UNITED STATES DEPARTMENT OF COMMERCE
Chief Financial Officer
Assistant Secretary for Administration
Washington, D.C. 20230

FEB 1 0 2012

PROCUREMENT MEMORANDUM 2012-02

ACTION

MEMORANDUM FOR: **Bureau Procurement Officials**
Heads of Contracting Offices

Signed

FROM: Barry E. Berkowitz
Senior Procurement Executive and
Director for Acquisition Management

SUBJECT: Recommended Language for 'Instructions to Offerors' for Contracts, Purchase Orders or Task/Delivery Orders That Include Labor Hour Escalation Costs or Pricing

Background

In an increasingly budget-constrained environment within which federal employees are being asked to reassess ongoing activities toward cost reduction and forego salary increases, it is important to include federal contractors as our partners in these efforts. Toward that end, we have prepared recommended language for inclusion in Section L of requests for proposal, and all other 'instructions to offerors', that encourages prospective offerors to eliminate escalation of labor rates for contracts, purchase orders, and task/delivery orders that cross labor-hour adjustment periods. Such elimination of escalation costs can achieve significant savings in the aggregate.

The Office of the Chief Economist (OCE)/Department of Commerce (DOC), has provided data on labor rate and employment trends. OCE's analysis provides a basis for negotiations that result in elimination or significant limitation of labor rate increases for multi-year contracts. The memorandum from OCE is provided as Attachment A.

Purpose

The purpose of this memorandum is to prescribe the active pursuit of reasonable cost-saving measures that can be accomplished through solicitation, negotiation and award of contracts, purchase orders and task/delivery orders that eliminate or significantly limit labor hour escalation costs or pricing.

Applicability
The requirements of this memorandum are applicable to solicitations for proposals or quotes for all contracts, purchase orders and task/delivery orders that include labor hour escalation costs or pricing.

Required Actions
Contracting officers shall include the following language in all solicitations for contracts, purchase orders and task/delivery orders that contain labor hour escalation costs or pricing:

Required solicitation language:
Current significant budgetary constraints demand that the impact of these constraints and ownership of the solution be shared throughout the public sector including its contractors. Offerors are asked to consider reduction or elimination of costs/pricing of the escalation of labor hour rates during the performance period of this contract.

Negotiation, acceptance and award based on reduction or elimination of escalation costs/pricing shall be managed on a case-by-case basis with all reasonable efforts to accomplish cost savings. In most cases, the elimination of labor hour escalation rates is appropriate. Acceptance or limited reduction of labor hour escalation rates may be negotiated where contractor performance and mission success would be significantly harmed by total elimination.

Contracting officers may determine any associated impact to the weight and/or significance of cost/price as a factor in the solicitation and evaluation process.

Effective Date
The requirements herein are effective immediately until rescinded.

Please direct any questions or comments regarding this memorandum to Lori Donovan, ldonovan@doc.gov or (202) 482-1716.

Attachment A: Memorandum from Office of Chief Economist, DOC

cc: Mark Langstein, OGC
Mark Doms, OCE
David Langdon, OCE
Acquisition Community
Acquisition Council

Attachment A

UNITED STATES DEPARTMENT OF COMMERCE
Economics and Statistics Administration
Washington, D.C. 20230

January 2, 2012

MEMORANDUM FOR Lori Donovan
Office of Acquisition Management

From: David Langdon **Signed**
Economics and Statistics Administration
Office of the Chief Economist

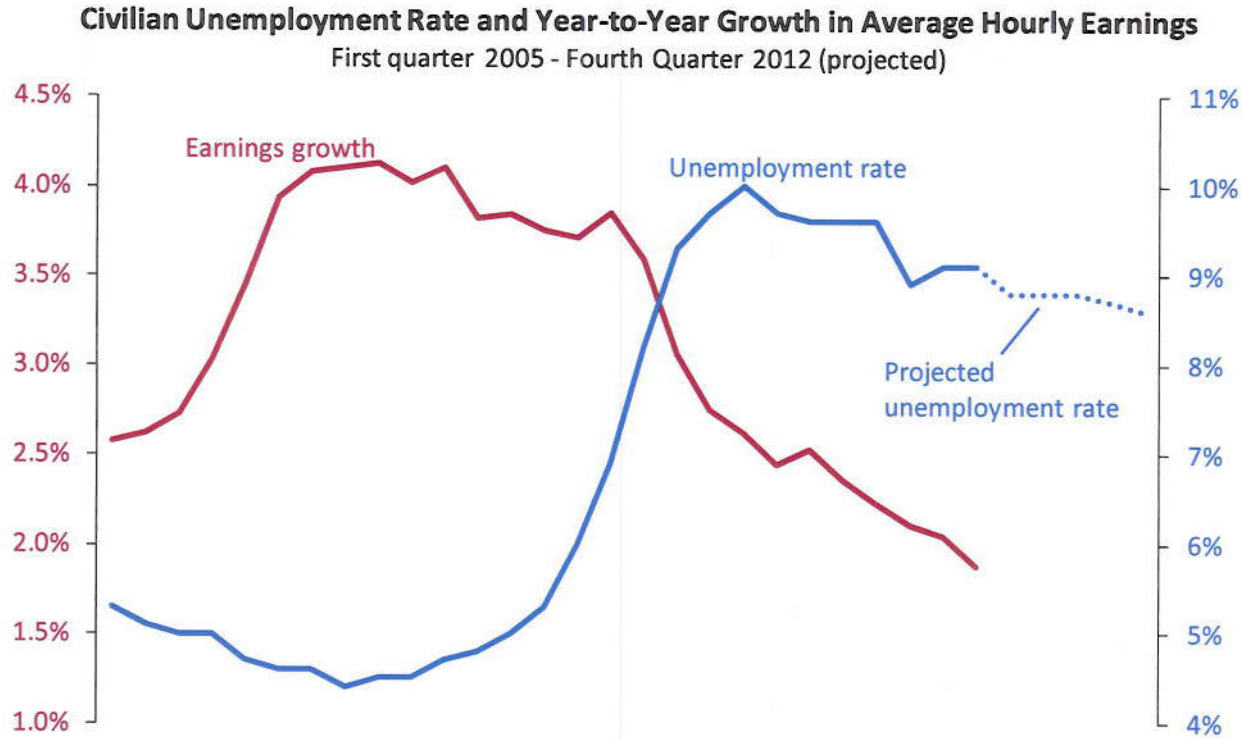
Subject: Wage escalators in Department of Commerce contracts

The freeze on federal pay enacted for fiscal years 2011 and 2012 echoes a broader slowing in wage and salary growth in the private sector. As outlined below, private sector earnings growth is likely to be subdued in the coming years as the unemployment rate is projected to take several years to return to the level associated with full employment, and inflation is expected to be low. These factors call into question the size of wage escalators contained in contracts awarded by the Department of Commerce.

Private sector earnings growth slowed sharply during the Great Recession as unemployment surged, and earnings growth has weakened even more during the economic recovery. Indeed, at the same time that inflation has picked up, earnings growth has decelerated to historic lows. Over the year ended November 2011, nominal average hourly earnings of production or nonsupervisory workers rose just 1.6 percent.

To a large extent, simple supply and demand dynamics underlie the lack of earnings growth. The national unemployment rate of 8.6 remains well above the roughly 5 percent figure often associated with full employment. Furthermore, the labor force participation rate (the share of the civilian non-institutional population age 16 and over that is either working or looking for work) has plunged to its lowest level since the mid 1980s. Low labor force participation tells us that millions of workers are sitting on the margins of the labor market, and many are likely to begin or resume looking for work when they perceive that job growth is gaining speed and hiring opportunities are available to them. To be specific, there are 6.6 million workers who are not in the labor force but who want a job and their entry or re-entry into the labor force is likely to put upward pressure on the unemployment rate and additional downward pressure on wages over the coming years.

ECONOMICS AND STATISTICS ADMINISTRATION



Source: Bureau of Labor Statistics and Blue Chip Economic Indicators.
Note: Earnings are for production or nonsupervisory workers. Both data series are seasonally adjusted.

Weak labor force participation rates combined with projections of modest real GDP growth have led private sector economists to project a slow decline in the unemployment rate in 2012 and the coming years. Blue Chip projections are for the unemployment rate to remain at 8.6 in the fourth quarter of 2012 (see chart). White House projections are for an 8.2-percent unemployment rate in calendar year 2012 and 7.4 percent in 2013. Likewise, consumer prices are expected to increase slowly. Blue Chip projections are for 2.1-percent growth over the year ended fourth quarter 2012, while White House projections are for 1.9-percent growth in calendar years 2012 and 2013.

These conditions strongly suggest that overall private sector earnings growth will remain subdued in the coming years. With such a large backlog of available workers and inflation contained, there is little need for employers to bid up wages in order to fill vacancies. Indeed, as we have seen over the past year, earnings growth is currently failing even to keep up with overall inflation.