SEC. 807. EXTENSION TO ALL CONTRACTOR EMPLOYEES OF APPLICABILITY OF THE SENIOR EXECUTIVE BENCHMARK COMPENSATION AMOUNT FOR PURPOSES OF ALLOWABLE COST LIMITATIONS UNDER GOVERNMENT CONTRACTS.

(a) ALLOWABLE COSTS UNDER DEFENSE CONTRACTS.—

(1) CERTAIN COMPENSATION NOT ALLOWABLE.—Subsection (e)(1)(P) of section 2324 of title 10, United States Code, is amended by striking "senior executives" and inserting "employees".

(2) CONFORMING AMENDMENT.—Subsection (l) of such section is amended by striking paragraph (5).

(b) ALLOWABLE COSTS UNDER NON-DEFENSE CONTRACTS.—

(1) CERTAIN COMPENSATION NOT ALLOWABLE.—Subsection (a)(16) of section 4304 of title 41, United States Code, is amended by striking "senior executives" and inserting "employees".

(2) CONFORMING AMENDMENT.—Section 4301 of such title is amended by striking paragraph (4).

(c) EFFECTIVE DATE.—The amendments made by this section—

(1) shall be implemented in the Federal Acquisition Regulation within 180 days after the date of the enactment of this Act; and

(2) shall apply with respect to costs of compensation incurred after January 1, 2012, under covered contracts entered into before, on, or after the date of the enactment of this Act.

Section-by-Section Analysis

This proposal would amend provisions of law relating to allowable costs under Government contracts — section 2324 of title 10, United States Code, and section 4304 of title 41, United States Code — to expand the existing executive compensation cap so that it would apply to all employees of a contractor instead of just the "five most highly compensated" management employees of each contractor's segment or home office, as under current law. Changes are required to both title 41, United States Code (Public Contracts), and title 10, United States Code (Armed Forces), the former for non-defense contracts and the latter for defense contracts. The Department of Defense (DoD) is not recommending any changes in the way that the compensation cap is calculated in accordance with section 1127 of title 41, United States Code.

Under current law, the allowable costs of compensation of senior executives of contractors is limited to the benchmark compensation amount set by the Administrator of the Office of Federal Procurement Policy under section 1127 of title 41 United States Code. In accordance with that section, the Administrator of the Office of Federal Procurement Policy shall review commercially available surveys of executive compensation and, on the basis of the results of the review, determine a benchmark compensation amount to apply for each fiscal year. The benchmark compensation amount (commonly referred to as the "compensation cap") applicable for a fiscal year is the median amount of the compensation provided for the five most highly compensated employees in management positions at each home office and each segment of the contractor (i.e., senior executives) of all benchmark corporations for the most recent year for which data is available. The term "benchmark corporation" means a publicly-owned United States corporation that has annual sales in excess of $50,000,000 for the fiscal year. Collectively, these sections limit the allowable cost of compensation of the five most highly compensated employees in management positions at each home office and each segment of the contractor to the benchmark compensation amount.

In the mid-nineties, there was increasing concern in Congress regarding seemingly excessive individual compensation charged to DoD contracts. As a result, for fiscal year (FY) 1995 and FY 1996, Congress limited the allowability of individual compensation of all employees on covered DoD contracts. For 1997 through 2009, Congress revised the application of the compensation ceiling so that it applied only to certain contractor personnel generally identified as the top five most highly compensated individuals in senior management positions at each home office and each segment of a contractor. The Department of Defense believes that the current law, which limits the compensation of only the five most highly compensated employees in management positions, places the Government at an unacceptable risk of reimbursing contractors for excessive compensation costs.

The intent of the compensation cap is to reduce the risk of excessive individual compensation charged to Government contracts. Audits by the Defense Contract Audit Agency have shown that there are lower level executives not subject to the cap and non-executive employees who receive compensation in excess of the benchmark compensation amount. In addition, if a contractor is not organized into multiple segments, only the top five executives are covered by the benchmark compensation amount, whereas similarly sized contractors with multiple segments will have additional employees subject to the cap. Limiting the application of

the compensation cap to only the top five executives places the Government at risk of reimbursing contractors for excessive compensation. Therefore, as a matter of public policy, DoD recommends extending the limits on all contractor employee compensation.

Budget Implications: This proposal has no budgetary impact. It only proposes to expand the applicability of the executive benchmark compensation amount allowable cost limitation to all contractor employees.

Changes to Existing Law: This proposal would amend section 2324 of title 10, United States Code, and sections 4301 and 4304 of title 41, United States Code, as follows (inserted text is represented by **bold underline**; eliminated text is ~~struck through~~):

Title 10, United States Code

§2324. Allowable costs under defense contracts

(a) ***

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(e) SPECIFIC COSTS NOT ALLOWABLE.—(1) The following costs are not allowable under a covered contract:

(A) ***

* * * * *

(P) Costs of compensation of ~~senior executives~~ **employees** of contractors for a fiscal year, regardless of the contract funding source, to the extent that such compensation exceeds the benchmark compensation amount determined applicable for the fiscal year by the Administrator for Federal Procurement Policy under section 1127 of title 41.

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(l) DEFINITIONS.—In this section:

(1) ***

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~~(5) The term "senior executives", with respect to a contractor, means the five most highly compensated employees in management positions at each home office and each segment of the contractor.~~

(6) The term "fiscal year" means a fiscal year established by a contractor for accounting purposes.

Title 41, United States Code

§ 4301. Definitions

In this chapter:

(1) ***

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~~(4) SENIOR EXECUTIVE.—The term ''senior executive'', with respect to a contractor, means the 5 most highly compensated employees in management positions~~.

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§ 4304. Specific costs not allowable

(a) SPECIFIC COSTS.— The following costs are not allowable under a covered contract:

(1) ***

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(16) Costs of compensation of ~~senior executives~~ **employees** of contractors for a fiscal year, regardless of the contract funding source, to the extent that such compensation exceeds the benchmark compensation amount determined applicable for the fiscal year by the Administrator under section 1127 of this title.

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