Use Code 4 on 38% of reported dollars compared to 12% for the Army and 1% for the Navy. Use Code 4 was designed for use with the Alternate Structured Approach. Accordingly, the statistics make it appear that the AF is using the weighted guidelines method only 62% of the time.

AFMC attributes the high use of code 4 to previous direction to use the code for reporting negotiation summary data in several other situations, including: consolidating multiple DD 1547s when combining contract types into a single contract; T&M actions; net amounts from change orders; modifications where the basic contract rate was used.

In coordination with OSD, AFMC is revising its reporting practices. This briefing reviews interim guidance pending revision of the AFMCFARS. In the future, only cite Use Code 4 for ASAs.



## MULTIPLE CONTRACT TYPES

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- PREPARE SEPARATE DD1547s FOR INDIVIDUAL CONTRACT TYPES (I.E., ALL FPI ON ONE 1547, ALL CPFF ON ANOTHER 1547, ETC)
- APPLY RESULTANT PROFIT OBJECTIVES TO RESPECTIVE PORTIONS
- REPORT ONLY THAT DD1547 WHICH REFLECTS THE LARGEST DOLLAR AMOUNT
  - do not consolidate all DD1547s into a single DD1547 for reporting purposes
  - one DD1547 is submitted per action; other smaller dollar forms are retained with PNM and contract file
  - if largest contract type does not exceed \$500K, do not report

3/30/95 2:28 PM

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When a contract action involves more than one contract type (e.g., combination of FPI and CPFF portions), prepare a separate DD 1547 for the costs involved with each contract type. This will produce different profit objectives to be applied to respective portions of the actions.

For profit reporting purposes, only the individual DD 1547 reflecting the largest negotiated dollar value will be reported, assuming it exceeds \$500K. For example, if an action is negotiated with a \$1.3M FPI portion and an \$900K CPFF portion, report only the FPI portion. However, if an \$850K action is negotiated and consists of \$450K FPI and \$400K CPFF, no reporting will be accomplished on the action.



## T&M CONTRACTS

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- **WHERE A FIRM T&M EFFORT IS BEING PLACED ON CONTRACT**
  - use contractor's proposal to develop objective position
  - use DD1547 to develop profit objective for the effort
  - REMEMBER: treat as CPFF for assigning contract type risk
- **REPORT DD1547 IF NEGOTIATED VALUE ON FORM EXCEEDS \$500K**
- **REMEMBER: MATERIAL IS COST REIMBURSABLE**
  - exclude it from the DD1547 so it doesn't factor into the profit calculation
  - do not consider it when determining the \$500K threshold

3/30/95 2:26 PM

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If a specific requirement is being placed on contract on a T&M basis, a proposal will be obtained covering that effort. Develop an objective position on that effort and insert the figures into a DD 1547 computation. Remember that the profit policy specifies use of CPFF values for contract type risk. Contract type U will be assigned in block 10 of the DD 1547.

If the negotiated value reflected on the form exceeds \$500K, it must be reported.

Remember that material costs are reimbursable through T&M contracts; therefore, do not include them on the DD 1547. The negotiated value shown on the DD 1547 will also exclude material costs. This is the value that determines reportability, not the total value on the contract.

Atch 95-6D (FAR 15)



## T&M ORDERING CONTRACTS (FIRM INITIAL ORDER KNOWN)

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- **NEGOTIATING INDIVIDUAL LOADED LABOR RATES**
- **USE DD1547 TO COMPUTE PROFIT OBJECTIVE**
  - prepare DD1547 based on value of firm initial order
  - report if DD1547 negotiated total price > \$500K
  - **REMEMBER:** exclude material costs from DD1547 and when determining reporting threshold
- **DO NOT REPORT INDIVIDUAL ORDERS UNLESS NEW PROFIT ANALYSIS IS PERFORMED**

3/30/95 2:26 PM

5

When awarding instruments against which T&M orders may be subsequently placed, the PCO negotiates individual loaded labor rates for inclusion in the basic instrument. This negotiation is typically conducted using cost analysis, so a profit analysis would also be required. The WGM is normally be used to establish a profit objective, but the format depends on whether a firm initial order is known at the time the instrument is being negotiated.

When a firm order is known, a proposal should be obtained for the value of that order. Using that proposal as a basis, prepare an objective position on costs and subject it to the DD 1547 profit analysis. Remember that the CPFF range for contract type risk is used with T&M actions. The resultant profit objective translates into a percentage which can be applied to each labor category for use in negotiating rates. However, the value of that order as shown on the DD 1547 determines whether the action is reportable. Ensure that reimbursable material costs have been excluded (from the proposed and negotiated summary figures, too, for comparability).

Subsequent individual orders are not reportable unless a separate profit analysis is performed and the order (excluding materials) exceeds \$500K.



## T&M ORDERING CONTRACTS (FIRM INITIAL ORDER NOT KNOWN)

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- **NEGOTIATING INDIVIDUAL LOADED LABOR RATES**
- **USE DD1547 TO COMPUTE PROFIT OBJECTIVE**
  - select representative/average rate and identify cost elements
  - multiply individual elements by a constant factor, e.g. 1000 (to offset DD1547 rounding functions)
  - insert figures into DD1547, assign values and weights (remember to use CPFF range for contract type risk)
- **DO NOT REPORT!**
- **DO NOT REPORT INDIVIDUAL ORDERS UNLESS NEW PROFIT ANALYSIS IS PERFORMED**

3/30/95 2:56 PM

6

When a firm initial order is not known, the WGM should still be used, but certain alterations will be employed to produce usable information. The goal is to obtain an objective profit percentage to apply across all rates. Since the relationship between cost elements should be relatively constant across all rates (note that only the figures for subtotal costs, G&A, total costs, and COM, DD 1547 blocks 18-20 and 32, are important in applying profit weights and factors), select any average or representative rate for application of the WGM. Because individual rates are small figures (tens of dollars instead of millions of dollars), multiply the cost elements of the selected rate by a factor of 1000 to avoid significant impacts of rounding functions within the DD 1547. Insert the increased figures into the DD 1547 and perform a typical WGM computation. Remember that the CPFF range for contract type risk is used with T&M actions. The resultant profit objective translates into a percentage which can be applied to each labor category for use in negotiating rates.

Reporting is not required since an initial known order exceeding \$500K does not exist. Subsequent orders are not reportable either unless a new profit analysis has been performed, and then only if the order exceeds \$500K as shown on the new DD 1547.



## NON-PROFIT-BEARING COSTS

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- **EXAMPLES INCLUDE CERTAIN STATE INCOME TAXES AND REIMBURSABLE COSTS SUCH AS TRAVEL AND MATERIAL REIMBURSEMENTS**
- **PREPARE DD1547 TO DEVELOP PROFIT OBJECTIVE**
  - exclude non-profit-bearing costs from elemental costs
  - assign weights and values giving consideration only to types of efforts and costs subject to profit
  - apply resultant objective rate to portion receiving profit
- **SUBMIT PREPARED DD1547 FOR PROFIT REPORTING**
  - non-profit-bearing costs will not be reported

3/30/95 2:28 PM

7

Occasionally, an acquisition involves costs which will be reimbursed under the contract "at cost" (no profit allowed), or are otherwise included in the contract price without allowing profit. Examples would be certain state income taxes, travel costs, or reimbursable materials. When preparing the DD 1547 to apply the WGM, exclude such costs from the cost element totals placed on the form. Be sure not to apply the computed objective profit rate to those costs when you compile your objective total price, either!

For reporting purposes, submit the DD 1547 which you prepared. The non-profit-bearing costs will not be reflected in your objective position, so be sure you remove them from the proposed and negotiated figures reflected in the DD 1547 negotiation summary section. This way you will be presenting an apples-to-apples comparison.



## CHANGE ORDERS

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- NO GUIDANCE IS SPECIFIC TO CHANGE ORDERS
- RECOMMENDED APPROACHES:
  - apply basic contract rate if conditions are met (refer to DFARS exceptions to using weighted guidelines)
  - use DD1547 to compute separate profit objectives for added and deleted work
- FOR REPORTING PURPOSES
  - report only if change results in net increase exceeding \$500K
  - only report added work

3/30/05 2:26 PM

Regulatory guidance does not specify how profit should be determined in change order situations. The easiest approach would be to apply the negotiated contract rate, assuming the action fits the criteria for WGM exception set forth in DFARS. If the contract rate is not available, or its use is otherwise inappropriate, the situation may be more complex.

When the change involves only "added" work or only "deleted" work, insert the costs into the DD 1547 and perform a standard WGM computation. If both "added" and "deleted" work are involved, a separate profit objective must be computed for "added" work. For "deleted" work you may elect to use the profit rate computed for the "added" work, use the basic contract rate, or complete a separate DD 1547 analysis.

The action is reportable only if it results in a net increase in the contract price exceeding \$500K. In that case report the DD 1547 prepared for the "added" work. Examples: (1) \$1M adds, \$300K deletes, \$700K net increase -- report \$1M adds; (2) \$1M adds, \$800K deletes, \$200K net increase -- no reporting.



## MODIFICATIONS USING BASIC CONTRACT RATE

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- **CAN USE BASIC CONTRACT RATE FOR CHANGES AND MODIFICATIONS IF:**
  - essentially same type and mix of work
  - relatively small dollars vs. total contract value
  - relevant variables have not materially changed (e.g., performance risk, interest rates, progress payment rates, facilities distribution)
- **DO NOT PREPARE DD 1547 FOR REPORTING BECAUSE YOU DID NOT DO A NEW PROFIT ANALYSIS**
- **NOTE: IF PROFIT ANALYSIS WAS NOT PERFORMED ON BASIC CONTRACT (E.G., COMPETITIVE AWARD), YOU MUST PERFORM ANALYSIS ON CHANGES**

3/30/95 3:54 PM

9

FAR 15.903(f), as supplemented, authorizes an exception to the weighted guidelines method of profit analysis for certain changes and modifications to contracts. These actions must involve essentially the same type and mix of work as the basic contract, and they must be of relatively small dollar value in comparison to the basic effort. The exception assumes that a profit analysis was performed when the basic contract was awarded. The contracting officer must ascertain that relevant variables (as shown on the chart) have not materially changed since that initial profit analysis was performed.

Profit reporting is required only when WGM, ASA, or modified WGM is used. When the basic contract rate is applied to a modification, none of these methods has been used for the instant action; therefore, reporting is not required. DO NOT prepare a DD 1547.

The exception may not be used when modifying contracts such as competitively awarded contracts, where a profit analysis was not performed for the original award.



## INDEFINITE-DELIVERY CONTRACTS

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- **PREPARE TYPICAL DD1547**
  - for definite-quantity contracts, cost element figures are based on total definite quantities for contract period
  - for requirements contracts, cost element figures are based on best estimated quantities (BEQs)
  - for indefinite-quantity contracts, cost element figures are based on estimated or maximum contract quantities
- **REPORT DD1547 IF NEGOTIATED VALUE EXCEEDS \$500K**
- **REMEMBER TO TREAT OPTIONS SEPARATELY**

3/30/95 3:45 PM 10

Indefinite-delivery contracts may present an anomaly because the variability of quantity presents the question of what quantity should be represented in the cost analysis and, subsequently, the profit analysis. DFARS 253.215-70(b)(5) suggests the annual requirements should be consolidated. Definite-quantity contracts don't present a problem -- use the definite quantities. With requirements contracts, cost element figures should be based on the Government's best estimated quantities (BEQs). With indefinite-quantity contracts, the figures should be based on BEQs if they exist; otherwise, use the maximum quantities which could be ordered.

Report the prepared DD 1547 if the negotiated value shown exceeds \$500K. This threshold is separately applied to the basic and each option period.



## OPTION REQUIREMENTS

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- **SEGREGATE REQUIREMENTS BETWEEN BASIC CONTRACT PERIOD AND EACH OPTION**
- **PREPARE SEPARATE DD1547s FOR EACH CONTRACT PERIOD (ONE FOR BASIC, ONE FOR OPTION 1, ETC)**
- **FOR REPORTING PURPOSES**
  - submit DD1547 covering basic contract when contract is awarded
  - submit DD1547 covering particular option when option is exercised
  - **REMEMBER:** if total price for any contract period is under \$500,000, do not report that DD1547!

3/30/05 3:45 PM 11

When negotiating a contract containing options, a separate WGM computation should be performed for each contract period/option.

Profit is reported only when an action is awarded. Report only the DD 1547 covering the basic period requirement when the initial contract is issued. When an option is exercised, then report the DD 1547 covering that option. (Remember that the report number and the action date must reflect the fiscal year in which the reporting is accomplished, regardless of when the negotiation occurred.) Of course, if an option is exercised at the same time the basic contract is awarded, you will be submitting two DD 1547s at that time, although two different report numbers will be used.

Also remember that the reporting threshold is \$500K. This applies to individual report submissions, not the total contract amount. If any contract period is less than \$500K as reflected on the DD 1547, do not report that DD 1547.



## QUICK REFERENCE

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<u>SCENARIO</u>	<u>REPORT?</u> (assume > \$500K)
multiple contract types	yes, largest type (type >\$500K)
time and materials	
specific effort	yes
ordering contract, 1st task known	yes, 1st task only
ordering contract, 1st task unknown	no
non-fee-bearing costs	no
change order	yes, adds only (if <u>net</u> > \$500K)
basic contract rate	no
indefinite-delivery	yes
options	yes, at time of exercise

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3/30/95 3:45 PM 12

Here is a quick summary of the situations as a handy reference.

multiple contract types -- separate DD 1547s for each type, report only the largest form if that form > \$500K

T&M -- negotiating specific task > \$500K, report; negotiating ordering contract, only report if initial order is known and > \$500K (report based on value of that order)

change orders -- report DD 1547 on added work (not deleted work) only if there is a net increase > \$500K

indefinite-delivery -- report based on definite quantity, BEQ, or maximum quantity expected to be ordered in the period if > \$500K

options -- report separately when exercised if > \$500K

DO NOT REPORT non-fee-bearing costs or mods using the basic contract rate

**REMEMBER: don't cite Use Code 4 unless ASA is used!**