

DoD Continues to Interpret "Commercial Item" Broadly, Despite Recent Attempts to Narrow



IN SHORT

The Situation: The U.S. Department of Defense has faced criticism from the Office of Inspector General and the Government Accountability Office concerning its handling of commercial item procurements.

The Response: As a result of this criticism, DoD has tried to impose stricter standards for commercial items.

The Outcome: Despite the DoD's efforts, its recent guidance confirms that the standards for qualifying as a commercial item remain as broad as ever.

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In recent years, the Department of Defense ("DoD") has attempted to limit the products and services that qualify for commercial item procurements. While DoD has not succeeded, it has shown no sign that it will abandon these efforts. Nonetheless, DoD's January 31, 2018, response to comments on a final rule, originally proposed in August 2016 to address price reasonableness and commercial item determinations and to encourage opportunities for nontraditional defense contractors, acknowledges the low threshold imposed by existing statutes and regulations for satisfying the definition of "commercial item." DoD's response also provides guidance on how products and services can qualify as commercial items when they have only been offered for sale.



The Department of Defense has lobbied for a more restrictive interpretation of 'commercial item' in recent years.



Defining "Commercial Item"

Consistent with the Federal Acquisition Streamlining Act, the Federal Acquisition Regulation ("FAR") defines "commercial item" in eight categories. This definition, abbreviated below, applies to both civilian agency and DoD procurements.

1. Any item of a type customarily used by the general public or by nongovernmental entities for purposes other than governmental purposes that has been (a) sold, leased, or licensed, or (b) offered for sale, lease, or license to the general public.
2. Any item evolved from an item described in (1) that is not yet available in the commercial marketplace but will be in time to satisfy the delivery requirements under a government solicitation.
3. Any item that would satisfy (1) or (2) but for (a) modifications of a type customarily available in the commercial marketplace, or (b) minor modifications not of a type customarily available in the commercial marketplace.
4. Any combination of items satisfying (1), (2), (3), or (5) that are of a type customarily combined and sold in combination to the general public.
5. Installation services, maintenance services, repair services, training services, and other services if (a) such services are procured for support of an item referred to in (1), (2), (3), or (4), and (b) the source of such services provides similar services contemporaneously to the general public under terms similar to those offered to the federal government.
6. Services of a type offered and sold competitively in substantial quantities in the commercial marketplace based on established catalog or market prices for specific tasks performed or specific outcomes to be achieved and under standard commercial terms and conditions.
7. Any item, combination of items, or service referred to in (1) through (6) of this definition, notwithstanding the fact that the item, combination of items, or service is transferred between or among separate divisions, subsidiaries, or affiliates of a contractor.
8. Nondevelopmental items developed exclusively at private expense and sold in substantial quantities to multiple state and local governments.

Although the government has provided little guidance on how to interpret and apply terms such as "of a

type" and "offered for sale," the limited guidance available uniformly acknowledges that the definition of "commercial item" should be interpreted broadly.

DoD has lobbied for a more restrictive interpretation of "commercial item" in recent years. For example, in 2012, DoD unsuccessfully urged Congress to remove the statutory "of a type" and "offered for sale" criteria. In DoD's view, this change would have permitted the government to acquire commercial items at better prices by ensuring that such items included only those that actually have been sold, leased, or licensed in the commercial marketplace.

Similarly, DoD issued a proposed rule in 2015 that effectively would have altered the "commercial item" definition and eliminated the "of a type" and "offered for sale" criteria. After drawing heavy criticism from industry, DoD ultimately withdrew the proposed rule.

Taking a different approach with commercial items, DoD proposed another rule change in August 2016 with the aim of "provid[ing] guidance to contracting officers for making price reasonableness determinations, promot[ing] consistency in making commercial item determinations, and expand[ing] opportunities for nontraditional defense contractors to do business with DoD." DoD made the rule final on January 31, 2018.

The final rule adds several new Defense Federal Acquisition Regulation Supplement, or DFARS, provisions. Under the new regulations, contractors must submit information adequate for determining price reasonableness at the same time they submit information to support a commercial item determination. Further, the rule implements a statutory change allowing contracting officers to rely on prior commercial item determinations.

The Final Rule's Limitations

Perhaps more notably is what the rule does not accomplish. Despite its recent efforts to impose stricter standards, DoD expressly rejected a suggestion to narrow "commercial item" to "mean goods or services that are actually sold to the general public in like quantities" and noted that the rule "does not revise the definition of 'commercial item' in FAR part 2, nor alter the requirements for commercial item determinations for 'of a type' items."

DoD's comments also confirmed that a "commercial item" does not require that the identical proposed item must be sold or offered for sale to the general public. Though hardly a new concept, DoD went a step further in providing guidance on the type of activities that satisfy the "offered for sale" criteria. Specifically, DoD acknowledged that advertisements on a website, sales orders, quotes, and other information may demonstrate that an item has been "offered for sale."

Although DoD may continue to look for ways to address perceived vulnerabilities in the commercial item procurement process, it is clear that the scope of those efforts will be limited without Congressional approval. Commercial item contractors should continue to assert that DoD and civilian agencies should broadly interpret commercial item requirements.

THREE KEY TAKEAWAYS

1. DoD may attempt to continue its push to impose stricter standards for commercial item procurements, but it has recently conceded that "commercial item" must be interpreted broadly under current statutes and regulations.
2. Absent Congressional action, goods and service should continue to qualify as commercial items based on the "of a type" and "offered for sale" criteria.
3. Contractors can satisfy the "offered for sale" test of commerciality through website advertisements, sales orders, quotes, or other information.

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