February 18, 1998

VIA FACSIMILE 202-606-0633

Abby L. Block  
Chief, Insurance Policy and Information Division  
Office of Personnel Management  
c/o Mary Ann Mercer  
Rm. 3451  
1900 E Street, NW  
Washington, DC 20044

Re: Final Rule, Federal Employees Health Benefits Program Acquisition Regulation;  
Truth in Negotiations Act and Related Changes,  

Dear Ms. Block:

On behalf of the Section of Public Contract Law of the American Bar Association ("the Section"), I am submitting comments on the above-referenced matter. The Section consists of attorneys and associated professionals in private practice, industry and Government service. The Section's governing Council and substantive committees contain members representing these three segments, to ensure that all points of view are considered. In this manner, the Section seeks to improve the process of public contracting for needed supplies, services and public works.

The Section is authorized to submit comments on acquisition regulations under special authority granted by the Association's Board of Governors. The views expressed herein have not been approved by the House of Delegates or the Board of Governors of the American Bar Association and, therefore, should not be
construed as representing the policy of the American Bar Association.

These comments are submitted to identify concerns the Section has with OPM's final rule issued September 10, 1997, regarding implementation of the Truth in Negotiations Act ("TINA") for the Federal Employees' Health Benefits Program ("FEHB" Program). 62 Fed. Reg. 47569-01 (September 10, 1997). Most importantly, the Section believes that OPM's conclusion that community-rated contracts do not qualify for the commercial item exemption to TINA is erroneous. In this respect, the Section would like to bring to OPM's attention a recent General Accounting Office ("GAO") decision that discusses the parameters of the commercial item exception. The new FEHB Acquisition Regulation ("FEHBAR") could be interpreted to require carriers to produce or retain information that exceeds the TINA requirements by requiring: (1) submission of judgmental information and (2) submission of information that relates to subscriber groups that are not Similarly Sized Subscriber Groups ("SSSGs") and therefore would have no impact on the pricing received by the Government. FEHBAR 1602.170-5. The Section requests an opportunity to meet with individuals at OPM responsible for the implementation of OPM's new regulation to discuss these and other issues outlined below.

OPM's Position on Commercial Items Should Be Reconsidered

OPM states in the preamble to its rule that "the FEHB Program community-rated contracts are neither contracts for commercial services, nor are they catalog or market price contracts as those terms are intended by FASA, FAR, and the FAR."1 / The preamble further states that the use of Adjusted Community Rating ("ACR") "is actually a form of experience rating, that is, prospective experience rating" and that carriers using ACR "base their rate directly on the past experience of the Federal group." Therefore, OPM concludes, "no rate based on ACR can possibly be construed to be a market price." Based on these conclusions, OPM made a broad determination that FEHB Program community-rated contracts are not commercial item contracts (including, but not limited to, those applying the ACR methodology) and are, therefore, not exempt from TINA coverage.2 /

(i) The FAR Definition of Commercial Item

The FAR definition of stand-alone commercial services does not require that the exact same services and the exact same prices be found in the commercial marketplace. Rather, the definition provides flexibility by requiring that the services be "of a type" found in the commercial marketplace and that the prices be "based on" market prices. FAR § 2.101 defines commercial items to include stand-alone commercial services as follows:

> 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 under standard commercial terms and conditions. This does not include services that are sold based on hourly rates without an established catalog or market price for a specific service performed.

(Emphasis added). OPM's FEHB Program regulations depart from this definitional flexibility.

(ii) The GAO Decision

The flexibility in the definition of commercial services was given meaning in a bid protest decision issued by the General Accounting Office subsequent to the issuance of the OPM regulations. In Aalco Forwarding, Inc. et. al., B-277241.8; .9, Oct. 21, 1997, 97-2 CPD 110. GAO ruled that household moving services for military personnel qualify as commercial services within the FAR definition of commercial items.

In Aalco Forwarding, the protesters challenged the contracting agency's designation of the military moving services as commercial services within the FAR definition of commercial items. Among other things, the protesters argued that the military moving services were not commercial services because there is no equivalent service in the commercial marketplace and because the international shipment of goods involved in military moving services is not based on established catalog or market prices. GAO rejected both arguments. GAO found that the types of military moving services at issue were essentially the same types of moving services provided in the commercial market, in that movers use the same trucks, warehouses,
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ocean or air carriers, crews, packing materials, and other equipment to perform both DoD's and the commercial market's household goods moving requirements.

With regard to the second argument, GAO found that although there is no standard tariff for international shipments and the rates vary from shipment to shipment, international shipping rates were nevertheless based on established market prices for specific tasks. In this regard, GAO determined that even though the actual overall rates for international shipments were not charged in the commercial marketplace, the overall rates were based on component market rates for component services which did have equivalents in the marketplace.

The same rationale applied in the Aalco Forwarding decision should be applied to community-rated contracts under the FEHB Program. Clearly, the health benefit services being provided under the FEHB Program contracts to Federal Government employees are the same types of health services provided in the commercial marketplace to corporate employees. Similarly, although the actual rates contained in the FEHB contracts are not identical to rates found in the commercial market, the components and methodologies from which the FEHB rates are derived are the same as those utilized in the commercial marketplace.

In sum, because the FEHB Program rates are determined in the same manner as the rates for commercial health benefit contracts, i.e., utilizing the same components and methodologies as commercial rates, it is appropriate to apply the commercial item exception.

Further evidence that the FEHB Program contracts should be considered commercial item contracts is that Congress has specifically categorized the agreements with Uniformed Services Treatment Facilities ("USTF") for managed health care services as "commercial item" contracts within the meaning of the FAR. In Section 722(b)(2) of the Defense Department Authorization Act for 1997 (Pub. L. 104-201, now codified in 10 U.S.C. § 1073 note), Congress specifically defines those USTF agreements as acquisitions of commercial items. Payments under the USTF agreements are on a full risk capitation payment basis, which means that the payments are "based on the utilization experience of enrollees and competitive market rates for equivalent health care services for a comparable population to such enrollees in the area in which the designated provider is located." Section 726(a) of Pub. L. 104-201 (codified in 10 U.S.C. § 1073 note). The rates to be charged under the USTF agreements are equivalent to the ACR rates to be charged under the FEHB Program contracts in that both are based on utilization experience of enrollees. Congress has specifically determined that such agreements qualify as acquisitions of commercial items.

For all of the above reasons, OPM should determine that the FEHB Program contracts involve the acquisition of commercial items and revise its regulations to indicate that the commercial item exemption from TINA is applicable to these contracts.

The "Cost or Pricing Data" Definition

In promulgating its TINA regulation, OPM has recognized that the FEHB Program community-rated contracts are unique and do not fit into either the fixed-price or cost reimbursement categories of contracts. OPM has created a new classification of "negotiated benefits contracts" for these unique contracts. OPM has concluded that this new term more accurately describes these community rated contracts. OPM also has recognized that the data used by community-rated contractors is not similar to cost or pricing data in the more traditional government contract context, which typically consists of labor rates and material costs. Accordingly, the FEHBAR contains its own definition of "Cost or pricing data for community rated carriers" as follows:

"Specialized rating data used by carriers in computing a rate that is appropriate for the federal group and the SSSGs [similarly sized subscriber groups]. Such data include, but are not limited to, capitation rates; prescription drug, hospital, and office visit benefits utilization data; trend data; actuarial data; rating methodologies for other groups; standardized presentation of the carrier's rating method (age, sex, etc.) showing that the factor predicts utilization; tiered rates information; "step-up" factors information; demographics such as family size; special benefit loading capitations; and adjustment factors for capitation.
OPM's definition of cost or pricing data is confusing. It gives cost or pricing data a meaning completely different from the meaning it has acquired over the last 35 years. OPM has defined "cost or pricing data" so as to limit its meaning, yet the "Certificate of Accurate Cost or Pricing Data" is open-ended and could be read to include cost or pricing data in the more traditional sense. Additionally, it is not clear if OPM considers the information underlying the state approved capitation rates to be cost or pricing data that must be submitted to OPM, or whether only the approved capitation rate would qualify as cost or pricing data.

Other significant differences exist between the FEHB Program and the typical contracts subject to TINA. It should be recognized that FEHB Program contracts are not negotiated; these contracts are automatically renewed each year. This difference is significant because there is no process of negotiating costs and, therefore, there is no need for the "informational parity" sought by Congress in passing TINA. The price for the FEHB Program contract is determined by the pricing methodology used by the SSSGs. The selection of SSSGs is determined in accordance with OPM regulations and instructions from OPM. Thus, there is no negotiation of "price," either.

TINA is a disclosure statute intended to put the government on equal footing with contractors during negotiations. The key concept is that contractors must disclose to the government all cost or pricing data in their possession prior to agreement on price. The FAR requires the Contracting Officer to prepare a price negotiation memorandum ("PNM") to document the extent to which he or she relied on the cost or pricing data submitted by the contractor. FAR 15.808. Among other things, this price negotiation memorandum must state the extent to which the Contracting Officer relied upon the submitted cost or pricing data. In contrast, the OPM does not require disclosure of "cost or pricing data" prior to contract renewal. It is difficult to perceive how OPM can rely on cost or pricing data that OPM is not requiring to be submitted with an offeror's rate proposal. See FEHBAR 1615.802.

It is apparent that OPM's attempted application of TINA to the FEHB poses significant problems, of which we have addressed a few of the more important.

The Section appreciates the opportunity to provide these comments and is available to provide additional information or assistance as you may require.

Sincerely,

Marcia G. Madsen
Chair
Section of Public Contract Law

cc: David A. Churchill
    Rand L. Allen
    Gregory A. Smith
    Patricia A. Meagher
    Marshall J. Doke, Jr.
    John T. Kuebls
    Michael K. Love
    Council Members
    Chair and Vice Chairs, Health Care Contracting Committee
    Chair and Vice Chairs, Commercial Products Committee
    Chair and Vice Chairs, Accounting, Cost, and Pricing Committee
    Alexander J. Brittin

1 / One of the key facets of FASA, and subsequently FAR, was the goal of reducing the burden that the TINA requirements imposed on commercial companies. 60 Fed. Reg. 48210. When the proposed FAR provision implementing FASA's TINA amendments was published in the Federal Register, the drafters commented that:
Use of "cost or pricing" data is coupled with a reminder that unnecessarily requiring that type of data is not desirable and can lead to additional costs to both the government and the contractor. 60 Fed. Reg. 48208.

2 / On July 31, 1996, the Section submitted comments to the OPM that responded to OPM's proposed rule amending the FEHBAR to eliminate the long-standing statutory interpretation by OPM that community-rated contracts qualify for the market pricing exception to TINA. At that time, the GAO had not issued its decision providing additional clarification of the term "commercial item."

3 / The specific rate charged the FEHB Program is affected by FEHB Program utilization of health care services when ACR is used to develop a group's rate. The cost components from which the FEHB Program rate is derived for ACR--including carrier administrative expenses, provider costs such as capitation (fixed per member per month amounts), and provider fee-for-service payments are the same components used to set rates in the commercial market.

4 / At a minimum, OPM should revise the regulations to indicate that the commercial item exemption applies to those contracts based on traditional community rating or community rating by class because they do not involve the use of experience data in the rate development process.