



JUL 28 2004

GSA Office of the Chief Acquisition Officer

MEMORANDUM FOR RONALD POUSSARD  
DIRECTOR  
DEFENSE ACQUISITION REGULATIONS COUNCIL

FROM: *John* *Rodney P. Lantier*  
RODNEY P. LANTIER, DIRECTOR  
REGULATORY AND FEDERAL ASSISTANCE  
PUBLICATIONS DIVISION

SUBJECT: FAR Case 2004-003, Payment Withholding

Attached are comments received on the subject FAR case published at 69 FR 29838; May 25, 2004. The comment closing date was July 26, 2004.

<u>Response Number</u>	<u>Date Received</u>	<u>Comment Date</u>	<u>Commenter</u>
2004-003-1	06/10/04	06/10/04	Anthony P. DeStefano
2004-003-2	06/29/04	06/29/04	Department of Justice
2004-003-3	07/22/04	07/22/04	AIA
2004-003-4	07/23/04	07/23/04	ITAA
2004-003-5	07/26/04	07/26/04	PSC
2004-003-6	07/28/04	07/21/04	DoD/IG

Attachments

2004-003-1



**Adestefano2@aol.com**

06/10/2004 10:18 PM

To: farcase.2004-003@gsa.gov

cc:

Subject: Response to Proposed Rule

Ladies and Gentlemen:

I am most pleased to respond to your proposed rule entitled "Federal Acquisition Regulation; Payment Withholding," dated May 25, 2004 under FAR Case 2004-003.

For the record, I have over 22 years of experience in government contract accounting. I am unable to name my current employer because they may not consent to my response here. But I believe that the 5 percent withholding on time and material and labor-hour contracts is unnecessary and is not cost effective. Without detailing specific calculations used to make this determination, I believe that the administrative time spent by contractors in making, monitoring and recovering the withheld amounts, along with the time spent by government audit and administrative personnel in dealing with the withheld amounts, simply does not justify the small amount (\$50,000) withheld. The amount is not large enough to entice successful contract performance under most contracts, and clearly is not large enough to protect the government against claims arising prior to the execution of a release by contractors.

Thank you again for this opportunity to respond.

Anthony P. DeStefano, CPA, CFCM  
1200 S. Courthouse Rd.  
Suite 726  
Arlington, VA 22204  
703-979-1611

2004-003-2



"Young, John"  
<YoungJo@ojp.usdoj.gov>

06/29/2004 11:34 AM

To: farcase.2004-003@gsa.gov  
cc: "Towles, Robyn" <TowlesR@ojp.usdoj.gov>  
Subject: FAR Case 2004-003 Comment in Favor of Removing "Requirement" for CO to withhold 5% under T&M Contract

Dear FAR Secretariat:

The proposed change is reasonable and fair and should ease an administrative burden on both contracting officers, comptroller/accounting offices, and all contractors, to include small businesses. The purpose of 52.232-7, Payments under Time and Materials and Labor-Hour Contracts, is to protect the government by requiring contracting officers to withhold 5% up to a maximum of \$50,000 in the event of poor or non-performance. However, the fact is that most T&M contracts and orders are ongoing professional services requirements covering six to twelve months, often with options for another 12 or more months. Such services are almost always invoiced monthly for the previous month's services, meaning the contracting officer always has a most recent invoice against which he/she may withhold in the relatively rare instances where withholding is necessary and appropriate. Withholding small mandatory amounts monthly and then aggregating the totals and reporting on them for accounting/audit purposes is tedious and time consuming. 99% of such orders never have a performance problem significant enough to require withholding and to require it be done automatically on each invoice up to a maximum of \$50,000 is a tremendous waste of time and record keeping by procurement and accounting offices. So, while having withholding as a discretionary option where needed makes sense, making it mandatory was/is ridiculous and this change remedies the problem. You can't make this change effective fast enough, but sooner is better than later. Thank you.

John Young  
Supervisory Contract Specialist  
Department of Justice  
Office of Justice Programs

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2004-003-3



July 22, 2004

General Services Administration  
FAR Secretariat (MVA)  
800 F Street, NW, Room 4035  
ATTN: Laurie Duarte  
Washington, DC 20405.

Re: FAR Case 2004-003

Dear Ms. Duarte:

The Aerospace Industries Association (AIA) appreciates the opportunity to provide comments on the proposed rule to remove the requirement in the Federal Acquisition Regulation (FAR) that a contracting officer withhold 5 percent of the payments due under a time-and materials (T&M) or labor-hour contract, unless otherwise prescribed in the contract Schedule. The proposed rule would permit, but not require, the contracting officer to withhold payment amounts if the contracting officer determines the withholding to be necessary to protect the Government's interests.

We fully concur with the decision to extend the relaxation of this requirement from the DFARS to the FAR. This withholding requirement is administratively burdensome and results in the withholding of amounts that exceed reasonable amounts needed to protect the Government's interests. In this regard, we have identified activities (of both DoD and its contractors) that will be reduced or eliminated if withholding on T&M and labor hour contracts is optional. We estimate that the amount of cost savings on these types of DoD contracts that will occur as a result of reduction or elimination of those activities is approximately \$1.8 million annually. We do not have information on which to base an estimate of savings on other federal agency T&M and labor hour contracts, but comparable savings should occur. Another significant benefit that accrues from relaxing this requirement is not having to use current year appropriations to cover payments of previous withholds. The need to use current year funds occurs in many cases because funds earmarked to pay withheld amounts cancel before the contractor is authorized to bill the withholds.

While we are pleased that the Councils have decided that this change should also be included in the FAR, we are disappointed that the proposed changes are not consistent with the changes to relax the requirement that were included in the DFARS on December 15, 2003. The changes to the DFARS in Parts 232 and 252 stated that if it was necessary to withhold payment to protect the Government's interest, the Contracting Officer would "issue a modification requiring the contractor to withhold 5 percent of the amount due, up to a maximum of \$50,000."

003-3

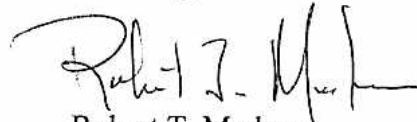
General Services Administration  
July 22, 2004  
Page 2

We believe this language was adopted by the DAR Council to be consistent with the language used by DCMA Headquarters when it issued Information Memorandum No. 03-121 (Attachment A) on January 14, 2003, providing guidance on "Fee Withholds on Cost-Reimbursement Type Contracts." While this guidance is only for DoD Contracting Officers, we think it should be applicable Government-wide because requiring withholds to protect the interests of the Government is a serious matter, necessitating, in our opinion, the execution of a formal contract modification. In the event a withhold is required, the contract modification should specify whether the withhold should be taken by the contractor or the payment office. We believe in most situations it will be more efficient and less costly for both parties if contractors take withholds prior to submission of their invoices.

To make the FAR and DFARS provisions consistent, we have lined out (see Attachment B) the proposed language in Parts 32 and 52 referencing the withholding authorization and procedures, and replaced it with the language that was added to the DFARS in the revisions that were issued in the Federal Register on December 15, 2003. We request that the Councils issue the FAR revisions as amended for the changes recommended in Attachment B.

If you have any questions or would like to meet to discuss our comments and recommendations, please contact Dick Powers of my staff. Dick can be reached on 703-358-1042. His email address is [powers@aia-aerospace.org](mailto:powers@aia-aerospace.org).

Sincerely,



Robert T. Marlow  
Vice President  
Government Division

Attachments

003-3

## Attachment A

### **Information Memorandum No. 03-121**

**Memorandum For** DCMA Districts and CMOs

**Subject:** Fee Withholds on Cost-Reimbursement Type Contracts (INFORMATION)

**Date:** January 14, 2002

**Target Audience:** Administrative Contracting Officers and Contract Administrators

### **New Information/Guidance/Tools:**

- FAR Clauses 52.216-8, Fixed Fee, 52.216-9, Fixed Fee – Construction, and 52.216-10, Incentive Fee, permit the Administrative Contracting Officer (ACO) to withhold fee if it is necessary to protect the Government's interest after payment of 85% of the fee.
- Normally, there should be no need to exercise the option of withholding fee for a contractor with a record of timely submission of final cost vouchers and certified final indirect cost proposals, and that complies with other contract terms and conditions.
- If the ACO determines that it is necessary to withhold fee to protect the Government's interests, written direction should be issued to the contractor by modification of the contract. The following paragraph provides suggested wording for the modification:
  - This modification is issued to incorporate fee withholding in accordance with FAR Clause 52.216-8 (or -9 or -10, as appropriate). In order to protect the Government's interest, [contractor] is hereby directed to begin withholding fee from billings under this contract until a reserve is set aside in the amount of \$\_\_\_\_\_ (amount of reserve shall not exceed 15% of the total fixed fee or \$100,000, whichever is less). Fee shall be released in accordance with FAR Clause 52.216-8 (or -9 or -10, as appropriate).
- In some instances contractor's are automatically withholding fee from billings, although not directed by anyone in the Government.
- ACOs should be aware that DCMA Headquarters has received queries from Industry regarding this long-standing practice and as a result of our discussions, many contractor's will stop automatically withholding fee from billings, unless directed by the ACO. Contractors may issue a letter to the ACO and Defense Contract Audit Agency alerting them of this change in fee withholding practice.
- This information should aid in the administration of fee withholds under cost-reimbursement type contracts and is applicable to One Book Chapter 9.5, Public Vouchers.

### **Point of Contact for Further Information:**

**DCMA Headquarters:** Process Manager: Ms. Felisha Hitt, DCMA-OCB

Phone: 703-428-0988, DSN 328-0988; E-Mail: [felisha.hitt@dcma.mil](mailto:felisha.hitt@dcma.mil)

**DCMAE:** Process Manager: Ms. Karen Foley, DCMAE-OCB

Phone: 617-753-3129, DSN 955-3129; E-Mail: [Karen.Foley@dcma.mil](mailto:Karen.Foley@dcma.mil)

003-3

**DCMAW:** Process Manager: Ms. Jana Weston, DCMAW-OCB  
Phone: 310-900-6526, DSN 929-6526; E-Mail: [jana.weston@dcma.mil](mailto:jana.weston@dcma.mil)  
**DCMAI:** Process Manager: Mr. Gregory Frey, DCMAI-OCB  
Phone: 703-428-1765, DSN 328-1765; E-mail: [gregory.frey@dcma.mil](mailto:gregory.frey@dcma.mil)

**Signature:**

DAVID E. RICCI, Director, Contract Business Operations

Attachment B

32.111 Contract clauses for non-commercial purchases.

(a) \* \* \*

(7) The clause at 52.232-7, Payments under Time-and-Materials and Labor-Hour Contracts, in solicitations and contracts when a time-and-materials or labor-hour contract is contemplated.

(i) If the nature of the work to be performed requires the contractor to furnish material that is regularly sold to the general public in the normal course of business by the contractor and the price is under the limitations prescribed in 16.601(b)(3), the contracting officer shall use the clause with its Alternate I.

(ii) If a labor-hour contract is contemplated, and if no specific reimbursement for materials furnished is intended, the contracting officer may use the clause with its Alternate II.

(iii) If the contracting officer determines that it is necessary to withhold payment to protect the Government's interests, paragraph (a) (2) of the clause permits the contracting officer to withhold 5 percent of the amounts due until a reserve is set aside in an amount the contracting officer considers to be necessary, but not to exceed to unilaterally issue a modification requiring the contractor to withhold 5 percent of amounts due, up to a maximum of \$50,000. unilaterally issue a modification requiring the contractor to withhold 5 percent of amounts due, up to a maximum of \$50,000. The Contracting Officer shall ensure that the modification specifies the percentage and total amount of the withhold. Normally, there should be no need to withhold payment for a contractor with a record of timely submittal of the release discharging the Government from all liabilities, obligations, and claims, as required by paragraph (f) of the clause.

\* \* \* \*

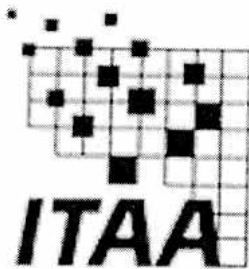
52.232-7 Payments under Time-and-Materials and Labor-Hour Contracts.

(a) \* \* \*

(2) ~~Unless otherwise prescribed in the Schedule, the Contracting Officer may withhold 5 percent of the amounts due under this paragraph (a), but the total amount withheld shall not exceed \$50,000. The amounts withheld shall be retained until the Contractor executes and delivers the release required by paragraph (f) of this clause.~~ The Contracting Officer may unilaterally issue a contract modification requiring the Contractor to withhold amounts from its billings until a reserve is set aside in an amount that the Contracting Officer considers necessary to protect the Government's interests. The Contracting Officer may withhold 5 percent of the amounts due under this paragraph (a), but the total amount withheld shall not exceed \$50,000. The amounts withheld shall be retained until the Contractor executes and delivers the release required by paragraph (f) of this clause.

\* \* \* \* \*





2004-003-4

*PRIVILEGED & CONFIDENTIAL*

July 23, 2004

Via E-mail

General Services Administration  
FAR Secretariat (MVA)  
1800 F Street, NW  
Room 4035  
Washington, DC 20405  
ATTN: Ms. Laurie Duarte

**Re: FAR Case 2004-003; Proposed Rule Removing 5 Percent  
Withholding Requirement, 69 Fed. Reg. 29838 (May 25, 2004)**

Dear Ms. Duarte:

The Information Technology Association of America (ITAA) submits these comments in response to the proposed rule recently published by the Civilian Agency Acquisition Council and the Defense Acquisition Regulations Council regarding the current 5 percent withholding requirement applicable to time-and-materials and labor-hour contracts. The proposed rule would revise the contract clause located at FAR 52.232-7 to remove the requirement that a contracting officer withhold 5 percent of the payments due under a time-and-materials or labor-hour contract. Also, the proposed rule would add FAR 32.111(a)(7)(iii) to permit contracting officers to withhold payments under time-and-materials and labor-hour contracts only when necessary to protect the Government's interests. The ITAA supports both of these proposed revisions.

The proposed revisions would remove a payment practice that has proven to be burdensome and unproductive for both the Government and contractors. Of particular significance to ITAA members, the current withholding process deprives contractors of cash flow that often is needed for on-going performance, including the payment of subcontractors and material providers. Funds are withheld even where performance is acceptable or there otherwise is no reason to believe that withholding of payment is needed to protect the Government's interests. The adverse impact of this practice is especially felt by small businesses that may find it difficult to "front" the funding of performance for the Government.

**Information Technology Association of America**

1401 Wilson Boulevard, Suite 1100, Arlington, Virginia 22209-2318 ■ Phone: (703) 522-5055 Fax: (703) 525-2279

The current withholding requirement also is inconsistent with the manner in which most service contracts are structured in the commercial market. The companies that provide these services—especially with respect to IT services—are companies that derive a vast majority of their revenues from the commercial market. Importantly, the withholding requirements compel these companies to set up processes that differ from their standard practices so that they can track and account for amounts that would otherwise be payable. The requirements also create an additional factor that should be considered when pricing work for the Government market, which can be very significant considering the thin profit margins associated with many types of services. Except in rare instances when withholding may be justified, agencies should structure payment terms to omit withholding requirements in order to benefit from the increased competition that is expected to flow from the removal of such significant non-commercial terms. We note that such an approach would also be consistent with the Federal Acquisition Streamlining Act (Sections 8002 and 8104), which requires that an agency revise, to the maximum extent practicable, its procurement policies, practices, and procedures not required by law to reduce impediments to the acquisition of commercial items.

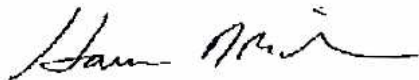
For these reasons, ITAA strongly supports the proposed rule and urges its immediate implementation.

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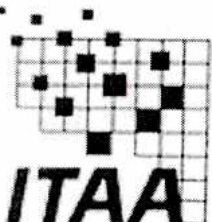
ITAA provides global public policy, business networking, and national leadership to promote the continued rapid growth of the IT industry. ITAA consists of over 400 corporate members throughout the U.S. and a global network of 50 countries' IT associations. The Association plays the leading role in issues of IT industry concern including information security, taxes and finance policy, digital intellectual property protection, telecommunications competition, workforce and education, immigration, online privacy and consumer protection, government IT procurement, human resources and e-commerce policy. ITAA members range from the smallest IT start-ups to industry leaders in the Internet, software, IT services, ASP, digital content, systems integration, telecommunications, and enterprise solution fields. For more information visit [www.ita.org](http://www.ita.org).

ITAA greatly appreciates this opportunity to provide our comments.

Respectfully submitted,



Harris N. Miller  
President



2004-003-5



PROFESSIONAL SERVICES COUNCIL

July 26, 2004

General Services Administration  
FAR Secretariat (MVA)  
Room 4035  
1800 F Street, N.W.  
Washington, D.C. 20405

Attn: Laurie Duarte

Re: FAR Case 2004-003

Dear Ms. Duarte:

The Professional Services Council (PSC) is pleased to submit comments on the FAR proposed rule published in the Federal Register on May 25, 2004 (69. F.R.29838). The rule would remove the requirement that a contracting officer must withhold five percent of the payments due under a time and materials or labor-hour contract unless otherwise prescribed in the contract schedule.

Under the current FAR rule, a contracting officer must withhold such funds, regardless of need, unless the contract provides otherwise. This proposed rule revises the Payments clause to make withholding discretionary with the contracting officer if necessary to protect the Government's interest. PSC strongly supports this rule and recommends that it be finalized as quickly as possible.

PSC is the leading national trade association representing the professional and technical services industry doing business with the Federal Government. PSC's approximately 165 member companies provide a wide range of services to all agencies of the Federal Government, from information technology to high-end consulting, engineering, scientific and environmental services.

As you may be aware, on December 15, 2003, the Defense Department issued a final rule, effective immediately, amending the DFARS to provide additional flexibility when determining the need to withhold payments under these contracts. The final DFARS rule clarifies that, normally, there should be no need to withhold payment for a contractor with a record of timely submittal of a release discharging the Government from all liabilities, obligations and claims under a contract. PSC submitted comments on that DFARS rule on May 2, 2003 and some of our comments were incorporated into the December DFARS final rule. We strongly support that final rule and recommend that this FAR rule be aligned with the DFARS rule.

More specifically, with respect to the proposed revision to FAR 32.111 (a)(7)(iii), we recommend adding after the first sentence a new sentence as follows: "The amounts withheld shall be retained until the Contractor executes and delivers the release required by paragraph (f) of the clause." This point of release is properly covered in the current 52.232-7(a)(2) clause and retained in the proposed revisions to the clause and should be addressed in the prescription.

With respect to the proposed revision to FAR 52.232-7(a)(2), we recommend adding after the first comma the phrase "if the contracting officer determines that it is necessary to withhold payment to protect the government's interest,". Adding this language brings into the clause the rationale and the flexibility for the discretionary withholding that is already provided for in the proposed 32.111(a)(7)(iii) revision.

PSC appreciates the opportunity to comment on the proposed rule. If you have any questions or need any additional information, please do not hesitate to let me know. I can be reached at (703) 875-8059 or by email at [Chvotkin@pscouncil.org](mailto:Chvotkin@pscouncil.org).

Sincerely,



Alan Chvotkin, Esq.  
Senior Vice President and Counsel



INSPECTOR GENERAL  
DEPARTMENT OF DEFENSE  
400 ARMY NAVY DRIVE  
ARLINGTON, VIRGINIA 22202-4704

2004-003-6

JUL 21 2004

Ms. Laurie Duarte  
General Services Administration  
FAR Secretariat (MVA)  
1800 F Street, NW, Room 4035  
Washington, DC 20405

Dear Ms. Duarte:

In accordance with Federal Register, Vol. 69, No. 101, May 25, 2004, we have reviewed the proposed Federal Acquisition Regulation (FAR) Case No. 2004-003, "Payment Withholding," that proposes to amend the FAR by removing the requirement that a contracting officer withhold 5 percent of the payments due under a time and materials or labor-hour contract, unless otherwise prescribed in the contract schedule.

The revised FAR Part 32, "Contract Financing," Section 32.111, and Part 52, "Solicitation Provisions and Contract Clauses," Section 52.232-7, make reference to a maximum reserve of \$50,000 that the contracting officer can withhold from payment to protect the Government. However, the proposed FAR change does not clarify whether the \$50,000 is per task order or for the entire contract.

In a prior report, OIG DoD identified this issue and recommended that the \$50,000 ceiling on withholdings be applied to each time-and-materials order, involving basic ordering agreements or indefinite delivery contracts, when orders are closed separately. Accordingly, we suggest that this issue be clarified in the current FAR change. This clarification will assist contracting officers in performing their jobs.

Thank you for the opportunity to comment on the proposed rule. If you have any questions, please contact Mr. Edward Van Why at (703) 604-8748.

Patricia A. Brannin  
Assistant Inspector General  
for Audit Policy and Oversight