Defense Department Report Questions Undefinitized Contractual Actions (UCAs)

On June 28, 2013, the Department of Defense (DoD) published its Performance of the Defense Acquisition System, 2013 Annual Report. The purpose of the annual report was to use objective data and analysis to measure macro-level performance indicators for the defense acquisition system as a whole, particularly Major Defense Acquisition Programs (MDAPs). While the annual report discussed multiple acquisition issues, one of its most significant findings related to Undefinitized Contractual Actions (UCAs), which are procurement actions entered into by the head of an agency where the contractual terms, specifications or price are not agreed upon before performance begins.

UCAs have been widely used in large development contracts for a wide range of products and services, including aircraft, missiles, tanks, ships and related components. The annual report stated that UCAs are a concern in development contracts because they correlate with increased contract costs and longer schedules. The DoD's increased focus on UCAs may result in increased scrutiny of these contracting actions in MDAP development-phase procurements.

HOW AND WHEN DOD USES UCAS

The DoD typically prefers to avoid UCAs unless there is no alternative for meeting urgent requirements. This may occur when DoD has insufficient time to negotiate a contract to meet its requirements but has an interest in entering a binding commitment with a contractor. Letter contracts and undefinitized orders issued against basic ordering agreements are primary examples of UCAs. The statute authorizing UCAs, 10 U.S.C. § 2326, requires the requesting activity to describe the anticipated effect on a military department's activities if the procurement was delayed for purposes of determining contractual terms, specifications and price before beginning performance.

The statute also precludes a contracting officer from entering into a UCA unless it provides that the missing terms will be settled within 180 days of the start of performance or the obligation of more than 50 percent of the ceiling price of the action. Notably, the limitations can be waived for contingency or humanitarian operation contracts. In addition, the following contracts are also exempt: foreign military sales, simplified acquisitions, special access programs, and congressionally mandated long-lead procurement contracts. Regulations implementing the statute are found at DFARS Subpart 217.74. DoD guidance also requires the contracting officer to identify the risk of using an UCA and the means by which the government will mitigate the associated risk because of missing contract terms.

THE COST AND TIME EFFECT OF UCAS

The annual report's analysis of historical data found that DoD's entry into a UCA, at any time during a development contract, correlated to a more than seven percent increase in contract cost growth, measured across all DoD contracts from 1970-2011. The effect was most pronounced on DoD ship-development contracts, where the annual report found a 41 percent higher cost growth with UCAs, compared to contracts without UCAs. The Navy used UCAs at a rate of 39 percent of MDAP contracts from 1970 through 2011. The annual report found no statistically significant effect of UCAs on contracts for aircraft, missile, munitions or space systems development contracts. Throughout all DoD development contracts, however, the annual report found that UCAs increased development cycle time by increasing schedule growth, generally by "0.3 years or longer."

The annual report found that UCAs did not correlate with total cost growth in early production contracts, as it did with development contracts. In its concluding comments, under the heading "Intelligent acquisition is key," the annual report stated that "UCAs can be successfully employed in early production but are concerns for development work."

IMPLICATIONS OF ANNUAL REPORT FINDINGS ON DOD CONTRACTS

The annual report comes after several years of increased scrutiny, regulation and reporting requirements regarding UCAs. The U.S. Government Accountability Office has expressed concern that UCAs pose risks to the taxpayer because contractors reportedly lack incentives to control costs while contract terms and conditions are negotiated and definitized (i.e., agreement is reached on contract terms, specifications and price). GAO also noted that the government faces increased risk of incurring unnecessary costs if requirements change prior to definitization.

Similarly, a report by the DoD Inspector General found that contracting officers were: inconsistently complying with the UCA statute and regulation by, for example, failing to timely definitize UCAs; and inconsistently documenting profit determinations because of the possible reduced cost risk to the contractor.
The annual report provides a relatively high-level critique of UCAs and their effect on contract costs. Its findings, however, may motivate the DoD to scrutinize UCAs more aggressively pursuant to DoD cost-cutting initiatives such as the Better Buying Power directives. It also may promote additional auditing and compliance review of UCAs, particularly in development-phase contracts.

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