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## Commercial Purchasing: The Chasm between the United States Government's Evolving Policy and Practice

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**COMMERCIAL PURCHASING:  
THE CHASM BETWEEN THE UNITED STATES GOVERNMENT'S  
EVOLVING POLICY AND PRACTICE**

Steven L. Schooner<sup>1</sup>

**1. Introduction**

During the 1990's, the United States (U.S.) government accelerated its efforts to adopt more commercial practices and buy more commercial items. This entailed two related behavioral changes. First, the U.S. government touted its willingness to mimic the most successful buying practices of businesses and consumers. Second, the U.S. government committed to relying more heavily upon existing goods and services already produced in the marketplace, rather than demanding that firms create government-unique versions of similar goods and services.<sup>2</sup>

Thus, the commercial buying trend introduced two seemingly ephemeral concepts into the mainstream vocabulary of U.S. procurement personnel: acquisition of commercial items (a focus on *purchasing different things*) and

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<sup>2</sup> Three decades of study have confirmed the inefficiencies associated with governmental purchasing of custom-designed goods and services. Steven Kelman, *Buying Commercial: An Introduction and Framework* 27 PUB. CONT. L.J. 249 n.1 (1998).

commercial purchasing practices (a focus on *different purchasing methodologies*). For the purposes of the U.S. procurement system, the term “commercial item” today refers to “any item . . . that is of a type customarily used for nongovernmental purposes and that [h]as been sold, leased, or licensed to the general public[.]”<sup>3</sup> As discussed below, the intent of this regulatory definition is to distinguish commercial items from those unique goods (such as sophisticated weapons systems) procured by the government, typically manufactured to idiosyncratic specifications, for which no legitimate nongovernmental market exists. For example, the now-popular term “commercial-off-the-shelf” (or COTS) refers to those goods readily available to the public in the retail marketplace, frequently through catalogue orders or cash-and-carry transactions.

Turning from *what* the government is buying to *how* the government buys, the government’s adoption of the term “commercial purchasing practices” reflects the government’s attempt both to: (1) act more like a consumer or a for-profit business; and (2) avoid buying according to the long-established statutes, regulations, policies, and practices that encompass the federal government procurement regime.

Change of this magnitude is difficult, and it frequently leads to missteps and meets resistance from policymakers, procurement personnel, and entrenched government suppliers. Nonetheless, the trend continues.

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<sup>3</sup> 48 C.F.R. § 2.101.

This paper introduces the U.S. efforts to make its government purchasing regime more commercial. These efforts entail the introduction of new policies, vocabulary, purchasing authorities, and practices. The paper then unveils a host of impediments that restrain the U.S. government from evolving into a truly commercial purchasing regime. These impediments derive from the nature of government, the specific needs of the government, and public's expectations regarding the expenditure of public funds. Ultimately, the paper suggests that the U.S. government is well served in its efforts to become *more* commercial, but divining a happy medium – or determining just how commercial to become – is a daunting task.

## **2. The United States: Adopting Commercial Behavior**

As suggested above, there are various aspects of the government's effort to embrace commercial behavior, ranging from the conceptual to the concrete, including principles, practices and platitudes. For the sake of this brief discussion, the author suggests that the following elements of the commercial purchasing movement merit discussion. First, as a matter of policy, the government articulated – and regulated – a preference for the procurement of commercial items. Second, the government enhanced its efforts to identify, attract, and select commercial contractors.<sup>4</sup> Third, the government today utilizes many putative

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<sup>4</sup> Many observers point to the recent, meteoric rise of Dell Computer – a commercial vendor of personal computers and peripherals – through the ranks of the Top 200 Government Contractors as an anecdotal success story.

commercial-type contractual vehicles. As discussed below, this topic is a mixed bag. The government unequivocally has benefited from the adoption of certain commercial purchasing vehicles (such as the garden variety credit card), but it has also spawned a number of bastardized, troublesome vehicles in the name of commercial practice. Fourth, the government reduced barriers to entry for commercial firms, specifically by (a) avoiding government-unique standards, specifications, provisions, and clauses and (b) reducing certain intrusive government-unique pricing, audit, and certification requirements. Fifth, the government increased its emphasis on privatization and outsourcing of commercial functions. While the author concedes that this organizational scheme is somewhat artificial, it should provide a sufficient entrée into the government-commercial realm.

### **2.1. Clarifying the Preference for Commercial Items**

The preference for commercial items and commercial practices, codified by the Federal Acquisition Streamlining Act of 1994 (FASA),<sup>5</sup> has led to the U.S. government's use of a number of different contractual vehicles. But before turning to these new practices, it seems appropriate to briefly discuss the underlying

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<sup>5</sup> Pub. L. No. 103-355, 108 Stat. 3243 (1994) (codified in scattered sections of 41 U.S.C. and 10 U.S.C.). This preference is bolstered by the regulatory order of precedence language in 48 C.F.R. § 12.102: "When a policy in another part of this chapter is inconsistent with a policy in this part, this Part 12 shall take precedence for the acquisition of commercial items."

policies and examine some of the new vocabulary utilized in the government-commercial purchasing regime.

### **2.1.1. Articulating the Policy of the Commercial Preference**

As discussed above, the rallying cry of the commercial movement was that the U.S. government should study, learn from, and ultimately imitate the most successful buying practices of businesses and consumers.<sup>6</sup>

Our models, teachers, and partners in this historic undertaking are America's best-run companies – companies that led the quality revolution of the past two decades . . . which have kept America competitive in the world market. They have already been through the transformation from industrial-age to information-age management. They have been through the learning curve, they have made the mistakes and fixed them, all while dealing with the risks of a free market. . . .

Most of what successful businesses, and now government, have learned can be summed up in two principles: focus on customers, and listen to workers. Old-fashioned bureaucracies focus on hierarchy and listen to instructions from the top. Doing otherwise is a big change.<sup>7</sup>

While this rhetoric may resemble cheerleading, these types of proclamations, delivered by high-ranking government officials, sent strong messages to

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<sup>6</sup> Proponents asserted that combining successful commercial practices with the elimination of government unique barriers would make the procurement system more efficient. *See generally* Kelman, *supra* note 2, at 250.

<sup>7</sup> *See* AL GORE, BUSINESSLIKE GOVERNMENT: LESSONS LEARNED FROM AMERICA'S BEST COMPANIES 3 (October 1997) (featuring the popular DILBERT comic strips by Scott Adams). Readers unfamiliar with DILBERT will enjoy visiting <<http://www.unitedmedia.com/comics/dilbert/>>.

procurement personnel: changed behavior was required in the post-acquisition reform environment.

At the same time, the government has committed itself to relying more heavily upon the existing goods and services produced in the marketplace. Specifically, this means that the government is attempting to break its longstanding habit of demanding that firms create government-unique versions of goods and services available in the commercial marketplace. For example, in 1996, the government touted its purchase of T-shirts as a breakthrough because the government bought Jockey's standard product, rather than mandating that manufacturers produce a shirt to unique government specification and provide sensitive pricing data so that the government could determine a fair price.<sup>8</sup>

As discussed below, however, a critical observation of the post- acquisition reform regime discloses a noticeable rift between policy and practice. Where the government practice aligns well with the underlying policies, the government, private firms, and the public appear to benefit. Where the government stretches the lessons learned from the commercial marketplace, or contorts the commercial experience to achieve specific objectives, the results have proven less appealing.

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<sup>8</sup> VICE PRESIDENT AL GORE, THE BEST KEPT SECRETS IN GOVERNMENT 14 (September 1996).

### 2.1.2. Introducing a New Vocabulary

Developing meaningful definitions for the language of this new commercial regime has proven challenging.<sup>9</sup> This is not surprising given the inherent confusion associated with two similar sounding, arguably related, but conceptually distinct efforts – the purchase of more commercial items and the effort to engage in more commercial behavior.

The Federal Acquisition Regulation (FAR) expanded the regulatory definition of commercial items aiming to include anything available in the marketplace that was not developed exclusively for the Federal government.<sup>10</sup> The primary definitional message became: if the item is customarily used for a nongovernmental purpose and the public consumes the item, whether through

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<sup>9</sup> The Uniform Commercial Code (UCC), which has been adopted, with minor modifications, by the legislatures in all fifty of the United States, and is addressed at length below, provides some useful analogies. The drafting committee responsible for revising Article 2, which deals with sales of goods, confronted the problem that definitions often need to be somewhat amorphous in order to be sufficiently broad to cover the relevant field. The UCC's merchant definition has been criticized as a "wonderland of exotic words which may be a delight to the lovers of intricate semantics, but which will rise to plague any lawyer, businessman or judge who attempts to apply such a statute to regulation of everyday transactions." Frederick K. Beutel, *The Proposed Uniform Commercial Code as a Problem in Codification*, 16 LAW & CONTEMP. PROBS 141, 148 (1951). Further, the current code, in defining its scope, refers simply to "transactions in goods," but did not address whether computer information falls within that definition. This ambiguity led courts to apply article 2 to computer information transactions "either directly or by analogy, in ways that lead to inappropriate results." Ann Lousin, *Symposium on Revised Article 1 and Proposed Revised Article 2 of the Uniform Commercial Code: Proposed UCC 2-103 of the 2000 Version of the Revision of Article 2*, 54 SMUL. REV. 913 (SPRING 2001).

<sup>10</sup> 48 C.F.R. § 2.101.

purchase, lease, or license, the item is commercial.<sup>11</sup> In the effort to maximize the government's flexibility, however, the scope of the commercial item definition became staggeringly broad. The definition includes items that have been "offered" but not yet actually sold to the public; any item that *evolves from* a commercial item; nondevelopmental items that were developed exclusively at private expense and sold to multiple sub-Federal governments; and any commercial item that has experienced certain "minor modifications." The regulations describe these types of modifications as follows:

*Minor modifications of a type not customarily available in the commercial marketplace made to meet Federal Government requirements.* Minor modifications means modifications that do not significantly alter the nongovernmental function or essential physical characteristics of an item or component, or change the purpose of a process. Factors to be considered in determining whether a modification is minor include the value and size of the modification and the comparative value and size of the final product. Dollar values and percentages may be used as guideposts, but are not conclusive evidence that a modification is minor. . . .<sup>12</sup>

Professor Steven Kelman, formerly Administrator for Federal Procurement Policy, applauds this "move away from *government-unique* specifications and standards towards broad needs descriptions that enable vendors to offer a wide variety of commercial solutions[.]" He argues that government unique-specifications unintentionally disqualify many competent potential offerors and, in

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<sup>11</sup> See generally 48 C.F.R. § 2.101.

<sup>12</sup> 48 C.F.R. § 2.101 (emphasis added).

so doing, substantially limit the “government’s ability to secure the best match between government needs and marketplace capabilities.” Kelman suggests that the revised regulations permit agencies to describe their needs in broad terms, which allows private firms to “rely on existing product literature and propose more than one product,” resulting in lower offered prices.<sup>13</sup>

Less enthusiastic observers fret over the broad scope of the definitions and complain that these terms frequently seem amorphous. Critics suggest that the current definition of commercial item is so broad, that almost all government contracts could be considered commercial. The “internal . . . joke [posits] that the only items not considered commercial items under the new definition are the Seawolf submarine and the B-2 Stealth bomber. . . .”<sup>14</sup> These criticisms are fuelled by the recognition that, included under the umbrella of commercial items is the “other transactions” authority, which entails the procurement of cutting-edge, frequently large-scale, research and developmental work.<sup>15</sup>

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<sup>13</sup> Kelman, “Buying Commercial” *supra* note 2, at 251.

<sup>14</sup> See Department of Labor, *Contracting for Commercial Items*, (July 21, 2001), available at <http://www.dol.gov/dol/oasam/public/regs/statutes/comlitem.htm>. See also James W. Brown and James E. Shipley, *Defense Commercial Pricing Management Improvement: Back to the Commercial Acquisition Reform Drawing Board* 18 J.L. & COM. 31 (Fall, 1998) (suggesting that the commercial item definition is too broad, which may lead to inclusion of items (a) that are not truly commercial and (2) lack prices determined by market forces).

<sup>15</sup> 10 U.S.C. § 2371. Other transactions were developed to “attract to the defense marketplace commercial concerns with leading edge technologies who were generally unable or unwilling to comply with DOD-unique requirements” See *generally* <<http://www.abm.rda.hq.navy.mil/bptrans.cfm>> explaining that: “Other

Similar concerns arise with regard to the definition of commercial services.

The first category of commercial services includes installation, maintenance, repair, training, and other service in support of commercial items.<sup>16</sup> In contrast, stand-alone commercial services, which must be based on established catalogue or market prices, are:

Services of a type offered and sold competitively in substantial quantities in the commercial marketplace based on established catalogue or market prices for specific tasks performed under standard commercial terms and conditions. . . .<sup>17</sup>

The definition, however, precludes, among other things, services sold at hourly rates for unspecified tasks.<sup>18</sup>

To generate momentum for these new efforts, the procurement regulations direct acquisition officials to “define requirements in terms that enable and

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transactions are agreements used for research and prototype projects that are principally defined in terms of what they are not. They are not a contract, grant, or cooperative agreement. To the extent that a statute or regulation is limited in its applicability to the use of a contract, grant or cooperative agreement, it generally does not apply to an other transaction. For example, the Contracts Disputes Act and the Federal Acquisition Regulation do not apply to other transactions.”

<sup>16</sup> 48 C.F.R. § 2.101.

<sup>17</sup> 48 C.F.R. § 2.101. Established catalogues and market prices are discussed at 48 C.F.R. § 15.804-3.

<sup>18</sup> This has led to a push for regulations including additional contract types such as time-and-materials and labor-hour. *But see The New Commercial Acquisition Rules, available at* <<http://www.ffhsj.com/cmemos/00f4143>> (“[The exclusion of services sold at hourly rates] would seem to be a conscious choice of the regulation writers, not to import the special restrictions on commercial services contained in the commercial item rules into the new rules governing the TINA exceptions for adequate price competition and established catalog or market price.”).

encourage offerors to supply commercial items”<sup>19</sup> and, to the maximum extent practicable, acquire non-developmental items to meet agency needs.<sup>20</sup>

Accordingly, agencies now enjoy broad discretion to determine whether or not supplies, services, and nondevelopmental items are consistent with the FAR Part 12 commercial definitions.<sup>21</sup>

With regard to purchasing practices, the new vocabulary arises primarily in the context of the new vehicles or mechanisms, discussed below. But even the absence of new language could not insulate the new policy from criticism.

Observers are quick to point out that neither the enabling legislation nor the regulations define the “standard” or “customary” commercial practices intended to serve as a model for government behavior.<sup>22</sup>

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<sup>19</sup> 48 C.F.R. § 11.002.

<sup>20</sup> See also *The New Commercial Acquisition Rules*, available at <<http://www.ffhsj.com/cmemos/00f4143>> (“Requirements must be defined so that commercial items (or NDI if commercial items are not available) can fulfill those requirements.”) The preference for NDI’s may have the effect of “significantly expanding the government’s ability to acquire cutting-edge technology from commercial companies.”

<sup>21</sup> See 48 C.F.R. § 12.301(e); (f).

<sup>22</sup> Carl L. Vacketta & Susan H. Pope, *Commercial Item Contracts: When is a Government Contract Term or Condition Consistent with “Standard” or “Customary” Commercial Practice?* 27 PUB. CONT. L.J. 291, 301-306 (1998) (“this failure raises the concern that a federal agency or one of its [contracting officers] may conclude that a term or condition is consistent with customary commercial practice based upon merely isolated or anecdotal information rather than upon mere substantiated industry research and statistical analysis of its usage”). The FAR drafters “created a ‘tailoring’ mechanism by which a CO could alter, add to, or delete from the nineteen ‘core’ terms and conditions to reflect more accurately that which is ‘customary’ in the particular industry.” *Ibid.* at 298. Conversely, the FAR “limits the CO’s ability to tailor” by prohibiting contracting

## 2.2. Attracting and Utilizing Commercial Firms

One of the primary justifications for the commercial movement derived from the widely held belief that many government unique aspects of the procurement system have made selling to the government unattractive to commercial entities. Firms are hesitant to sell commercial products to the federal government because of the complex web of procurement requirements (whether deriving from laws, regulations, policies, or practices). They fear the requirements related to tracking and disclosing cost data and other financial information, in conjunction with the government's broad audit rights, can lead to costly missteps. They are intimidated by scores of government unique terms and conditions and daunted by the prospects of granting unlimited rights to the government in their technical and proprietary data. Many of these concerns derive from established government practices that are uncommon in, and perceived as untenable by, the private sector.”<sup>23</sup>

Accordingly, one of the most difficult aspects of the government's efforts to adopt commercial practices and strategies was the elimination of the barriers that dissuaded commercial firms from entering the government market. The government's most successful efforts in this regard were: (1) reducing and eliminating government-unique financial record keeping and reporting (or

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officers from tailoring those contract terms and conditions that “implement statutory requirements” and those terms and conditions that are “inconsistent with customary commercial practice without first going through a written waiver process set up by the contracting agency[.]” *Ibid.* at 298-299.

<sup>23</sup> See H.R. REP. NO. 103-545, pt. 2, at 104 (1993).

disclosure) requirements; (2) eliminating numerous contractor certifications and representations; and (3) reducing its reliance upon government-unique specifications and standards.<sup>24</sup>

Government-unique accounting requirements frequently head the list of maladies that prevent commercial businesses from contracting with the government.<sup>25</sup> These requirements prohibit reimbursement of many commonly-incurred costs of doing business (such as advertising, alcohol, and lobbying),<sup>26</sup> grant the government substantial access to contractors' accounting books through disclosure and audit,<sup>27</sup> and typically lead to the establishment of government unique record-keeping. Moreover, businesses that run afoul of the complex requirements find themselves subject to severe criminal and civil sanctions (in

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<sup>24</sup> Kelman, *supra* note 2, at 250-253.

<sup>25</sup> The government has not completely eliminated the audit rights that traditionally deterred businesses from entering into contracts with the government. *See* 48 C.F.R. § 52.212-5(d)(1) (the government retains the right to examine a contractor's "directly pertinent records involving transactions related to this contract"); 48 C.F.R. § 15.402(a)(1), (2); 15.403-1; 15.403-3(b) (granting contracting officers the discretion to obtain pricing information in order to determine price reasonableness when adequate competition is lacking).

<sup>26</sup> *See, e.g.*, 48 C.F.R. § 31.205-1 (public relations and advertising costs) through 31.205-51 (costs of alcoholic beverages).

<sup>27</sup> *See* 48 C.F.R. 52.215-2 (audit of books and records). One of the partial success of the commercial acquisition effort were the expanded exemptions from Truth in Negotiations Act (TINA), 10 U.S.C. § 2306a; 41 U.S.C. § 254b; 48 C.F.R. § 15.4. TINA requires the submission of cost and pricing data during the negotiation of large, negotiated contracts unless certain exceptions (including the procurement of commercial items) apply. The new TINA exemptions also limit the extent of the government's access to business records. *See* 48 C.F.R. § 52.215-41(a)(2).

addition to nightmarish media scrutiny). Contractors often complain that the rapidly escalating sanctions of the Civil False Claims Act (FCA),<sup>28</sup> which may be imposed for incomplete or inaccurate disclosure, represent a significant, if not insurmountable, barrier to private firm participation in government contracts.<sup>29</sup> Accordingly, the revised practices attempt to exempt commercial firms from these record-keeping, disclosure, and audit requirements when they provide commercial items or services to the government.

Professor Kelman expected that “reducing reporting requirements and relying more on competition as an alternative to more traditional forms of

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<sup>28</sup> 31 U.S.C. § 3729.

<sup>29</sup> Although changes to TINA eliminated many of the barriers to attracting and utilizing firms, “most favored customer” pricing remains a major concern. *See generally* Richard J. Wall and Christopher B. Pockney, *Revisiting Commercial Pricing Reform* 27 PUB. CONT. L.J. 315, 326 (1998) (Most favored customer prices are risky for contractors. “A large commercial company might never be sure of what constituted the best deal, thus running the risk of violating the broad scope of disclosure obligations covering best discounts and greatest concessions.”) I reject, however, the contractor community’s broader assertions regarding the apocalyptic impact of the False Claims Act’s qui tam provisions. Specifically, I do not perceive the False Claims Act as a significant barrier to entry with regard to firms’ willingness to do any business at all with the federal government. I am unpersuaded that any significant number of commercial firms refuses to do business with the government based solely upon fear of the False Claims Act. As my colleague, Professor Bill Kovacic concedes, “it would be an exaggeration to say that . . . oversight, standing alone, commonly induces firms to deal solely in the commercial arena. *It is doubtful that any single attribute of the procurement regulatory system has that discouraging effect.*” William E. Kovacic, *The Civil False Claims Act as a Deterrent to Participation in Government Procurement Markets* 6 SUP. CT. ECON. REV. 201, 239 (1998) (emphasis added) (suggesting that contractors regard this “oversight as a costly, substantial burden of doing business with the government”).

oversight (such as audits) should also significantly enhance the government's ability to rely on the commercial marketplace.”<sup>30</sup> He argued that government-unique audit rights are unnecessary when utilizing commercial practices because the “purchase of a commercial item logically lends itself to simplified procedures because there exists a yardstick in the commercial marketplace against which to measure price and product quality and to serve as a surrogate for government-unique procedures.”<sup>31</sup>

The government also historically required that contractors sign numerous representations and certifications prior to, or at the time of, contract agreement. Collected in section K of the uniform contract format,<sup>32</sup> these “reps and certs,” as they are commonly known, required contractors to acknowledge that, among many other things, they qualify as a small business; comply with applicable employment, labor, and environmental laws; will deliver an end product manufactured primarily in the U.S.; and have *not* disclosed their pricing to their competitors, offered gratuities or kickbacks, or been convicted of certain offences. In response, the Clinger-Cohen Act mandated the elimination of the lion’s share of these representation and certification requirements.<sup>33</sup> Despite significant improvement, a daunting consolidated list of representations and certifications remains for

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<sup>30</sup> Kelman, *supra* note 2, at 252.

<sup>31</sup> *Ibid.* at 254 n. 11 (*citing* H.R. REP. NO. 104-222, pt. 1, at 48 (1995)).

<sup>32</sup> 48 C.F.R. §§ 14.201-1, 15.204-1.

<sup>33</sup> Pub. L. No. 104-106, § 4301(b); 62 Fed. Reg. 233 (January 2, 1997).

commercial contractors.<sup>34</sup> The reforms also eliminated or modified many non-essential (but by no means all) provisions and clauses and made certain government unique laws inapplicable to commercial item acquisitions.<sup>35</sup>

Further, plenty of commercial firms hesitated to pursue government business because of the numerous unique specifications that permeate government contracts. Humorous anecdotes abound of government-unique recipes for fruitcakes, detailed descriptions of lead pencils, or complex requirements for manufacturing ashtrays. Proponents of acquisition reform claim that, “acquiring Government-unique items often engenders higher costs, increased Government design risk, and greater potential for obsolescence... [because] the Government often pays for all production costs including added set up charges, special tooling and any research and development costs. Products take a much longer time to acquire than those commercial items that are readily available ‘off-the-shelf’.”<sup>36</sup> As a result, the current regulations make clear that the buyer is expected to conduct market research to determine whether commercial items could meet the agency’s requirements and acquire commercial items when they are available.<sup>37</sup>

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<sup>34</sup> 48 C.F.R. §§ 12.301(b)(1), 52.212-3.

<sup>35</sup> 48 C.F.R. § 12.301; General Services Administration, *White Paper: Acquisition Sources and Alternatives* (August 1998) [hereinafter *GSA, White Paper*], available at <<http://www.itpolicy.gsa.gov/mke/acqwp.htm>>.

<sup>36</sup> *Memorandum from William N. Gormley, CPPO Assistant Commissioner, Office of Acquisition to FSS Contracting Activities (FC Distribution List)* (February 26, 1999) <<http://www.dsp.dla.mil/policy/FC-99-3.html>>.

<sup>37</sup> 48 C.F.R. §§ 12.101(a), (b).

The description . . . must contain sufficient detail for potential offerors of commercial items to know which commercial products or services may be suitable. . . . [The agency should] describe the type of product or service to be acquired and explain how the agency intends to use the product or service in terms of function . . . , performance requirement[, ] or essential characteristics. . . . [This] allows offerors to propose methods that will best meet the needs of the Government.<sup>38</sup>

### **2.3. Reliance on Commercial Contractual Vehicles**

Ultimately, however, the most visible manifestation of the commercial regime is the proliferation of new or revised contractual vehicles that have been deemed consistent with commercial practice. These range from common sense application of commonly available tools – such as credit cards or electronic catalogues – to sophisticated vehicles that allegedly follow private sector examples.

#### **2.3.1. Contract Pricing: A Threshold Issue**

Examining the types of contracts employed by the government highlights some of most difficult issues to reconcile in the discussion of commercial purchasing. As a matter of policy and regulation, when acquiring commercial items, agencies generally must use firm-fixed price contracts.<sup>39</sup> In conventional

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<sup>38</sup> 48 C.F.R. § 12.202.

<sup>39</sup> *See* 48 C.F.R. § 12.207 (“Agencies shall use firm-fixed-price contracts or fixed-price contracts with economic price adjustment for the acquisition of commercial items.”) The FAR also permits agencies to use indefinite-delivery contracts where the prices are established based on a firm-fixed-price or fixed-price with economic price adjustment. *See* 48 C.F.R. § 16.5.

fixed-price contracting, if a contractor fulfils its contractual promise for less than the contract price, the contractor realizes a profit. (The contractor's profit is calculated by subtracting its incurred costs from its contract price.) If performance proves more costly to the seller than the contract price, the seller suffers a loss. The government's use of fixed-price vehicles for commercial purchasing makes sense because fixed-price contracts are most appropriate where performance risk is low. Performance risk should be low when the government seeks to procure things currently available in the commercial marketplace, whether office furniture, personal computers, or telephone service (where the government agrees to pay a fixed-price for each minute of telephone usage, whether local or long distance).

If a company manufactures and widely advertises for sale its product or service, consumers might reasonably conclude that, barring unanticipated contingencies, the company is capable of delivering the promised goods or services on time for the price offered. Moreover, unless the government buys in unusually large quantities, the seller's price is determined by the seller's assessment of the market value of the item or service (or, in other words what reasonable business people or consumers are willing to pay), rather than isolated negotiations between the seller and the government buyer (in which the price is determined by the seller's projected cost of performing the contract).

Yet, frequently, the government obtains goods and services for which no market of consumers or businesspeople exist. In the absence of a market

mechanism to set prices, and particularly where the manufacturer or seller lacks sufficient production or marketing information or experience to set a reasonable price, the government employs a cost reimbursement contracting mechanism. The cost reimbursement mechanism, which obligates the government to reimburse the contractor for its reasonable costs to perform the contract,<sup>40</sup> eliminates the contractor's risk that performance will become prohibitively expensive. (At the same time, the government assumes the risk of cost overruns, which it attempts to control to some extent by utilizing various long-standing tools, such as the Limitation of Costs Clause.<sup>41</sup>)

The correlation between commercial contracting and contract type selection quickly devolves into circular reasoning. Reform advocates suggest that the government, whenever possible, should purchase commercial items or services. Pursuant to the regulations, commercial items can only be purchased using fixed-price contracts. This should pose no problem because these items should already have been developed outside of the government marketplace, and the government should find (when it enters the marketplace) that savvy consumers and businesspeople have established, for any given commercial item, an optimal (or at least a reasonable) price.

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<sup>40</sup> These contracts are structured so that profit or fee can be calculated independent of the contractor's incurred costs. *See, e.g.*, 48 C.F.R. § 16.306.

<sup>41</sup> 48 C.F.R. § 52.232-20.

Accordingly, reform advocates frequently broaden the debate to suggest that the government should, on a more global basis, move towards price-based contracting<sup>42</sup> (or away from cost-reimbursement contracting). This theory assumes that, if the government consistently tries to avoid cost-based contracts and buy based upon market prices (or simply mandates price-based contracting to the exclusion of cost-based contracting), the government will gravitate towards commercial solutions available in the marketplace. Further, if the government relies upon contractor or market pricing, there is no need for contractors to disclose propriety cost information to the government (which, historically, has been deemed necessary to negotiate cost reimbursement work).

All of which is true, unless the government needs items and services for which there is no commercial market, such as where the government requires development of hugely expensive and sophisticated military-unique items.<sup>43</sup> Contractors that agree to perform developmental work for fixed prices assume high, and in many cases unreasonable, degrees of risk. Historically, cost reimbursement contracts insulated those contractors from assuming unreasonable

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<sup>42</sup> “Price-based acquisition is a way . . . to buy . . . that does not rely primarily on a supplier providing cost data. . . . ‘[P]ure’ price-based acquisition is at one end of a continuum. At the other end is ‘pure’ cost-based acquisition . . . where virtually every aspect of the [government-]supplier relationship demands that the supplier provide [the government] with actual or estimated costs.” Defense Contract Management Agency, *Price Based Acquisition Report*, available at <<http://www.dcmamil/reference/pbareport.doc>>.

<sup>43</sup> In the U.S. procurement system, these are frequently dubbed “major systems.” See generally 48 C.F.R. § 34, referencing OMB Circular A-109.

risks, but that insulation comes at a price. The price, at a minimum, is that the government buyer obtains access to much of the company's proprietary cost information. Once the government begins requesting proprietary cost or pricing data, most agree that the transaction is no longer perceived as commercial.

This long-winded scenario bears out this author's perception, discussed further below, that commercial purchasing policies suit the government best when applied in moderation. Commercial purchasing makes sense in low-dollar, high-volume, lower complexity procurements. As individual procurements expand in size, grow in complexity, and assume greater significance, it becomes more rational to fall back upon procurement policies intended to insulate government agencies, end users, and taxpayers from undue risk.

### **2.3.2. Other Commercial Vehicles**

In developing a commercial item purchasing regime, the government has become increasingly reliant on commercial contractual vehicles. The various vehicles reflect the drafters' intent to simplify the solicitation and evaluation procedures.<sup>44</sup> The acquisition reform movement created numerous options for contracting officers to satisfy their requirements and provided contracting officials with greater discretion to determine how best to achieve their goals.<sup>45</sup> Numerous

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<sup>44</sup> *See generally* 48 C.F.R. § 12.601.

<sup>45</sup> GSA, White Paper, *supra* note 35.

“streamlined solicitation procedures” sprang up, promising to reduce the time required to acquire commercial items.<sup>46</sup>

This author believes that the single most successful effort to make the government more commercial is found in the low-visibility arena of high-volume, low-dollar purchasing. In this arena, two innovations – creation of the micro-purchase threshold<sup>47</sup> and the use of purchase cards<sup>48</sup> – have dramatically altered the way in which the government does business. Further, these developments appear

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<sup>46</sup> See, e.g., 48 C.F.R. § 12.601 (“These procedures are intended to simplify the process of preparing and issuing solicitations, and evaluating offers for commercial items consistent with customary commercial practices.”); 48 C.F.R. § 12.602 (b) (“For many commercial items, the [evaluation] criteria need not be more detailed than technical (capability of the item offered to meet the agency need), price and past performance”).

<sup>47</sup> See GSA, White Paper, *supra* note 35 (“The underlying philosophy . . . is the realization that expending considerable effort for a competition under \$2,500 would not generate sufficient savings to justify the expense. As such, . . . if the price is considered reasonable, [micro-purchases] may be awarded without soliciting competitive quotations. . . .”)

<sup>48</sup> 48 C.F.R. § 13.001 explains that the “‘Government-wide commercial purchase card’ . . . [is] similar in nature to a commercial credit card, issued to authorized agency personnel to use to acquire and to pay for supplies and services.” See also generally, 48 C.F.R. § 13.301. (“Purchase cards let agencies streamline the buying process, use online catalogs, improve the payment process and make payments electronically.”) Statement of Frank P. Pugliese Jr., commissioner of GSA’s Federal Supply Service, *available at* <[http://www.gcn.com/vol19\\_no19/news/2400-1.html](http://www.gcn.com/vol19_no19/news/2400-1.html)>. For an extensive examination of the proliferation of purchase card activity, see Neil S. Whiteman, *Charging Ahead: Has the Government Purchase Card Exceeded Its Limit?* 30 PUB. CONT. L.J 403 (2001); Steven L. Schooner & Neil Whiteman, *Purchase Cards and Micro-Purchases: Sacrificing Traditional United States Procurement Policies At the Altar of Efficiency* 9 PUB. PROCUREMENT L. REV.148 (2000).

truly commercial, in that the government's behavior mimics that of common consumers and businesses.

Although the government only began widespread use of conventional charge cards for purchasing in the last decade, the practice spread quickly.<sup>49</sup> The real catalyst credited with accelerating government purchase card usage was the legislatively created micro-purchase authority below the threshold of \$2,500.<sup>50</sup> Below that threshold, buyers may ignore the government's normal procurement rules and procedures (which mandate transparency and competition). Quite simply, government buyers, armed with a purchase card, can purchase what they want, from whomever they please, however they prefer (in person, over the telephone, via the Internet, etcetera), so long as individual purchases do not exceed \$2,500.

Critics fear that this flexible procedure, without diligent oversight, is susceptible to abuse. For example, buying offices recognize the benefits – in terms

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<sup>49</sup> Although the Government long had used plastic purchase or charge cards for employee travel and fleet use (e.g., gasoline purchases), it did not permit charge card use for the general procurement function. Instead, for small purchases, the Government primarily relied upon purchase orders or its equivalent of petty cash, known as the imprest fund. The imprest fund is a “cash fund of a fixed amount established by an advance of funds, without charge to an appropriation, from an agency finance or disbursing officer to a duly appointed cashier, for disbursement as needed from time to time in making payment in cash for relatively small amounts.” 48 C.F.R. § 13.001.

<sup>50</sup> 48 C.F.R. § 2.101 explains that a micro-purchase is an acquisition of supplies or services which does not exceed \$2,500, except for construction, where the limit is \$2,000. *See generally* 41 U.S.C. § 428; 48 C.F.R. §§ 13.201, 13.202; Pub. L. No. 103-355, § 1054 (October 13, 1994).

of their time and effort -- of (improperly) splitting their larger requirements into smaller units to stay below micro-purchase threshold.<sup>51</sup> In Fiscal Year 2000, more than 670,000 government employees spent in excess of five percent of all Federal procurement dollars (more than \$12 billion) without: risk of protest or third-party monitoring; full and open competition typically mandated for the government's business;<sup>52</sup> use of standard solicitation provisions and contract clauses that insulate the government from frequently acknowledged risks; or visibility<sup>in</sup> the Federal Procurement Data System (FPDS).<sup>53</sup>

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<sup>51</sup> Although there is only limited insight into how the purchase cards are used, isolated problems have surfaced. *See generally* Glenda Cooper, *Education Dept. Credit Cards Seized in Anti-Fraud Effort*, WASHINGTON POST, July 18, 2001, at A27.

<sup>52</sup> *See generally* The Competition in Contract Act of 1984 (CICA), Pub. L. No. 98-369, Div. B., Title VII, 98 Stat. 1175 (July 18, 1984).

<sup>53</sup> This entails more than 23 million transactions per year. *See* Federal Procurement Data System, *Federal Procurement Report* (2000), p. 13, *available at* <<http://fpds.gsa.gov/Fpds/FPR2000a.pdf>>. The FPDS provides statistical data -- at the time of contract award or inception -- about Federal Executive Branch procurement contract transactions. Contrasted with the extensive information provided for most procurements, the FPDS provides only summary data on purchase card transactions -- no more than the number of transactions and dollars spent by individual agencies. *See generally* 41 U.S.C. §§ 405(d)(4)(A), 417, mandating the establishment of an automated system for collecting, evaluating, and disseminating information about Federal procurement contracts. *See also* FPDS (last visited August 1, 2000) <<http://fpds.gsa.gov/fpds/fpds.htm>>. It appears that the Defense Department is moving in the direction of at least attempting to remedy this situation. *See generally* 65 Fed. Reg. 39707 (June 27, 2000), amending, *inter alia*, 48 C.F.R. § 204.670-1, including, for the first time, “[p]urchases made using the Governmentwide commercial purchase card” in the definition of “contracting action.”

Once purchases become large enough to exceed the micro-purchase threshold, government buyers proceed to the streamlined simplified acquisition procedures (SAP).<sup>54</sup> Simplified acquisition procedures<sup>55</sup> are “designed to reduce the administrative burden of awarding the lower dollar value procurements. They allow informal quoting and competition procedures, encourage accepting oral quotes vice written quotations, prefer comparing quoted prices vice conducting negotiations, and provide streamlined clauses to support the award document.”<sup>56</sup> These purchases – *above* the micro-purchase threshold, but *below* the separate simplified acquisition threshold of \$100,000 – are not free from *all* government

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<sup>54</sup> See GSA, White Paper, *supra* note 35 (“Simplified acquisition procedures (SAP) recognize that the time and expense of conducting a full and open competition is not warranted for acquisitions under the SAP threshold (generally \$100,000). As such, SAP encourages the use of several techniques including; Credit card purchases; Purchase Orders; electronic purchasing; Blanket Purchase Agreements (BPAs)... (1) permit innovative approaches (2) emphasize the use of FACNET and other electronic purchasing techniques (3) permit oral solicitation in certain circumstances (3) allow the use of a combined synopsis/solicitation (4) have eliminated many full and open clauses and provisions (5) Simplified acquisitions are set aside for small business (if over \$2,500), publicized, and competed to the "maximum extent practicable.")

<sup>55</sup> See generally Pub. L. No. 103-355 §§ 4001, 4201, et seq.; 48 C.F.R. Subpart 13.3. “‘Simplified acquisition threshold’ means \$100,000, except that in the case of any contract to be awarded and performed, or purchase to be made, outside the United States in support of a contingency operation . . . or a humanitarian or peacekeeping operation . . . , the term means \$200,000.” 48 C.F.R. § 2.101 (citations omitted). Simplified acquisition procedures are intended to: “(a) Reduce administrative costs; (b) Improve opportunities for small, small disadvantaged, and women-owned small business concerns to obtain a fair proportion of Government contracts; (c) Promote efficiency and economy in contracting; and (d) Avoid unnecessary burdens for agencies and contractors.” 48 C.F.R. § 13.002.

<sup>56</sup> *Simplified Acquisition Procedures (SAP)*, at <<http://www.acq-ref.navy.mil/turbo2/topics/be.cfm>>.

procurement rules and procedures. Yet they offer substantial insulation from the normal time-consuming competition- and transparency-related requirements. Accordingly, these streamlined procedures also increase efficiency at the expense of public notice and, as a result, competition and oversight.

The defining characteristics of many of these actions is that the contracting officer: (1) need only “promote competition to the maximum extent practicable” as opposed to seeking full and open competition;<sup>57</sup> (2) can limit the competition to as few as three vendors “within the local trade area”; (3) may “solicit quotations orally to the maximum extent practicable”; and (4) in certain circumstances, solicit from a single source.<sup>58</sup> Contrasted with the government’s typical policy of broadly advertising its procurements,<sup>59</sup> fewer firms are aware of (or realize they missed the opportunity to compete for) the large number of Federal purchases under the \$100,000 simplified acquisition threshold. Procurement officials claim that the federal government benefits from these contracts because they reduce contract award times, administrative costs, prices, and delivery times for products and services. The government has considered raising the \$100,000 threshold to \$5

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<sup>57</sup> GSA, White Paper, *supra* note 35.

<sup>58</sup> 48 C.F.R. §§ 13.104, 13.106-1(b), (c). It appears that even minimal competitive market research – in this case requesting quote from three sources – is not required. *See* Cybertech Group, Inc. v. United States, 48 Fed. Cl. 638 (2001).

<sup>59</sup> For other purchases, the Government publicizes its pending requirements in print and on the Internet through the *Commerce Business Daily* (CBD). *See generally* 48 C.F.R. § 5.101(a)(1); *available at* <<http://cbdnet.gpo.gov>>.

million, yet recent reports have shown that the utilization of simplified acquisition procedures does not always result in a fair and reasonable price.<sup>60</sup>

The General Service Administration (GSA) Federal Supply Schedule (FSS) Contracts simplify an agency's ability to acquire commercial items.<sup>61</sup> The program permits program managers access to existing contracts with over 6,000 vendors offering millions of products. Consistent with the proliferation of government-sponsored electronic catalogues, the GSA – the closest the U.S. gets to a centralized purchasing agency – facilitates on-line purchasing through GSA Advantage!<sup>62</sup> Because they are flexible, the supply schedules are especially useful for repetitive purchases.<sup>63</sup> “This program, which is implemented in FAR part 8,

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<sup>60</sup> See 48 C.F.R. § 13.5, raising the threshold to \$5 million for a limited test period due to expire on January 1, 2002. Critics cite the SAP exemption from advertising in Commerce Business Daily as a possible reason for this failure. See generally GEN. ACCT. OFF., REPT. NO. GAO-01-517, *Contract Management: Benefits of Simplified Acquisition Test Procedures Not Clearly Demonstrated* (April 20, 2001), available at <<http://www.gao.gov>>.

<sup>61</sup> See GSA, White Paper, *supra* note 35 (“FSS contracts provide program/project managers simplified ordering vehicles to acquire commercial products and services: (1) nearly every commercial product and major service provider is available under GSA schedule; (2) ordering authority can be delegated; (3) considerable flexibility in the selection process; (4) Streamlined BPA's for repetitive purchases”); *but see id.* (“(1) the number of contractors with which orders are placed can dilute product standardization. Unless a BPA is established, each order must go through the FSS competitive process; (2) The FSS contracts set standard contract terms and conditions...Agency loses some control; (3)FSS contractor past performance information is generally not available”).

<sup>62</sup> “GSA Advantage! is a valuable shopping resource that anyone can use to find and research products, services and vendors. However, to make purchases on the system, you must be a Federal Government employee buying on behalf of your agency.” See generally <<http://www.gsaadvantage.gov>>.

<sup>63</sup> GSA, White Paper, *supra* note 35.

provides federal agencies with a simplified process for obtaining commonly used supplies and services at prices associated with volume buying.”<sup>64</sup> Although the FSS offers significant time savings, it has significant limitations. For example, each order must go through a competitive process and contractor past performance information is generally not available to buyers. Further, agencies cede a fair amount of control to the GSA system, because contract terms and conditions are set when the FSS contract is formed.<sup>65</sup>

Agencies frequently use “blanket purchase agreements” (BPA’s) when they foresee a continuing need for products or services.”<sup>66</sup> BPA’s allow the agency to “aggregate requirements and obtain quantity discounts from the vendors” because once the BPA is awarded, further competition is not required.<sup>67</sup> Government buyers may use BPA’s to “negotiate lower prices and better delivery terms” instead of awarding new contracts. Additionally, because BPA’s under the FSS schedules theoretically entail competitive procedures, “schedule users are not required to synopsize requirements, seek further competition, make a separate determination

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<sup>64</sup> Linda S. Lebowitz, “Bid Protest Issues Arising in Commercial Item Acquisition.” (Winter, 1998) 27 PUB. CONT. L.J 429, 449.

<sup>65</sup> GSA, White Paper, *supra* note 35.

<sup>66</sup> *See* GSA, White Paper, *supra* note 35 (“A BPA for products is particularly useful where the agency wants to standardize on a set of products for interoperability and integration. Instead of conducting a competition for each purchase, the agency can conduct a one-time BPA competition”)

<sup>67</sup> *See* GSA, White Paper, *supra* note 35.

of fair and reasonable pricing, or consider small business set-asides.”<sup>68</sup> Blanket purchase agreements are useful “where the agency wants to standardize on a set of products for interoperability and integration.”<sup>69</sup>

Another type of contractual vehicle that merits examination is loosely referred to as the umbrella contract. These vehicles facilitate the government’s purchase of varying amounts of supplies or services during a fixed period (within stated limits, usually expressed in numbers of units or as dollar values), with deliveries or performance to be scheduled by placing orders directly with the contractor.<sup>70</sup> Indefinite-*delivery* contracts permit the time of delivery to remain unspecified in the original contract but later be established by the contracting officer during performance. An indefinite-*quantity* contract provides for volume fluctuations within stated maximum or minimum limits, of specific supplies or services to be furnished, with deliveries to be scheduled by placing orders with the

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<sup>68</sup> *Air Force, Navy Guidance Curtail New Blanket Purchase Agreements*, 68 FED. CONT. REP. (BNA) No. 18, p. 8 (November 17, 1997).

<sup>69</sup> See GSA, White Paper, *supra* note 35 (“A BPA for products is particularly useful where the agency wants to standardize on a set of products for interoperability and integration. Instead of conducting a competition for each purchase, the agency can conduct a one-time BPA competition”)

<sup>70</sup> 48 C.F.R. § 16.501 explains: “There are three types of indefinite-delivery contracts: definite-quantity contracts, requirements contracts, and indefinite-quantity contracts. The appropriate type of indefinite-delivery contract may be used to acquire supplies and/or services when the exact times and/or exact quantities of future deliveries are not known at the time of contract award. . . . [R]equirements contracts and indefinite-quantity contracts are also known as delivery order contracts or task order contracts.”

contractor.<sup>71</sup> Collectively, the two are more commonly referred to as indefinite-delivery/indefinite-quantity or ID/IQ contracts.<sup>72</sup>

The government's use of indefinite-quantity contracts is not new. What is novel is the legislative preference for making *multiple awards* of indefinite-quantity contracts. In multiple award ID/IQ contracts, the government uses a single solicitation for the same or similar supplies or services but awards a contract – in effect an opportunity to compete – to two or more previously identified sources.<sup>73</sup>

The most unique and popular of the new ID/IQ vehicles are the multiple award contracts, which serve a single agency, and the Government Wide Acquisition Contracts, or GWAC's, awarded and serviced by one agency, but made available to other agencies.<sup>74</sup> Similar to the GSA FSS schedule contracts, these ID/IQ contracts are existing contract vehicles (or umbrella contracts) that offer program managers a selection of products, services, and suppliers. This pool of contractors then

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<sup>71</sup> 48 C.F.R. § 16.504(a); RALPH C. NASH, STEVEN L. SCHOONER & KAREN O'BRIEN, 296 THE GOVERNMENT CONTRACTS REFERENCE BOOK (2d ed. 1998).

<sup>72</sup> See generally 48 C.F.R. § 16.5.

<sup>73</sup> 48 C.F.R. § 16.504(c). See GSA, White Paper, *supra* note 35 (“In contrast to GSA FSS contracts, the majority of [these contracts] are written for a particular purpose and contain special terms and conditions for that activity...FASA established a statutory preference for [these contracts]. In most cases, maintaining a competitive environment through multiple awards leads to decreased prices, increased quality, better performance, and increased flexibility for the agency.”)

<sup>74</sup> J.A. Howell, *Governmentwide Agency Contracts: Vehicle Overcrowding on the Procurement Highway*, 27 PUB. CONT. L.J., 395, 397 (1998).

competes for individual task or delivery orders under a streamlined “fair opportunity” process.

Proponents of GWAC’s assert that because they maintain a competitive environment throughout the life of the contract (at the task or delivery order level), their utilization results in “decreased prices, increased quality, better performance, and increased flexibility for the agency.”<sup>75</sup> Because Congress expected that there would be robust competition under this regime, the legislative mandate bars contractors from protesting award decisions for individual task or delivery orders (which effectively bars third-party contractor oversight). The theory was that protests would be superfluous in the anticipated hyper-competitive environment.<sup>76</sup> Unfortunately, less than a decade ago, the goods and services obtained through these individual task or delivery orders represented hotly contested individual procurements. Today, part and parcel of the multiple award ID/IQ contract phenomenon is the ability to by-pass time consuming “full and open competition,” which, for more than fifteen years, has served as the defining standard for award of most government contracts. As a result, despite the fact that competition proved to

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<sup>75</sup> GSA, White Paper, *supra* note 35.

<sup>76</sup> 48 C.F.R. § 16.505(a)(7) explains that: “No protest under [FAR] Subpart 33.1 is authorized in connection with the issuance or proposed issuance of an order under a task order contract or delivery order contract except for a protest on the grounds that the order increases the scope, period, or maximum value of the contract.”

be chimerical,<sup>77</sup> these contract vehicles insulate an ever increasing piece of the procurement pie from meaningful competition. Equally significant, these vehicles deny the government, contractors, and the public third-party oversight of this spending.

The rapid evolution of electronic commerce also serves as a useful study because the private sector, rather than the government, led the transition from paper-based procurement to e-commerce. As many Internet shoppers now recognize, e-commerce offers a cheap, accessible, and ubiquitous method of obtaining comparative and competitive information on product quality,

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<sup>77</sup> In principle, up-front competition is conducted for the initial multiple-award contract. Contractors were supposed to compete to become part of an umbrella contract, which offers them little more than the opportunity to compete for individual task or delivery orders. Unfortunately, the anticipated competition rarely materializes – agencies tend to include all comers on the contract vehicle. This makes sense, to the extent that inclusion on the contract is no more than an opportunity to compete, akin to a “hunting license.” Yet real competition also is absent in the task order stage. Because all “contract holders” may market their services directly to individual agencies, those agencies – affected by considerations including speed, convenience, personal preference, and human nature – frequently obtain those services on a sole source or non-competitive basis from those possessing these hunting licenses. As a result, legitimate competition infrequently occurs. *See generally* GEN. ACCT. OFF., REPT. NO. GAO/NSIAD-00-56 at 4, *Contract Management: Few Competing Proposals for Large DOD Information Technology Orders* (March 20, 2000). As a result, this popular, time-saving purchasing methodology proliferates despite its failure to comply with Congressional intent. Professor John Cibinic described the current situation as “virtual anarchy.” John Cibinic, Jr., *Task and Delivery Order Contracting: Congress Speaks, GAO Reports, and the FAR Does a Fan Dance*, 14 NASH & CIBINIC REP. ¶ 32 (June 2000) (“It is obvious that Congress smells something fishy but doesn’t quite know what to do about it.”).

availability, and price.<sup>78</sup> Governments play an important role in e-commerce, because, in its leadership role, it can either facilitate or inhibit electronic trade. “Government officials must respect the unique nature of the medium and recognize that widespread consumer choice and increased competition should be the defining features of the new digital marketplace.”<sup>79</sup> Fortunately, the government has embraced the power of e-commerce in order “to enhance . . . customer relationships, achieve leverage in the marketplace, reduce costs and the need to retain large inventories, and obtain faster and more reliable deliveries of material and services.”<sup>80</sup>

Government agencies have developed various resources in order to implement e-commerce into their procurement regimes. For example, agencies have developed catalogue systems accessible through the World Wide Web.<sup>81</sup>

Electronic catalogues offer several advantages. They enable agencies to exhaust fewer resources to make repetitive purchases, allow agencies to leverage buying

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<sup>78</sup> Professor David Darcy, *E-Government Best Practices: An Implementation Manual*, available at United States General Services Administration <<http://egov.gov/library.htm>>.

<sup>79</sup> Letter from the White House, Office of the Press Secretary, to the Heads of Executive Departments and Agencies (July 1, 1997) available at <<http://egov.gov/documents/ecpress.htm>>.

<sup>80</sup> L. Gordon-Murnan, *Business-to-Government E-Commerce Procurement: Business Models, E-Mails, and Special Groups*, (July 23, 2001), available at <<http://special.northernlight.com/ecommer/procurement.htm>> (citing The Federal Electronic Acquisition Team final report, *Streamlining Procurement through Electronic Commerce* (1994).)

<sup>81</sup> See, e.g., Defense Department’s E-Mall at <<http://www.emall.dla.mil/>>, and the Small Business Mall at <<http://www.smallbizmall.gov/>>.

buyer through “volume purchasing” and permit agencies to make “spot” purchases.<sup>82</sup> Conversely, the rapid, almost frenetic proliferation of these e-catalogues leads to government purchaser confusion. Also, in its increasingly balkanised configuration, e-catalogue shopping denies the government valuable opportunities to leverage its buying power to gain favorable pricing through volume purchasing.

Active buying agencies have jumped onto the bandwagon of exciting new electronic commerce techniques, such as utilizing “reverse auctions” to make commercial purchases.<sup>83</sup> Reverse auctions permit buyers to specify what they want to buy and suggest a price they are willing to pay; sellers then compete in an on-line auction hall to offer the best price for the product.”<sup>84</sup> Although certain problems remain with this new technology (such as formalizing the end of bidding and flexibility to entertain additional offers in “overtime”), proponents of reverse

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<sup>82</sup> Memorandum from Steven Kelman from the Office of Federal Procurement policy to the Agency Senior Procurement Executives and the acting Deputy Under Secretary of Defense. (March 14, 1997) *available at* <<http://www.arnet.gov/Library/OFPP/PolicyDocs/eccat327.html>>. Catalog systems involve: “a contract with pre-established business arrangements with industry; a means for the customer to identify and order goods and services, either from within an agency (intra-agency) or by more than one agency (inter-agency); and sufficient information (updated to reflect changes) for the customer to compare the items offered by performance, price and delivery.”

<sup>83</sup> *See generally* Buyers.Gov – Reverse Auctions *at* <[http://www.buyers.gov/private\\_home.html](http://www.buyers.gov/private_home.html)>.

<sup>84</sup> Colleen O’Hara, *GSA Moves Ahead with Reverse Auctions*, (June 1, 2001) *at* <<http://www.fcw.com/fcw/articles/2001/0604/web-buyer-06-06-01.asp>>.

auctions point to substantial savings achieved through the utilization of this procurement method.

Consistent with the e-commerce expansion, the government recently introduced FedBizOpps,<sup>85</sup> its fledgling “single point of entry” for procurement opportunities.<sup>86</sup> Intended as an electronic procurement clearinghouse, agencies use FedBizOpps to post relevant procurement information on the Internet (including procurement notices, solicitations, drawings, and amendments) and eventually receive electronic proposals. As this technology becomes more widely used, commercial vendors can react more quickly to procurement opportunities because they are better informed.<sup>87</sup>

#### **2.4. Reliance on the Private Sector to Perform Commercial Functions**

As suggested earlier, the government’s effort to act more like a business has coincided with a renewed interest in, and in so doing injected immediacy into, privatization and contracting out. Because the process of outsourcing existing

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<sup>85</sup> See generally, W. Kelley, *Electronic Posting System/ Federal Business Opportunities System Manual* (August 24, 2000) at <<http://www2.eps.gov/EPSSBuyersManual/coversheet.htm>> (“The EPS/FedBizOpps System provides the functionality to forward synopses for agency requirements to the Commerce Business Daily (CBD). The system also provides the functionality for vendors to obtain access to agency business opportunities and to register to receive email notification of these requirements.”)

<sup>86</sup> See generally <<http://www.eps.gov/>>.

<sup>87</sup> See United States General Services Administration, *FedBizOpps Designated as Governmentwide Point of Entry for Procurement Opportunities*, at <<http://www.eps.gov/PR-9825FedBizOpps.html>> (last visited May 18, 2001).

government functions reflects the government's willingness to increase its reliance on the private sector to perform its commercial functions, it provides a useful microcosm for examination here. There is a wide-spread perception that outsourcing reduces the size of the Federal government and permits the government to provide necessary services with less burden on the taxpaying public.<sup>88</sup> Further, proponents assert that outsourcing will lead agencies to conduct themselves in a more "businesslike manner," increasing flexibility and taxpayer savings.<sup>89</sup>

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<sup>88</sup> In response to these perceived needs, the Bush administration recently ordered over 40,000 federal workers to compete for their jobs with the private sector. Ellen Nakashima, *Bush Opens 40,000 Federal Workers' Jobs to Competition*, THE WASHINGTON POST, Friday, June 8, 2001, at A27. The naïve quest for a "smaller" government masks the more important policy question of whether a large shadow government (or contractor corps) is preferable to the perceived entrenched and bloated civil service). "The public does not want a government that works better and costs less, but one that looks smaller and delivers more." Consequently, the government has responded by outsourcing jobs outward to a shadow workforce. Paul C. Light, *The Public Service* (June 1, 1999) available at <<http://GovExec.com>>. Light suggests that the shadow government, which resided mostly outside the public's consciousness, reflects decades of personnel ceilings, hiring limits, and unrelenting pressure to do more with less.

<sup>89</sup> See also Statement of Thomas G. McInerney Lieutenant General, USAF (Ret.), Former President and CEO, BENS before the National Defense Panel of the Quadrennial Defense Review pursuant to the Military Force Structure Review Act Of 1996 available at <[http://www.bens.org/other\\_0497.html](http://www.bens.org/other_0497.html)> ("Outsourcing and privatization can do for defense what it did for America's leading edge businesses – free up resources to concentrate on core competencies... the Federal Government must accept "that when it comes to running commercial-type operations, the private sector has built a better mousetrap.").

The U.S. Government's policy is to rely on the commercial sector<sup>90</sup> or, more specifically, commercially available sources,<sup>91</sup> to provide commercial products and services. OMB Circular A-76 directs that "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."

This basic policy implies that all commercial activities should, or at the very least might, be contracted out to private concerns. The government defines commercial activities as functions operated by a Federal executive agency that provide a product or service that can be obtained from a commercial source.<sup>92</sup> The

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<sup>90</sup> In the process of governing, the Government should not compete with its citizens. 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 supply the products and services the Government needs. *See* OMB Circular A-76.

<sup>91</sup> A commercial source is a business or other non-Federal activity located in the United States, its territories and possessions, the District of Columbia or the Commonwealth of Puerto Rico, which provides a commercial product or service. *See* OMB Circular A-76.

<sup>92</sup> By definition, "inherently Governmental functions," cannot be obtained from a commercial source. Inherently Governmental functions are so intimately related to the public interest as to mandate performance by Government employees. These functions require either the exercise of discretion in applying Government authority or the use of value judgment in making decisions for the Government. Inherently Governmental functions normally fall into two categories: the act of governing (or the discretionary exercise of Government authority) or monetary transactions and entitlements, such as tax collection or control of the money supply. *See* OMB A-76. *But see* Statement of Max Sawicky, Economic Policy Institute, Commercial Activities Panel (Public Hearing, Washington, D.C. June 11, 2001) ("The OMB Circular's way of defining services that are 'inherently governmental' is seriously flawed. . . . "); Statement of John Sweeney, National President, AFL-CIO, Commercial Activities Panel (Public Hearing, Washington,

policy appears simple: if a private source can provide the product or service, the government should not be in the business of competing with that private source. To facilitate this policy, the government recently mandated that all agencies publicly disclose an inventory of all (non-inherently governmental) commercial activities performed by federal employees.<sup>93</sup>

The primary exception to this policy, however, is an economic one, and it is manifested through the threshold mechanism for determining whether a commercial activity should be outsourced – the cost comparison. The government may keep performance of a commercial activity in-house if a cost comparison demonstrates that the government either is operating *or can operate* the activity at an *estimated* lower cost than a qualified commercial source. These small caveats – “operating or can operate” and “estimated lower cost” – permit the government to structure (or construct or, arguably, imagine) a most efficient organization (MEO) of the in-house government work force, and then compare this MEO with qualified commercial providers. Not surprisingly, this makes the cost comparison a controversial, frequently litigated linchpin of the contracting out process.<sup>94</sup>

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D.C. June 11, 2001) (“The government should broadly define the concept of “inherently governmental” functions. Not only should the government err on the side of caution in determining that a particular service is not inherently governmental, but should also be careful about the extent to which even commercial services are outsourced.”).

<sup>93</sup> The Federal Activities Inventory Reform Act (FAIR), Public Law No.105-270, 112 Stat. 2382 (1998).

<sup>94</sup> *See generally* James H. Ward, John C. Deal & Drew Hamilton *Outsourcing Pits Mission vs. Money* (April 1, 2001 ), *available at*

Problems arise because the contracting out of existing governmental functions typically means: (1) displacing government employees (or civil servants)<sup>95</sup> and (2) diffusing the management power of high-level government officials,<sup>96</sup> both of which frequently lead to intense institutional resistance to contracting out.<sup>97</sup> Accordingly, the private sector lacks confidence that the government fairly and accurately represents its true costs of performance. This cynicism is fuelled by the private sector's perception that the government does not include in its pricing the element of risk. If the government underestimates the true costs of its performance – a low-risk proposition in the absence of a profit motive or shareholders – the government is more likely to retain the work in-house. Underestimation of costs by private firms could lead to financial disaster. Yet

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<<http://www.govexec.com/features/0401/0401viewpoint.htm>>.

<sup>95</sup> Strong opposition comes from policymakers and labor unions that doubt that privatization and outsourcing actually saves the government money or make procurement more efficient. For example, popular author Robert Kuttner has pointed out several of the disadvantages of privatization: accountability, for-profit thriving at the expense of the nonprofit, hidden costs, and a possible decrease in the continuity and quality of service. *See The Disadvantages of Privatization Not Readily Apparent, Author Says*, 75 FED. CONT. REP. (BNA) NO.3, p. 66 (January 16, 2001).

<sup>96</sup> Opponents also argue that, because the private industry is not subject to the same rules that constrain public officials, accountability problems will arise. *See Ellen Nakashima, Bush Opens 40,000 Federal Workers' Jobs to Competition*, THE WASHINGTON POST, Friday, June 8, 2001, at A27.

<sup>97</sup> For example, government documents frequently suggest that “there is no assumption that the private sector will win the competition. This process has been referred to as ‘outsourcing’ or ‘contracting-out’, but only ‘competitive sourcing’ accurately describes and refers to the A-76 process.” *See Share A-76! Glossary* (defining “competitive sourcing” at <<http://emissary.acq.osd.mil/inst/share.nsf>>).

there are few, if any, analogous risks for government employees if subsequent performance experience demonstrates that government performance indeed proved more costly than the government's estimate.

### **3. Impediments To a Truly Commercial Federal Procurement Regime**

Numerous aspects of the Federal procurement regime inhibit the government's ability to adopt truly commercial practices. To some extent, these impediments highlight the differences between government norms and the mores of the commercial marketplace.<sup>98</sup> Some of these distinguishing issues reflect the nature of the U.S. political landscape, and many are larger than the fundamental buying practices that one would expect to constitute procurement policy.<sup>99</sup>

Historically, the government has behaved differently from private enterprise, and the courts reinforced the distinction between private and government

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<sup>98</sup> Although there are any number of efforts to distinguish the government from a commercial buyer, at least four differences imply that the government may never fully embrace commercial practices: (1) the government and commercial buyers have different responsibilities; (2) the government's funding rules – particularly the annual budget cycle that results in successive one-year contracts – limit the government's ability to properly consider affordability, cost of money, or financing; (3) the effect of social and economic programs; and (4) the impact of monopsony, particularly with regard to military-unique items. *See generally* James C. Roan, Jr., *Streamlining Government Acquisition (Or, 'Why Can't the Government Figure Out How to Use Commercial Practices?')*, ARMY LAW. 58 (May 1995).

<sup>99</sup> Conversely, this does not suggest that there are not systemic limits that have slowed the government's efforts to become more commercial. For example, the government's failure to invest in training in existing workforce has been penny-wise and pound-foolish. This failure has been exacerbated by seemingly random reductions in acquisition personnel leaving a graying, overburdened, and (all too frequently) dispirited procurement workforce.

contracts.<sup>100</sup> This distinction exposes a fundamental tension that underlies the ongoing evolution of federal government contract law, policy, and case law. Compelling arguments favor both the distinctions and the similarities between government and private purchasing. As my colleague, Joshua Schwartz observes, the U.S. embraces *both* the traditions of “exceptionalism” and “congruence.” The exceptionalist view of government contracting emphasizes the unique status, attributes, and needs of the federal government. The **congruent view** seeks to assimilate the government's contractual rights and duties to those of private entities.<sup>101</sup> The effort to buy more commercial items and incorporate commercial practices signals a resurgence of congruent-type policy making. Yet the exceptionalist constraints, which impede the implementation of a truly commercial government purchasing regime, cannot be ignored.<sup>102</sup>

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<sup>100</sup> See *Krygoski Construction Co., Inc. v. United States*, 94 F.3d 1537 (Fed. Cir. 1996), *cert. denied*, 117 S. Ct. 1691 (1997) (upholding termination for convenience). *But see* *United States v. Winstar Corp. et al.*, 518 U.S. 839 (1996). (limiting the government's rights and duties to those generally applicable to contracts between private individuals).

<sup>101</sup> Joshua I. Schwartz, *Liability for Sovereign Acts: **Congruence** and **Exceptionalism** in Government Contracts Law*, 64 GEO. WASH. L. REV. 633 (1996).

<sup>102</sup> The nature of the Government's buying practices prevents it from functioning similarly to the private sector. See generally Steven L. Schooner, *Impossibility of Performance in Public Contracts: An Economic Analysis*, (1986) 16 PUB. CONT. L.J 229, 262-63.

Of the many differences between government contracts and commercial contracts,<sup>103</sup> the greatest conceptual differences likely arise because the government is not driven by a profit motive.<sup>104</sup> In the absence of a profit motive (or the fear of incurring a loss), the government – both as an organization and a collection of individuals – lacks the engine that spurs the competitive marketplace. In this regard, there is stark contrast between the private and public sectors in the U.S. For example, in the private sector, executive compensation typically is structured to attract top talent and reward those who contribute to profit maximization (or shareholder return), frequently through stock incentive programs. In the public sector, civil service pay, based upon position and time in grade (rather than performance) frequently is criticized as inadequate; bonuses, when available, are insignificant.<sup>105</sup>

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<sup>103</sup> See generally Kathryn Dean Checchi, *Federal Procurement and Commercial Procurement under the U.C.C.—A Comparison*, 11 PUB. CONT. L.J. 358 (1980) (comparing the formation, modification, inspection/rejection rights, remedies, and warranties of government contracts and commercial contracts).

<sup>104</sup> See Michael K. Love, *Public v. Private Procurement: Your Tax Dollars at Work* (American Bar Association Section of Public Contract Law 1997 Annual Meeting Program) (claiming that the government practices can never mirror private practices because taxpayers want more than just best value for their money—they want social policies too; contracting officials must satisfy the “inconsistent needs of a variety of stakeholders” while private officials “satisfy corporate management [goals of profit maximization]first”); see also Marshall J. Doke, *Competition requirements in public contracting: the myth of full and open competition*, 64 FED. CONT. REP., (BNA) No. 3, special supplement (July 17, 1995) (“Most commercial purchaser buy on a sole source basis, buy more than they need, can afford to accept gifts, entertainment, and kickbacks”).

<sup>105</sup> A sampling of 50 of the largest U.S. industrial and service companies showed that total average executive compensation reached \$10.9 million in 2000. The bulk of pay came through stock options, with eleven corporate chiefs receiving

Further, because government purchases entail distribution of revenues collected through taxation, the government often treats the procurement system as a wealth distribution tool.<sup>106</sup> The government long has maintained that *all* qualified citizens should be made aware of, and have a fair chance to compete for, government contracts.<sup>107</sup> The comparative public procurement community would describe this as a commitment to transparency.<sup>108</sup> In practice, this means that,

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grant values in excess of \$50 million. CEOs at these firms received an average stock option package of \$6.5 million in 2000. *See* Shannon Jones, *US executive compensation rose 16 percent in 2000*, available at <<http://www.wsws.org/articles/2001/feb2001/exec-f28.shtml>>. Only recently was the salary of the President of the United States, the most highly paid civil servant, increased from \$200,000 to \$400,000. 3 U.S.C. § 102.

<sup>106</sup> The author does not believe that wealth distribution is one of the U.S. procurement system's primary goals. This does not suggest that the legislature does not use the procurement system to attempt to redistribute wealth. But those efforts are transitory for the same reasons they are controversial. Moreover, wealth distribution is merely a subset of the larger phenomenon of burdening the procurement process (or, for that matter, the process of governing) with efforts to promote social policies. These social policies potentially distribute wealth to domestic manufacturers, essential military suppliers, and small (and small disadvantaged and women-owned) businesses, while others mandate drug-free workplaces, occupational safety standards, compliance with labor laws, preferences for environmentally friendly purchasing practices, etcetera. Accordingly, while the author concedes that legislative manipulation of the procurement process is a significant aspect or feature of the system, the author cannot agree that wealth distribution is a fundamental purpose of the procurement regime.

<sup>107</sup> *See* Love, *supra* note 104 (arguing that competition is inconsistent with private procurement practices); *see also* Weaver, *supra* note 107 ("in spending taxpayer money, the government is obligated to act on a fair, open and equal basis (picking favorites and making custom deals could frustrate the government goal of promoting integrity)" unlike private companies who are not obligated to have competition.

<sup>108</sup> *See generally* Sue Arrowsmith, *Towards a Multilateral Agreement on Transparency in Government Procurement*, 47 INT'L & COMP. L.Q. 793, 796

despite commercial item reformations, government contracts continue to retain various practices, solicitation provisions, and contract clauses inconsistent with conventional commercial contracts.<sup>109</sup> Specifically, significant portions of a government contract are never truly subject to negotiation because certain contract terms and conditions are legislatively mandated.<sup>110</sup>

At first glance, the absence of “real negotiations” appears to be a practice difference, rather than an irreconcilable foundational issue. Many government solicitations (sealed bid procurements, which might be analogized to tendering) prohibit true negotiations by requiring “absolute responsiveness to invitations for bids.”<sup>111</sup> When responding to an invitation for bids, a government contractor must strictly abide by the form prescribed by the government. Any deviation from these requirements could result in a bid being declared non-responsive,<sup>112</sup> “even though (1988).

<sup>109</sup> See Love, *supra* note 104 (citing various government unique clauses including: rules for source selection, fairness requirements, negotiation procedures, agent authority, accounting and record keeping requirements, criminal penalties, public interest, political consequences, and national welfare impacts); see also F. Trowbridge vom Baur, *Differences Between Commercial Contracts and Government Contracts*, 53 A.B.A. J. 247 (March, 1967) (maintaining that the government always deals with contractors at an arm’s length (i.e.; limited authority of contracting officials, irrevocability of bids, limited negotiations, changes clause v. commercial “pre-existing legal duty rule”).

<sup>110</sup> For example, the *Christian* doctrine allows the government to obtain a benefit of a unique clause if it fails to include it in the contract (because they are read into the contract as a matter of law). See G.L. Christian & Assocs. v. United States, 312 F.2d 418 (Ct. Cl.), *certiorari denied*, 375 U.S. 954 (1963).

<sup>111</sup> vom Baur, *supra* note 109, at 248.

<sup>112</sup> Responsiveness is an objective, non-discretionary determination that a bid conforms to the invitations for bids. 10 U.S.C. § 2305(b)(3); 41 U.S.C. §

the bidder's deviation was accidental and the bidder is willing to correct his mistake."<sup>113</sup> Additionally, once bids have been opened, the government contractor cannot withdraw his or her bid. Unlike this firm-bid rule, commercial contracts are generally revocable up until the time of acceptance unless the parties explicitly agree that the offer will be irrevocable.<sup>114</sup>

By analogy, the UCC's contract formation standards are much less stringent than those required by the FAR. For example, under the UCC, a party may accept an offer "in any manner and by any medium reasonable in the circumstances."<sup>115</sup> Further, provided certain requirements are fulfilled, the UCC recognizes the formation of a contract even if the offeree's acceptance contains different or additional terms.<sup>116</sup>

Further, while other government solicitations (what we refer to as "requests for proposals") permit negotiations, the bartering remains limited.<sup>117</sup> Certain obligations are not subject to negotiation.<sup>118</sup> Conversely, negotiations are a

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253(b)(c); 48 C.F.R. §§ 14.301, 14.404-2.

<sup>113</sup> Checchi, *supra* note 103, at 362.

<sup>114</sup> See U.C.C. § 2-205 (firm-offers).

<sup>115</sup> UCC § 2-206(1)(a).

<sup>116</sup> UCC § 2-207. The official comments explain that: "Under this Article a proposed deal which in commercial understanding has in fact been closed is recognized as a contract."

<sup>117</sup> vom Baur, *supra* note 109, at 248.

<sup>118</sup> See J. C. Weaver, *Government v. Private Purchasing*, American Bar Association Section of Public Contract Law "Procurement Reform: A Never Ending Cycle?" (Sunday, August 3, 1997).

fundamental aspect of commercial contracts. In the commercial marketplace, a contract replete with non-negotiable, pre-drafted terms in which one party (for example, the government) enjoys substantially greater bargaining power is generally not enforceable in the commercial contracting arena.

Yet the question remains whether the differences between government and commercial practice can be reconciled. Many of these differences derive from significant governmental policies and cannot easily be jettisoned simply to promote commercial behavior. For example, the firm-bid rule, referenced above, promotes important government policies, *inter alia*, transparency, integrity and competition.<sup>119</sup> Commercial firms, unconcerned with transparency, scoff at public disclosure of bids and are not persuaded that rejecting other-than-“responsive” offers maintains a level playing field.

Another difference is the abundance of boilerplate terms or standard contract clauses. Although boilerplate is not uncommon in commercial contracting, the government does not engage in the “battle of the forms,”<sup>120</sup> because only the government’s standard clauses are used. Unlike commercial boilerplate terms, the

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<sup>119</sup> This author has asserted that these three policies have, in the past and should, in the future, continue to serve as the foundation for the U.S. procurement system. Steven L. Schooner, *Fear of Oversight: The Fundamental Failure of Businesslike Government*, 50 AM. U. L. REV. 627 (2001).

<sup>120</sup> See generally John E. Murray, Jr., *The Chaos of the ‘Battle of the Forms’: Solutions*, 39 VAND. L. REV. 1307 (1986); Douglas G. Baird & Robert Weisberg, *Rules, Standards, and the Battle of the Forms: A Reassessment of Section 2-207*, 68 VA. L. REV. 1217 (1982).

government's standard provisions and clauses cannot be ignored. The government's arsenal of standard clauses is not intended to be unfair to contractors, provided contractors learn what the clauses mean.<sup>121</sup> Inexperienced government contractors find themselves in serious trouble or waive valuable, valid claims simply because of a failure to understand the boilerplate. More strikingly, however, when dealing with the government, contractors are bound by certain regulatory requirements even if they inadvertently are left out of the contract.<sup>122</sup> This scenario simply could not exist in commercial practice where the existence of a commercial contract depends on a "meeting of the minds" – most U.S. courts refuse to enforce all or part of a contract that lacks mutual assent.

The UCC and its evolution<sup>123</sup> serve as an instructive model with regard to the development of commercial acquisition laws.<sup>124</sup> The UCC's drafters intended to create open-ended standards.<sup>125</sup> They believed that by avoiding formalities, they

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<sup>121</sup> vom Baur, *supra* note 109, at 248.

<sup>122</sup> vom Baur, *supra* note 109, at 249, (*citing* G.L. Christian and Associates v. United States, 312 F. 2d 418 (1963)).

<sup>123</sup> The drafters of this uniform commercial legislation continue to experience many difficulties in adopting revisions to the code. *See generally* Neil B. Cohen, *Taking Democracy Seriously*, 52 HASTINGS L.J. 667, 674 (March, 2001).

<sup>124</sup> The specialized courts and administrative boards that resolve government contract disputes remain cognizant of the UCC, but typically find that the government's purchasing regime is not bound by the UCC's dictates. *See generally* GAF Corp. v. United States, 932 F.2d 947 (Fed. Cir. 1991) (holding that the UCC is not binding in federal government contracts).

<sup>125</sup> Gregory E. Maggs, *Karl Llewellyn's Fading Imprint on the Jurisprudence of the Uniform Commercial Code*, 71 U. COLO. L. REV. 541, 554 (Summer, 2000).

could adjust the UCC to any changes in commercial practices. Similar goals are reflected in the government's regulation of commercial item acquisition. FAR Part 12 grants contracting officials broad discretion in awarding and soliciting contracts. This benefits commercial item acquisition by permitting broader contracting official discretion, greater flexibility, and less stringent rules that might better reflect private business practices. Similarly, it may allow the government to adapt to the rapid changes in technology.

Ultimately, however, greater buyer discretion means less governmental control over purchaser behavior. Less control entails sacrificing important policies, the most obvious of which is transparency. Unfortunately, policymakers rarely recognize, let alone acknowledge, these tradeoffs when implementing new policies.

While each of the issues discussed above suggests existing impediments to the government's adoption of commercial practices, a number of specific scenarios also merit examination. The exceptionalist view – justifying the government's unique behavior – seems unavoidable in certain significant circumstances.

### **3.1. Providing Necessary Services**

The government provides a wide range of vital services to the public, such as defense, air traffic control, and emergency disaster relief. In providing these services, the government perceives the public as its customer, end user, or beneficiary of the firm's contractual performance. In that context, the government

takes the position that the public is unwilling to experience performance interruptions for the sake of resolving contractual differences. Hence, the government maintains the right to force contractors to proceed with their work while their disputes are pending.<sup>126</sup> Ultimately, this suggests that the government does not believe that conventional contract damages – in the form of money – can make all of the parties, including the public as a party to the transaction, whole.

The longstanding requirement that a government contractor cannot stop work on a government contract seems defensible in the limited contexts discussed above. The policy remains subject to criticism, however, because it applies to *all* government contracts, regardless of the urgency of performance. As a result, contractors lose valuable leverage – in the form of a threat to stop work – in their ongoing contractual relationship with the government. As described below, however, this example is merely symptomatic of a larger inequity in the parties' footing.

### **3.1.1. Anticipating Contingencies**

The government recognizes that the universe of potential contingencies that may arise during the performance of its contracts exceeds its ability to anticipate those contingencies. Budgeting for contingencies is difficult and, as a matter of

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<sup>126</sup> For example, the standard “Changes” clause states that: “Failure to agree to any adjustment [of the contract price and/or schedule] shall be a dispute under the Disputes clause. However, nothing in this clause shall excuse the Contractor from proceeding with the contract as changed.” 48 C.F.R. § 52.243-1(e).

policy, the government has deemed the cost of insuring against contingencies untenable. Rather than burdening the public fisc (or the public) with the costs associated with anticipating contingencies, the government simply self-insures. In so doing, the government discourages contractors from padding their bids or proposals in anticipation of contingencies by promising to make the contractor whole if certain types of contingencies arise. Examples of this behavior include the government's right to unilaterally modify and terminate its contracts.

One of the most dramatic rights granted by a standard clause is the government's freedom to change contract terms without acquiring the consent of the contractor.<sup>127</sup> The standard "Changes" clause found in government contracts, "grants the government the unilateral right to order a change in the contract and allows the contractor an 'equitable adjustment' in exchange for this right."<sup>128</sup> Although the UCC abolished the common law pre-existing legal duty rule, in which any modification of the contract needed consideration in order to be enforceable, the UCC still requires the agreement of the two parties in order to be binding.<sup>129</sup>

Moreover, the classic or archetypical government-unique contract clause permits the government to terminate a contract for its own convenience, reimburse

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<sup>127</sup> vom Baur, *supra* note 109, at 250.

<sup>128</sup> 48 C.F.R. § 52.243-1, -2, -3, -4, -5; *see also* Checchi, *supra* note 103, at 363.

<sup>129</sup> *See* U.C.C. § 2-209.

the contractor for work done (plus its costs of closing out the contract), provide profit on the work performed, and avoid liability for the contractor's anticipated profit. "The concept . . . was developed primarily as a means to end the massive procurement efforts that accompanied major wars[,]""<sup>130</sup> but it subsequently morphed to include all government contracts.

Granted, to some extent, the government has been willing to limit its rights under these clauses in the acquisition of commercial items.<sup>131</sup> For example, commercial contractors benefit from a reduced cost information disclosure when negotiating a termination settlement.<sup>132</sup> Although the legislature *could* eliminate this unusual, exceptional contractual power, it would be ludicrous to expect the government to abandon such a right. Further, while some segment of the business

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<sup>130</sup> JOHN CIBINIC, JR. & RALPH C. NASH, JR., 1073 ADMINISTRATION OF GOVERNMENT CONTRACTS (3d ed. 1995).

<sup>131</sup> *See* 48 C.F.R. § 12.403(a) ("Consequently, the requirements of Part 49 do not apply when terminating contracts for commercial items and contracting officers shall follow the procedures in this section."); 48 C.F.R. § 12.403(b) ("The contracting officer should exercise the Government's right to terminate a contract for commercial items either for convenience or for cause *only when such a termination would be in the best interests of the Government*. The contracting officer should consult with counsel prior to terminating for cause.") (emphasis added); *see also* 48 C.F.R. § 52.212-4(c) (The FAR now provides that changes in commercial item contracts "may be made only by written agreement of the parties."); 48 C.F.R. § 52.212-4(l). (New provisions allow convenience terminations, but limit recoveries to a "percentage of the contract price reflecting the percentage of the work performed.").

<sup>132</sup> *See* 48 C.F.R. § 12.403 ("The contractor may demonstrate such charges using its standard record keeping system and is not required to comply with the cost accounting standards or the contract cost principles in Part 31. The Government does not have any right to audit the contractor's records solely because of the termination for convenience.")

community might benefit from a change, the cumulative risk to the public would outweigh any such benefit.

### **3.1.2. Developmental Work**

Much of what the government buys legitimately requires that the government invest in research and development (which entails risk) without an expected financial return on that investment. The commercial marketplace also constantly innovates and develops new technology. For example, Boeing and Airbus – in a highly competitive environment – attempt to anticipate consumer demand and compete to develop new aircraft (whether larger, faster, more fuel efficient, quieter, safer, or more comfortable) in the hope that their superior product will result in increased airline orders which, in turn, will lead to greater profits for shareholders and incentive payments to executives and employees.

While, arguably, airlines and passengers describe their needs, it is the commercial firm (here Boeing and Airbus) that determines whether its profits will be maximized by developing new aircraft or risking that, through lack of innovation, a new competitor may emerge. Conversely, the government's research and development investments are not market driven. For example, the government develops new submarines (more lethal, faster, quieter, safer, etc.) to defend ocean borders, neutralize ever-evolving enemy sea power, and project a nuclear threat. Thus, without being subjected to market forces, the government states its

requirements and compensates contractors to meet its needs. The contrast is dramatic.

In the commercial world, industry normally funds its own research and development, and companies develop products at their own expense with the idea that demand for the product will enable them to recoup their investment and, hopefully, make a profit. . . . [W]hat company would be willing to do that if only one buyer – the government – would be interested in its product, and the development costs run into the billions? . . . . We must distinguish between commercial . . . items . . . and items that must be specially developed for the military. . . .<sup>133</sup>

All of this, arguably, justifies the need for different contractual vehicles and pricing policy, introduced above. Boeing develops a new plane and determines what price the market will bear. The government describes a nuclear submarine and, while the private sector attempts to price the effort, the government frequently constrains true market pricing by publicly disclosing its available funding (which is determined by the legislature, not consumers). To the extent that such a relationship entails high degrees of risk, greater pricing flexibility is required, hence the use of cost reimbursement contracting. Due to the unusual risks associated with cost reimbursement contracting, other policies are implicated, such as the need for significant financial disclosures by contractors and governmental audit rights.

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<sup>133</sup> James C. Roan, Jr., *Streamlining Government Acquisition (Or, 'Why Can't the Government Figure Out How to Use Commercial Practices?')*, ARMY LAW. 58, 61 (May 1995).

Similarly, issues involving intellectual property arise. At one level, these issues resemble concerns experienced in the commercial marketplace. In the same manner as commercial airlines or shipping concerns, the government procures hardware (such as an aircraft carrier) and plans to have its own employees (for example, sailors or Seabees) service and repair the complex product. But the government wants, and arguably requires, additional rights. For example, the Navy may purchase components that it uses in other, similar platforms (such as aircraft engines or advanced radar or communications or weapon delivery systems) directly from one firm and provide them as “government-furnished property” to an airframe manufacturer. Unlike the scenario where an airframe builder (such as Boeing) buys engines directly from a supplier, the government requires intellectual property – sometimes as little as form, fit and function data, sometimes much more – from each of the contractors. Further, the government frequently prefers to obtain unlimited rights in technical data so that it subsequently can establish multiple sources for spare or repair parts.<sup>134</sup>

Accordingly, government-unique intellectual property rights long have been blamed for inhibiting the government’s access to technological advances made by

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<sup>134</sup> In defense contracts, the Government obtains unlimited rights in (1) data pertaining to an item, component, or process developed exclusively with Government funds; (2) studies, analyses, test data, or similar data produced as an element of the performance of a contract; (3) data created exclusively with Government funds; (4) form, fit, and function data; (5) data necessary for installation, operation, maintenance, or training purposes; etcetera. *See* 48 C.F.R. § 227.7103-5(a).

the private sector. Many commercial companies claim to avoid dealing with the government in order to protect their intellectual property rights.<sup>135</sup> Under the commercial procedures, however, the government is permitted to acquire “only the technical data and the rights in that data customarily provided to the public with a commercial item or process.”<sup>136</sup> While the private sector recognizes this concession is a step in the right direction, the government must cover much additional ground.

### **3.1.3. Military Service Contracting: An Anecdote**

As the government continues to contract out what it perceives as commercial services – driven by a strong executive mandate, as discussed above – defense support contracting raises unique concerns. Today, as more commercial firms perform military logistics and troop support, concerns arise regarding the status and activities of contractor personnel during mobilization or on the battlefield. Michael Davidson, an Army attorney, presents a thoughtful list of the advantages and disadvantages of this regime. The many advantages to using civilian contractor support include: (1) the ability to use (and maintain) scarce military

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<sup>135</sup> *Hearing Before the Subcommittee on Technology and Procurement Policy* (July 17, 2001) (statement of Jack Brock, Managing Director of Acquisition and Sourcing Management).

<sup>136</sup> 48 C.F.R. § 12.211 (“The contracting officer shall presume that data delivered under a contract for commercial items was developed exclusively at private expense. When a contract for commercial items requires the delivery of technical data, the contracting officer shall include appropriate provisions and clauses delineating the rights in the technical data in addenda to the solicitation and contract”).

personnel resources primarily to fight and defend; (2) the potential for cost savings (although this is difficult to demonstrate empirically); and (3) the flexibility for the military to project its limited force further and to different locations. At the same time, disadvantages of greater reliance on a civilian workforce include: (1) reduced opportunities for uniform personnel to acquire technical and managerial skills associated with support and logistics; (2) absence of power (other than monetary incentives) to maintain, direct, and control the workforce in unpleasant and dangerous conditions; (3) a reduced ability to defend rear areas or supplement forward forces when necessary; and (4) increased likelihood that civilians will become prisoners of war (under the Geneva convention) or be injured, tortured, or killed.<sup>137</sup> Only time and experience will tell whether the advantages outweigh the disadvantages.

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<sup>137</sup> Michael J. Davidson, *Ruck Up: An Introduction to the Legal Issues Associated with Civilian Contractors on the Battlefield*, 29 PUB. CONT. L.J 233, 263-267 (2000).

### 3.2. The Pervasive Effect of Social and Economic Policy

In the U.S., history suggests that the most daunting aspect of completely reforming the U.S. procurement system is the well established propensity of elected officials to impose social policies upon the procurement process.<sup>138</sup> It is axiomatic that these social policies impose significant costs upon the procurement system, regardless of whether they achieve their intended purpose.<sup>139</sup>

The tension between social policies and commercial purchasing has materialized in several different ways. First, after the 1990's acquisition reforms, contracting officials learned that pleasing the program manager (or end user) merited increased emphasis. Accordingly, it seems natural for government buyers to disregard these social policies to achieve greater customer satisfaction. Today,

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<sup>138</sup> See, e.g., 48 C.F.R. §§ 19 (small business programs); 22 (labor law compliance); 23 (environment, conservation, occupational safety, and drug-free workplace); and 25 (domestic preferences); for additional discussion, see Steven L. Schooner, *Mixed Messages: Heightened Complexity In Social Policies Favoring Small Business Interests*, 8 PUB. PROCUREMENT L. REV. CS78 (1999).

<sup>139</sup> Although voluminous reports detail the percentage of participation in the procurement process by various groups – such as small, disadvantaged, or women-owned businesses – little empirical information suggests that this participation derives from existing statutory preferences or programs. See generally *Federal Procurement Data System* at <<http://fpds.gsa.gov/>>.

for government buyers, customer service comes first, legislatively-mandated procurement policies finish second.<sup>140</sup>

Ultimately, however, something has to give. Either Congress must stop legislating social policy, or it must recognize that more commercial purchasing will render these policies ineffective (or, at very least, shift the burden of these policies onto the less commercial procurements). Promulgating complex rules but permitting them to be ignored is not a healthy recipe for public trust.

A businessman who bends the rules is showing flexibility, and a rule book which is highly general allows scope for individual initiative in the pursuit of profit. A civil servant who does the same is guilty of misconduct, and a rule book which allows large discretion to the official in dealings with the public is inviting arbitrariness in the treatment of different citizens. Rule keeping is not a means to the end of profit . . . but a value in itself.<sup>141</sup>

If this analogy does not ring true on first reading, substitute the word “contractors” for “citizens.” This substitution implicates citizenship at a number of different levels. Some contractors, particularly small businesses, are individual citizens. Larger contractors are owned, managed, and staffed by citizens, whose employment may depend upon certain contracts. Finally, citizens own stock in

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<sup>140</sup> Program managers or “customers” rarely appreciate the value of legislatively mandated social policies that may delay or deter their ability to obtain needed supplies or services. Steven L. Schooner, *Feature Comment – Buying the “Black Beret”: Balancing Customer ‘Needs’ and Socio-Economic Policies*, 43 GOV’T CONTRACTOR (Fed. Pubs. Inc.) ¶ 158 (April 18, 2001).

<sup>141</sup> DAVID BEETHAM, 32 BUREAUCRACY (2d ed. 1996).

companies that are affected by government purchasing decisions. In these, and other scenarios, affected citizens have reason to expect that the government will not be arbitrary in dealing with them or others similarly situated.

### **3.3. Oversight and Enforcement**

Because government procurement involves expenditure of public funds, the evolution towards more commercial purchasing implicates certain oversight and enforcement issues. Ultimately, the issue can be distilled to the simple question of how much the public is willing to pay to constrain purchaser and seller behavior, particularly avoiding fraud, waste, and abuse. Commercial firms, concerned with the bottom line, have sufficient incentives to minimize waste. Yet the model is not completely apt due to the government's obsession with maintaining the appearance of propriety in disbursing the public's tax dollars.

For example, consumers and commercial firms frequently select those with whom they do business – both in the short and long-term – based upon indefinite and even subconscious preferences and perceptions. This implies, of course, that consumers and businesses frequently *avoid*, or implicitly *discriminate* against, certain firms for both legitimate and less legitimate reasons. Conversely, the U.S. procurement system is structured to deny buyers a level of unfettered discretion that might tempt them to show favoritism or engage in corrupt behavior. “The distrust of contracting officials that is reflected in the complex and rigid rules that

now govern how competitions are conducted has ramifications that affect the acquisition process from the very beginning -- back to the point when the specifications and evaluation criteria are developed.”<sup>142</sup>

One of the most striking consequences of the U.S. procurement reforms of the 1990s was the reduction of both external and internal oversight over the process.<sup>143</sup> Although most in private industry cheered this development, others are less sanguine. “Drastically cutting oversight personnel blinds the government in its oversight of tens of billions of dollars of contracts each year. This serves only to make the government and the taxpayer highly vulnerable to exploitation by an industry with a blemished track record.”<sup>144</sup> This author worries that, as oversight of government spending has plummeted, our reformed, and surely more commercial, buying regime lacks meaningful oversight and rapidly is propagating a culture seemingly defined by lawlessness.

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<sup>142</sup> *Hearing Before the Committee on Small Business United States House of Representatives* (August 3, 1995) (Statement of Steven Kelman, Administrator for Federal Procurement Policy).

<sup>143</sup> Schooner, “Fear of Oversight,” *supra* note 119 (offering empirical data describing, and a provisional list of explanations for, the reduction in external monitoring).

<sup>144</sup> *Defense Waste and Fraud Camouflaged as Reinventing Government*, available at <<http://www.pogo.org/mici/money/camrpt.htm>> (citing Elizabeth Becker, *Big Lapses Found in Pentagon's Security-Clearance Check*, *THE NEW YORK TIMES*, August 17, 1999).

#### **4. Conclusion: Emphasis on “More Commercial” Practices: Progress and a Happy Medium**

A host of reasons justify the U.S. government’s efforts to act more like commercial businesses. Critics of the current system perceive that commercial purchasing will lead to greater efficiency in government. Reform advocates assert that commercial-style buying will strengthen the responsiveness and efficiency of the procurement system. Increased privatization and contracting out further serve the widespread desire to reduce the size of the existing government bureaucracy. Buyers, sellers, and end users (or customers) continue to express longstanding frustration with government-unique aspects of the procurement system. And, of course, there remains an ephemeral (if not chimerical) expectation that commercial purchasing will generate savings (either from better pricing or administrative efficiency).

When the government wants something that the commercial marketplace provides, it seems logical to buy commercial. Hence, there seems little debate that the government should buy commercial-off-the-shelf goods whenever possible. Yet, when the government wants to buy something that conventional consumers or businesses do not want (olive drab parachutes, blue polyester uniforms), cannot afford (space stations), or should not be entitled to possess (nuclear weapons, aircraft carriers, armored tanks, etc.), absolute reliance on the commercial marketplace seems naïve and counterproductive. The grey area, not surprisingly, falls in the middle.

If there is a lesson to be learned from the 1990's procurement reforms, it may be as simple as this: no simple, universal solution will solve the government's purchasing problems. It simply may prove impossible to maintain a *uniform* procurement system primarily defined by its size, breadth, and diversity. In the U.S., we recognize that a consumer may employ different techniques, and implicate unrelated legal regimes, when he or she obtains groceries, a new automobile, real estate or residential construction, or in-home child-care services. So too, the government must employ different techniques and, in so doing, balance competing policies. Knowing when to purchase commercial items and when to employ commercial purchasing techniques will enable the U.S. purchasing regime to become more efficient. But learning to recognize when commercial models are inappropriate will prove equally important to maintaining the public's trust in the procurement system.