



EXECUTIVE OFFICE OF THE PRESIDENT  
OFFICE OF MANAGEMENT AND BUDGET  
WASHINGTON, D. C. 20503

March 16, 2016

MEMORANDUM FOR THE HEADS OF EXECUTIVE DEPARTMENTS AND AGENCIES

FROM: Anne E. Rung  
Administrator  
Office of Federal Procurement Policy

SUBJECT: Determination of the Statutory Formula Benchmark Compensation Amount for Fiscal Years 2013 and 2014 for Certain Executives and Contractor Employees, Pursuant to Section 39 of the Office of Federal Procurement Policy Act, as amended (41 U.S.C. § 1127)

This memorandum sets forth the benchmark compensation amount for certain employees of Federal Government contractors as required by Section 39 of the Office of Federal Procurement Policy (OFPP) Act, as amended (41 U.S.C. § 1127, otherwise known as the statutory formula cap) for the cost allowability purposes of section 4304(a)(16) of title 41 and section 2324(e)(1)(P) of title 10 for covered contracts awarded before June 24, 2014. For covered contracts awarded on or after June 24, 2014, a new cap applies pursuant to section 702 of the Bipartisan Budget Act of 2013 (BBA), Pub. L. 113-67, December 26, 2013.

For contracts awarded prior to June 24, 2014, section 1127 limits the reimbursement or allowability of compensation costs under Federal Government contracts as implemented at Federal Acquisition Regulation (FAR) 31.205-6(p). In less technical terms, the statutory formula cap places a ceiling on the total annual compensation costs the Federal Government will reimburse a contractor for the compensation package the contractor provides to certain of its employees for work done pursuant to certain Federal Government covered contracts. This statutory formula cap applies to limit the reimbursement of the compensation costs of certain contractor senior executives on covered contracts with civilian and defense agencies. Additionally, as a result of changes made by section 803 of the National Defense Authorization Act for FY 2012, Pub. L. 112-81, December 31, 2011, for covered contracts with defense agencies (i.e., DOD, NASA and Coast Guard), the statutory formula cap was expanded to cover all other contractor employees and applies to the compensation costs incurred after December 31, 2011. With both civilian and defense agencies, the statutory formula cap applies only when the contractor is performing covered contracts that are of either a cost-reimbursable nature or other cost-based nature.

Section 1127 sets out a formula for determining the cap amount. Specifically, the statutory formula cap amount is set at the median (50<sup>th</sup> percentile) amount of compensation provided, over the most recent year for which data is available, to the five most highly compensated employees in management positions at each home office and each segment of all publicly-owned U.S. companies with annual sales over \$50 million. The determination is based on analysis of data

made available by the Securities and Exchange Commission. Compensation means the total amount of wages, salaries, bonuses, restricted stock, deferred and performance incentive compensation, and other compensation for the year, whether paid, earned, or otherwise accruing, as recorded in the employer's cost accounting records for the year.

Since enactment of the statutory formula in 1998, the cap has increased more than 300%. In 2010, the President began calling on Congress to replace the current statutory formula cap with a lower, more sensible limit that is on par with what the Government pays its own executives and employees. In December 2013, with the Administration's strong support, Congress reformed the ceiling on the reimbursement of contractor employee compensation. Section 702 of the BBA replaced section 1127 with a new cap of \$487,000 to be adjusted annually to reflect the change in the Employment Cost Index for all workers as calculated by the Bureau of Labor Statistics (otherwise known as the BBA cap). The new \$487,000 BBA cap provides a reasonable level of compensation for high value Federal contractor employees while ensuring taxpayers are not saddled with paying excessive compensation costs. On June 24, 2014, the Federal Acquisition Regulatory Council issued an interim rule to amend the Federal Acquisition Regulation to reflect the new BBA cap and issuance of a final rule is pending. However, the new \$487,000 BBA cap applies on a prospective basis only to contracts awarded on or after June 24, 2014. Because the statutory formula cap continues to apply to contracts awarded before June 24, 2014, the Administration is compelled by statute to determine the statutory formula cap amount for FYs 2013 and 2014 in accordance with the statutory formula set forth in section 1127 to address these pre-existing contracts.

After consultation with the Director of the Defense Contract Audit Agency, OFPP has determined, pursuant to the requirements of section 1127, that the statutory formula cap amount for the ceiling on the compensation of a contractor employee covered by this provision is \$980,796 for FY 2013, and \$1,144,888 for FY 2014. Each of these statutory formula cap amounts applies to limit the reimbursement, by the Government to the contractor, of the costs of compensation for certain contractor employees for costs incurred on all covered contracts, at the beginning of the contractor FY that begins January 1 for the respective year (or pro-rated over that portion of the contractor FY that includes January 1 for the respective year). The statutory formula cap amount (i.e., \$980,796) for FY 2013 is applicable to compensation costs incurred on all covered contracts during the period of January 1, 2013 through December 31, 2013 for the contractor's fiscal year. The statutory formula cap amount (i.e., \$1,144,888) for FY 2014 is applicable on all covered contracts to compensation costs incurred as of January 1, 2014 continues in subsequent contractor FYs, unless and until revised by OFPP. As explained above, this statutory formula cap applies only to covered contracts awarded before June 24, 2014 for both defense and civilian procurement agencies to limit the reimbursement of the compensation costs for certain contractor employees.

Employers continue to have the discretion to compensate their employees at any level they deem appropriate. The statutory formula cap only limits how much the Government will reimburse the contractors for the services of those affected employees.

Questions concerning this memorandum may be addressed to Raymond Wong, OFPP, at 202-395-6805.