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IN REPLY REFER TO MMPPP/ (DSN 427-1360)
PROCLTR 96-13

MEMORANDUM FOR PROCLTR DISTRIBUTION LIST

SUBJECT: Using Indefinite Quantity Contracts in the Reengineered Business Process Environment

The purpose of this PROCLTR is to examine contracting arrangements that will provide maximum flexibility to support our customers in the current business environment and in the reengineered logistics environment of the future. The implementation in FAR 16.504 of the FASA preference for making multiple awards of task and delivery order, indefinite-quantity contracts (IQCs) "to the maximum extent practicable," allows for post-award competition among two or more sources for the same or similar supplies or services (hereafter referred to as "items"), thereby providing customers enhanced ordering flexibility and choice. This statutory preference facilitates implementation by DLA of similar flexible ordering arrangements, including electronic commercial catalogs and electronic commerce mall, and virtual prime vendor, which are expected to enable DLA to realize its strategic goals of "faster, cheaper, better." These business arrangements will provide customers a choice among a wide range of items and sources for obtaining them, including prime vendors; depot stock; contracts with distributors, manufacturers and OEMs; on-demand manufacturing; and commercial catalogs, through which customers may browse, compare prices and features, and place orders directly with participating trading partners. DLA will become a value-added broker, negotiating leveraged, flexible prices and delivery terms with individual vendors. Such choices and services will soon become the lynchpin of DLA's procurement process, providing enhanced support to our customers and attracting new customers.

Everything we do, including the types of contracts we establish, should further the vision of DLA as the provider of choice in times of war, peace, and national emergencies. The IQC is the preferred contract type because it best promotes the agency's procurement objectives of providing optimum long-term ordering flexibility and customer choice in price, quality, and delivery. IQCs can be a tactical tool for leveraging our procurement resources. Generally, because they allow customers to choose among many different suppliers to find the item that best meets their needs, IQCs can incentivize vendors who are eager to participate, to offer better contract prices, delivery terms, and product quality. Further, IQCs facilitate more creative customer support arrangements, such as multiple IQC awards, corporate contracts for competitive items, and prime vendor access to DLA procurement instruments and supply sources. Establishing IQC arrangements now will facilitate loading the electronic shopping mall of the future with alternative sources, and ensure that we will continue to provide enhanced support to our customers.

This PROCLTR highlights the advantages of IQCs by focusing on those features which make IQCs more suitable contract vehicles than requirements type contracts (RTCs) in a reengineered logistics environment, namely, ordering flexibility and enhanced customer support, which IQCs provide in several ways:

a. The requirement to establish a guaranteed contract minimum in IQCs need not reduce the flexibility otherwise provided by this contract type, nor apply undue risk on contracting activities. Since the Government is not obligated to fund or purchase more than the stated minimum(s), there is no risk of breaching the contract if customers turn to other vendors and methods of supply to satisfy their needs, provided that **the** minimum is satisfied at some point during the contract term. The RTC does not provide similar long-term ordering flexibility and limits customer choice because it obligates the Government to obtain all requirements from the contract holder during the term of the contract. The IQC minimum must only be an amount sufficient to bind the parties to the terms of the contract; for example, a $1,000 minimum may be considered sufficient to establish a contract. We believe the risk is minimal for DBOF fund users, and it is an investment the agency is willing to make to obtain the potential benefits IQCs provide. Historically, IQC minimums represented a percentage of the maximum amount, an economic order quantity, and/or requirements on hand, which were satisfied through placement of the first delivery order at the same time the contract was awarded. However, the minimum need only be contractually sufficient, and does not have to be ordered at the time ofcontract award.

b. The IQC maximum represents a not-to-exceed contract ceiling, unlike the estimate in an RTC which can be exceeded during the contract term if additional requirements materialize; however, **this** need not **detract from** the suitability of the IQC as a long-term procurement instrument. **As we** change business practices and provide customers a choice among many ordering instruments, historic demand patterns are likely to shift, and it may prove even more difficult to anticipate with any certainty what customer demands are **likely** to be during the contract term. To reduce the likelihood of underestimating potential needs, contracting officers should provide for fluctuations in demand and for a reasonable amount of unanticipated requirements that may result from reengineering our business processes, by setting higher maximums than might otherwise be established relying solely on the best available current and historical data. (Of course, rationale for any departure from historical usage levels should be explained in the solicitation). Further, it **is** prudent to provide **ordering flexibility, and request *separate* pricing** for, **an estimated quantity, or,** when **the** range between the minimum and maximum is broad, more than one estimated quantity level or range. This is a frequently used commercial practice which provides for reduced cost risk to offerors and to our customers by allowing for the tailoring of prices for different order quantities. In this way, the IQC maximum provides as much ordering capacity as can reasonably be supported without appearing inflated.

c. IQCs can provide long-term ordering flexibility in additional ways, too, such as by providing multiple sources for contract items. Establishing different quantity limitations tailored to the capabilities of **different suppliers in** IQCs **awarded under the same solicitation also provides flexibility. This is most likely to** occur, for example, when awarding different product lines for generic requirements, awarding items solicited based on the production capacities or historic demand patterns among participating vendors, or awarding different items or destinations under solicitations with multiple line items.

d. Using evaluated options in conjunction with the basic contract is another administrative time saver and a flexible means of satisfying additional requirements not available under the basic contract. Both horizontal options which extend the term of the contract, and vertical options which provide additional quantities, may be used in IQCs, singly or in conjunction with each other, to provide greater long-term flexibility. Generally, there is no limit on the number of vertical options that may be included in a contract (but see **FAR** 17.203(g) **for** special circumstances affecting quantities available under vertical options).

e. There is considerable flexibility in establishing quantities and pricing arrangements to be included in an IQC. Quantities may be expressed as an amount of dollars or items **(DLAR** 16.504). While the **FAR** requires only that an IQC contain a stated minimum and maximum, contracting officers may choose to establish such limitations for each item or for the contract as a whole. In contracts for multiple items, for example, **such** as automated data processing equipment or medical x-ray systems with individual components and accessories, where it **is** difficult to anticipate how many of each individual component may be ordered, the Government may establish overall contract limitations rather than risking assigning amounts arbitrarily to each item. Some DLA contracting activities typically include a guaranteed minimum: an estimated quantity, which represents the

Government's best estimate of anticipated requirements during a specified contract period; and a maximum quantity, which is the contract ceiling. In some instances, activities may choose to include several ranges of quantity estimates and corresponding weighting factors representing the estimated probability, for each estimate, that the amount of orders will fall within that range. Available case law affirms our interpretation that estimates need not be exact projections, but should be realistic and established in good faith, based on the best historical and current information available.

f. There is no standard formula for evaluating IQC prices, provided that, in each case, there is some common basis for evaluating offers received (such as comparing discounts offered from catalog prices, comparing individual item prices, or comparing prices for overall quantity limitations); prices are evaluated for reasonableness up to the stated maximum at time of contract award; and evaluations include all quantities or quantity levels/ranges solicited, not just either the contract minimum or the maximum. Offers which include prices for the guaranteed minimum only shall be rejected. The selection of an evaluation method may depend on how effectively and/or precisely the Government is able to project its anticipated requirements and represent those amounts in the contract schedule. It also is affected by whether the Government seeks to include reduced prices or across-the-board discounts for volume orders. The Government may choose to request prices based on item estimates and/or an overall estimate of the total contract amount. Alternatively, the Government may choose to request prices for one or several estimated quantities or quantity levels/ranges (e.g., based on the most recent historical purchase data available for a representative period for all contract items solicited, or on a representative sample of past purchases for individual items, adjusted, as appropriate, to reflect anticipated demand or unforeseen requirements). The use of multiple ranges and corresponding probability factors, as discussed in the previous paragraph, provides vendors with more precise information about anticipated requirements, and, when used for price evaluation in source selection, facilitates more accurate pricing. As we continue to adopt procurement processes that parallel the best commercial practices, more creative pricing and evaluation methodologies may be developed.

In summary, establishing quantity estimates and limitations is a risk management decision; the more specific the information provided in the solicitation, and the more it provides for multiple price ranges or quantity discounts, the less risk to all parties to the contract, and the more likely that the parties will be able to negotiate the most favorable pricing and delivery terms (DLAR 16.504). While establishing IQC estimates and limitations does entail a degree of risk, similar risk is inherent in any contract, including an RTC, when it is difficult to predict with certainty the amount that will be ordered. This uncertainty may occur more often in the reengineered business environment, for example, with first time requirements where there is no prior usage history, when the contracting officer has limited knowledge about the vendor and/or customer base, or when requirements are awarded to multiple sources. When contract quantities are uncertain, the Government may have to rely more on the experience and knowledge of its vendor base in establishing quantity estimates and limitations that are both realistic and binding.

This PROCLTR is effective immediately and supersedes the coverage in this area contained in the DLA Long-Term Contracting Handbook, DLAH 4105.2 (July 1989). It expires upon incorporation of its contents into the DLAR, but no later than one year from the issue date. The POC is Ms. Ynette Shelkin, who can be reached by phone at (703) 767-1356 (DSN 427-1356), by facsimile at (703) 767-1359, or by e-mail at ynette_shelkin@hq.dla.mil.

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