DEPARTMENT OF DEFENSE

Defense Acquisition Regulations System

48 CFR Parts 231 and 242

[Docket DARS–2015–0070]

RIN 0750–AI81

Defense Federal Acquisition Regulation Supplement: Enhancing the Effectiveness of Independent Research and Development (DFARS Case 2016–D002)

AGENCY: Defense Acquisition Regulations System, Department of Defense (DoD).

ACTION: Final rule.

SUMMARY: DoD is issuing a final rule amending the Defense Federal Acquisition Regulation Supplement (DFARS) to improve the effectiveness of independent research and development (IR&D) investments by the defense industrial base, by requiring contractors to engage in technical interchanges with DoD before costs are generated.

DATES: Effective November 4, 2016.

FOR FURTHER INFORMATION CONTACT: Mr. Tom Ruckdaschel, telephone 571–372–6088.

SUPPLEMENTARY INFORMATION:

I. Background

DoD published a proposed rule in the **Federal Register** at 81 FR 7723 on February 16, 2016, to revise DFARS 231.205–18, Independent Research and Development and Bid and Proposal Costs, to require that proposed new IR&D efforts be communicated to appropriate DoD personnel prior to the initiation of these investments, and that results be shared with appropriate DoD personnel. Nine respondents submitted public comments in response to the proposed rule.

II. Discussion and Analysis

DoD reviewed the public comments in the development of this final rule. A discussion of the comments and the changes made to the rule as a result of those comments is provided, as follows:

A. Summary of Changes From the Proposed Rule in Response to Public Comments

1. The requirement at DFARS 231.205–18(c)(iii)(C)(*2*) to include a ''summary of results'' with the annual update to online inputs is removed in the final rule.

2. DFARS 231.205–18(c)(iii)(C)(*4*)(*i*) is revised to cite the Office of the Assistant Secretary of Defense for Research and Engineering (OASD R&E) as a resource for contractors who do not have a point of contact for the technical interchange. Contact information for OASD R&E can be found at *http://www.acq.osd.mil/rd/contacts/.*

B. Analysis of Public Comments

1. Support for the Rule

Comment: Three respondents expressed positive support of the rule and DoD's effort to enhance communications between industry and DoD regarding IR&D efforts.

Response: DoD acknowledges the respondents' support for the rule.

2. Favor Certain Projects/Different Priorities

Comment: One respondent, though generally supportive of the goals of the rulemaking effort, believed the proposed rule will make it more difficult to pursue IR&D projects at their infancy for the following reason: ''. . . by requiring technical interchange with Government employees before generating IR&D costs, defense contractors will shift toward IR&D projects that are of perceived interest to identifiable DoD officials.'' One respondent stated that the rule will favor companies that have their IR&D (efforts) preapproved. One respondent, though supportive of technical interchanges, was concerned that DoD individuals participating in the interchanges may not share the long-term priorities outlined in Better Buying Power 3.0. Another respondent is concerned that ''bona fide'' technical interchanges exist outside of the contractor's controls and that the proposed rule penalizes contractors without an ''ARDEC like'' agency as their customer.

Response: DoD anticipates that defense contractors will pursue IR&D projects intended to advance their ability to develop and deliver a superior and more competitive product to the warfighter. The requirement to hold a technical interchange is not a de facto approval process and will not favor one company over another. These technical interchanges are informal engagements designed to promote transparency, communication, and dialogue between IR&D participants and DoD. The intended outcome is to ensure that both IR&D performers and their potential DoD customers have sufficient awareness of each other's efforts and to provide industry with some feedback on the relevance of proposed and completed IR&D work. Consistent with that objective, the rule requires only that a technical interchange take place and that the date of the interchange and name of the DoD personnel contacted be reported to the defense innovation marketplace.

3. Existing Regulations and Practices

Comment: One respondent stated that the rule is not necessary and that the current text at DFARS 231.205–18 is sufficient. Another respondent questioned the proposed rule's statement that ''there are no known significant approaches to the rule that would meet the requirements'' when agencies are already successfully holding voluntary technical interchanges that are achieving the regulation's goals.

Response: The existing language at DFARS 231.205–18 does not include a requirement for technical interchanges. These technical interchanges are key to ensuring that both IR&D performers and their potential DoD customers have sufficient awareness of each other's effort. The fact that voluntary technical interchanges already exist, and are successfully achieving the regulation's goals, is consistent with the overall approach to the rulemaking effort.

4. Adverse Impact on Innovation

Comment: Several respondents stated that the proposed rule will adversely impact innovative ideas. Another respondent cautioned that the rule will create a barrier to innovation and entry to the marketplace.

Response: DoD believes that this rule supports and promotes innovative ideas and technologies, and will incentivize entry into the marketplace by ensuring that IR&D performers and their potential DoD customers have sufficient awareness of each other's efforts and that DoD can provide industry with feedback on the relevance of proposed and completed IR&D work.

5. Cost/Administrative Burden

Comment: A number of respondents stated that the rule will cost taxpayers more. One respondent stated that the rule will impose an administrative burden on contractors, administrative contracting officers (ACOs), and DoD personnel. Another respondent expressed concern with the significant costs associated with planning and conducting technical interchanges and the costs accrued prior to the technical interchange.

Response: While acknowledging that this rule imposes a slight administrative burden on contractors, ACOs, and DoD personnel, such burdens are overshadowed by the net benefit of ensuring that IR&D performers and their potential DoD customers have sufficient awareness of each other's efforts and

that DoD can provide industry with feedback on the relevance of proposed and completed IR&D work. Moreover, the long-term priorities outlined in Better Buying Power 3.0 are a strategic imperative for DoD.

6. Process Issues and Practicality

Comment: A number of respondents stated that the rule will create an unnecessary bureaucracy, citing concerns that the rule will create a ''bottleneck'' that will slow down industry IR&D efforts and require the shifting of DoD technical resources to evaluate the IR&D projects and respond to contractors. The respondents claimed that the requirement to conduct and document the interchange of information between contractor and DoD personnel with respect to IR&D projects prior to their commencement is not practical.

Response: The rule does not establish a requirement for DoD to evaluate or approve IR&D projects; rather, the rule requires contractors to communicate new IR&D efforts to appropriate DoD personnel via a technical interchange prior to the initiation of the investment. The requirement for technical interchanges is an extension of DoD's long-standing policy to engage in robust communication with all entities supporting the defense industrial base and promote transparent engagement with IR&D participants regarding research and development, including basic research, applied research, and development. This policy is outlined in DoD Instruction 3204.01, ''DoD Policy for Oversight of Independent Research and Development (IR&D).'' The technical interchanges are intended to be informal communications between IR&D participants and DoD. Their objective is to ensure that both IR&D performers and their potential DoD customers have sufficient awareness of each other's efforts and to provide industry with some feedback on the relevance of proposed and completed IR&D work. Note, the requirement for including a summary of results in the annual update on IR&D projects is removed in the final rule, thus easing any administrative burden.

7. Statutory Concerns

Comment: A number of respondents stated that the rule is in violation of existing statute and recreates the historic DoD technical reviews rejected by Congress.

Response: This rule is consistent with 10 U.S.C 2372 subsection (a), Regulations, which states that the Secretary of Defense shall prescribe regulations governing the payment, by the Department of Defense, of expenses incurred by contractors for independent research and development and bid and proposal (B&P) costs. To that extent, subsection (c), Additional Controls, states that the regulations prescribed pursuant to subsection (a) may include implementation of regular methods for transmission from contractors to the Department of Defense, in a reasonable manner, of information regarding progress by the contractor on the contractor's independent research and development programs.

8. DoD Responsiveness

Comment: A number of respondents expressed concern with DoD responsiveness to requests for technical interchanges, citing that the rule fails to outline DoD's obligations and unfairly saddles contractors with the full consequence of DoD's failure to take part in a technical interchange. One respondent is concerned that the proposed rule creates practical, time, resource, and data disclosure challenges for conducting technical interchanges, and that DoD Components will not have an adequate number of personnel designated to conduct the technical interchanges in the time mandated. Another respondent questioned the recourse contractors will have if DoD personnel refuse to engage.

Response: To assist contractors in ensuring that technical interchanges take place in a timely manner, the rule has been revised to identify the primary DoD focal point for technical interchanges as OASD R&E. Contact information for this office is available at *http://www.acq.osd.mil/rd/contacts/.* If a Contractor experiences difficulties scheduling a technical interchange, or does not have a point of contact for the technical interchange, the contractor may contact OASD R&E.

9. Protection of Data

Comment: Several respondents were concerned about reporting and protection of proprietary and classified information.

Response: This rule merely requires reporting of the name of the technical or operational DoD Government employee and the date of the technical interchange. The requirement to include a summary of results of the technical interchange in the annual update is removed in the final rule. There is an existing requirement at DFARS 231.205–18(c)(iii)(C) for submission of project summaries and annual updates to the DTIC Web site. It remains DoD policy to protect proprietary information in accordance with applicable laws and agency regulations. Firms have discretion regarding presentation of information they regard as sensitive when they submit project summaries; however, only unclassified IR&D project summary information should be provided. Both database screens and printouts will be marked ''Proprietary.'' Any markings on attachments provided by a contractor will not be altered.

Adequate controls are in place to protect information from compromise. It is DoD policy to protect national security information in accordance with national-level policy issuances. In accordance with DoD Instruction 5200.01, DoD Information Security Program and Protection of Sensitive Compartmented Information, DoD shall—

- Identify and protect national security information and controlled unclassified information (CUI) in accordance with national level policy issuances.
- Promote information sharing, facilitate judicious use of resources, and simplify management through implementation of uniform and standardized processes.
- Protect CUI from unauthorized disclosure by appropriately marking, safeguarding, disseminating, and destroying such information.

10. Additional Information

Comment: One respondent stated that DFARS language should be added stating that the Government may require additional information from the contractor.

Response: The objective of the technical interchanges is to ensure that both IR&D performers and their potential DoD customers have sufficient awareness of each other's efforts and to provide industry with some feedback on the relevance of proposed and completed IR&D work. Within that framework, the DoD personnel involved in technical interchanges will not be seeking additional information, *i.e.,* formal documentation from the contractor.

11. Reporting Burden

Comment: One respondent stated that the proposed rule inaccurately suggests that it does not require changes to reporting or recordkeeping. Another respondent stated that the rule adds to the contractor's existing reporting burden.

Response: As stated in the proposed rule, the impact of this rule on a contractor's reporting burden is negligible. Currently, contractors are required to (1) report IR&D projects to the Defense Technical Information

Center (DTIC) using the DTIC's online IR&D database and (2) update these inputs at least annually and when the project is completed. This rule merely changes the web address for submission of this report and requires major contractors to include in the report the name of the Government employee with which a technical interchange was held prior to initiation of the IR&D effort and the date of such interchange. In addition, the requirement to include a summary of results in the annual update on IR&D projects is removed in the final rule.

12. DoD Government Employee

Comment: One respondent stated that the rule does not specify the needed level of detail for the technical interchange or ''who'' in DoD should receive the technical information. Another respondent is concerned that the proposed rule does not adequately define the term ''DoD Government employee.''

Response: In accordance with the rule, contractors shall engage in technical interchanges with a technical or operational DoD Government employee who is informed of related ongoing and future potential interest opportunities. If the contractor does not have a point of contact for the technical interchange, the contractor may contact OASD R&E. Contact information for OASD R&E can be found at *http://www.acq.osd.mil/rd/contacts/.*

13. Advance Approval Requirement

Comment: One respondent recommended eliminating the DoD advance approval requirement of contractor's IR&D efforts.

Response: The rule does not contain a requirement for DoD to approve a contractor's IR&D efforts in advance.

14. Administrative Guidance/Standards for Technical Interchanges

Comment: One respondent asked if DoD will write additional administrative rules to outline DoD's obligation to participate in technical interchanges. Another respondent suggested that DoD adopt administrative rules, best practices, and guidance to counter the inconsistent support among DoD agencies and provide uniformity to the technical interchange process.

Response: The rule is intentionally crafted to allow informal technical interchanges to ensure that IR&D performers and their potential DoD customers have sufficient awareness of each other's efforts and that DoD can provide industry with feedback on the relevance of proposed and completed IR&D work.

15. Cost Allowability

Comment: One respondent recommended DoD reconsider the prerequisite for a determination of allowability. Another recommended the rule include a proviso allowing costs expended before the effective date of the final rule. One respondent states that DoD should not make allowability of IR&D costs contingent on the timing of technical exchange meetings. One respondent was concerned that the proposed rule restricts the allowability of costs related to mandatory technical interchanges; specifically, the proposed rule states that the contractor must engage in a technical interchange ''before IR&D costs are generated.'' Another respondent was concerned of the lack of specificity regarding verification for purposes of allowability determinations.

Response: The requirement to determine the allowability of IR&D costs is a preestablished requirement in DFARS 231.205–18(c)(iii)(C), which sets forth the requirement that for a contractor's annual IR&D costs to be allowable, the IR&D projects generating the costs must be reported to DTIC using the DTIC's online input form. This rule merely adds the requirement that contractors also engage in a technical interchange with a technical or operational DoD Government employee, and record the name of the employee and the date the technical interchange occurred using DTIC's online form. The rule applies to IR&D projects initiated in the contractor's fiscal year 2017 and later. However, as with all DFARS rules, unless otherwise stated, the rule is only effective upon publication. Therefore, IR&D costs incurred prior to the effective date of this rule are not subject to the requirements of this rule.

16. Dollar Threshold

Comment: Two respondents suggested DoD establish a dollar threshold for requiring technical interchanges.

Response: The requirements of this rule only apply to major contractors. Establishing an IR&D project dollar threshold would require speculative estimate of the IR&D project costs and, as such, would be impossible to administer, thus defeating the purpose of the technical interchange.

17. Cost Bases and Pools

Comment: Two respondents stated that the rule will require contractors to establish multiple accounting costs bases and pools.

Response: This rule does not impose new cost accounting requirements. The IR&D cost principle at Federal Acquisition Regulation (FAR) 31.205–18(b) states, ''The requirements of 48 CFR 9904.420, Accounting for independent research and development costs and B&P costs, are incorporated in their entirety. . . .'' The cost accounting standard at 48 CFR 9904.420–40, Fundamental requirement, paragraph (a) states, ''The basic unit for identification and accumulation of IR&D and B&P costs shall be the individual IR&D or B&P project.''

18. Annual Briefings/Frequency

Comment: A number of respondents questioned the frequency of the technical interchanges and whether they will be required annually. One respondent stated that many IR&D projects span several years, changing and evolving through the process, and that it is not clear whether these projects would need to be stopped and briefed annually. One respondent noted that one of the benefits of contractor IR&D is the ability to rapidly change direction as result of discovery or in response to a shifting market or defense environment.

Response: There is no requirement to brief IR&D projects annually. The rule requires the technical interchange to occur at the onset of the IR&D project, prior to generating any costs, for the annual IR&D costs to be considered allowable.

C. Other Changes

This final rule includes the following technical amendments:

1. The proposed paragraph regarding contractors that do not meet the threshold of major contractor is renumbered as DFARS 231.205–18(c)(iv) in the final rule.

2. At DFARS 242.771–3, the entity responsible for a regular method for communication is changed from the ''Director, Defense Research and Engineering (USD(A&T)DDR&E)'' to the ''Office of the Assistant Secretary of Defense for Research and Engineering (OASD R&E).''

III. Applicability to Contracts at or Below the Simplified Acquisition Threshold and for Commercial Items, Including Commercially Available Off-the-Shelf Items

This rule does not add any new provisions or clauses or impact any existing provisions or clauses.

IV. Executive Orders 12866 and 13563

Executive Orders (E.O.s) 12866 and 13563 direct agencies to assess all costs and benefits of available regulatory alternatives and, if regulation is necessary, to select regulatory approaches that maximize net benefits

(including potential economic, environmental, public health and safety effects, distributive impacts, and equity). E.O. 13563 emphasizes the importance of quantifying both costs and benefits, of reducing costs, of harmonizing rules, and of promoting flexibility. This is not a significant regulatory action and, therefore, was not subject to review under section 6(b) of E.O. 12866, Regulatory Planning and Review, dated September 30, 1993. This rule is not a major rule under 5 U.S.C. 804.

V. Regulatory Flexibility Act

A final regulatory flexibility analysis has been prepared consistent with the Regulatory Flexibility Act, 5 U.S.C. 601, *et seq.,* and is summarized as follows:

The objective of this final rule is to (1) ensure that both independent research and development (IR&D) performers and their potential DoD customers have sufficient awareness of each other's efforts and (2) provide industry with feedback on the relevance of proposed and completed IR&D work.

There were no significant issues raised by the public in response to the initial regulatory flexibility analysis.

DoD does not expect this final rule to have a significant economic impact on a substantial number of small entities, because DFARS 231.205–18(c)(iii) applies only to major contractors, which are defined as those whose covered segments allocated a total of more than $11 million in IR&D and bid and proposal costs to covered contracts during the preceding fiscal year. The final rule requires major contractors to communicate proposed new IR&D efforts to DoD personnel in a technical interchange prior to the initiation of such investments.

This rule impacts existing reporting and recordkeeping requirements in a very minor way. Only one element is being added to the existing reporting requirement to require major contractors to include the name of the DoD employee with which a technical interchange was held and the date of such interchange.

There are no known significant alternatives to the rule. The rule impacts major contractors and, as such, will have minimal impact on small entities.

VI. Paperwork Reduction Act

The final rule affects the information collection requirements at Defense Federal Acquisition Regulation Supplement (DFARS) 231.205–18, currently approved under the Office of Management and Budget (OMB) Control Number 0704–0483, entitled ''Independent Research and Development Technical Descriptions,'' in accordance with the Paperwork Reduction Act (44 U.S.C. chapter 35); however, the impact of this rule is negligible. Currently, contractors are required to (1) report IR&D projects to DTIC using the DTIC's online IR&D database and (2) update these inputs at least annually and when the project is completed. This rule merely changes the web address for submission of this report and requires major contractors to include in the report the name of the DoD Government employee with which a technical interchange was held and the date of such interchange.

List of Subjects in 48 CFR Parts 231 and 242

Government procurement.

Jennifer L. Hawes,

Editor, Defense Acquisition Regulations System.

Therefore, 48 CFR parts 231 and 242 are amended as follows:

■ 1. The authority citation for 48 CFR parts 231 and 242 continues to read as follows:

Authority: 41 U.S.C. 1303 and 48 CFR chapter 1.

PART 231—CONTRACT COST PRINCIPLES AND PROCEDURES

■ 2. Amend section 231.205–18 by—

■ a. Revising paragraph (c)(iii)(C);

■ b. Redesignating paragraphs (c)(iv) and (v) as paragraphs (c)(v) and (vi), respectively; and

■ c. Adding a new paragraph (c)(iv).

The revision and addition read as follows:

231.205–18 Independent research and development and bid and proposal costs.

* * * * *

(c) * * *

(iii) * * *

(C) For annual IR&D costs to be allowable—

(*1*) The IR&D projects generating the costs must be reported to the Defense Technical Information Center (DTIC) using the DTIC's online input form and instructions at *http://www.defenseinnovationmarketplace.mil/;*

(*2*) The inputs must be updated at least annually and when the project is completed;

(*3*) Copies of the input and updates must be made available for review by the cognizant administrative contracting officer (ACO) and the cognizant Defense Contract Audit Agency auditor to support the allowability of the costs; and

(*4*) For IR&D projects initiated in the contractor's fiscal year 2017 and later, as a prerequisite for the subsequent determination of allowability, the contractor shall—

(*i*) Engage in a technical interchange with a technical or operational DoD Government employee before IR&D costs are generated so that contractor plans and goals for IR&D projects benefit from the awareness of and feedback by a DoD Government employee who is informed of related ongoing and future potential interest opportunities. If the contractor does not have a point of contact for the technical interchange, the contractor may contact the Office of the Assistant Secretary of Defense for Research and Engineering (OASD R&E). Contact information for OASD R&E can be found at *http://www.acq.osd.mil/rd/contacts/;* and

(*ii*) Use the online input form for IR&D projects reported to DTIC to document the technical interchange, which includes the name of the DoD Government employee and the date the technical interchange occurred.

(iv) Contractors not meeting the threshold of a major contractor are encouraged to use the DTIC online input form to report IR&D projects to provide DoD with visibility into the technical content of the contractors' IR&D activities.

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PART 242—CONTRACT ADMINISTRATION AND AUDIT SERVICES

242.771–3 [Amended]

■ 3. In section 242.771–3, amend paragraph (d) introductory text by removing ''Director, Defense Research and Engineering (OUSD(AT&L)DDR&E)'' and adding ''Office of the Assistant Secretary of Defense for Research and Engineering (OASD R&E)'' in its place.

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DEPARTMENT OF DEFENSE

Defense Acquisition Regulations System

48 CFR Part 247

[Docket DARS–2016–0036]

RIN 0750–AJ09

Defense Federal Acquisition Regulation Supplement: Contiguous United States (DFARS Case 2016–D005)

AGENCY: Defense Acquisition Regulations System, Department of Defense (DoD).