

Costs and Cost Analysis

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Module Introduction

Welcome to Costs and Cost Analysis!

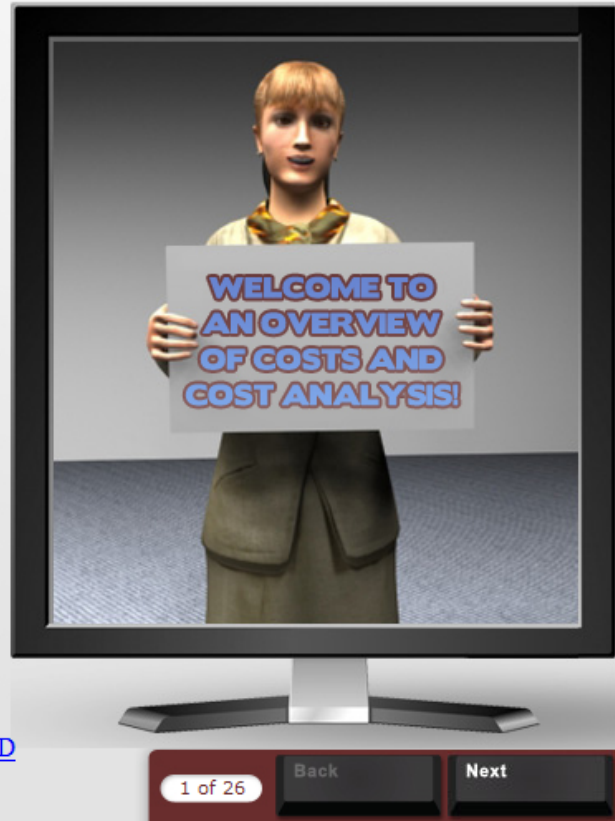
You might be wondering, "How will the information in this module help me in my job as a contract specialist?"

This module describes contract costs and cost analysis. As a contract specialist, you need to know about costs and cost analysis including:

- Fundamentals of cost analysis
- Government pricing objectives
- Key cost analysis terms, techniques, and considerations
- Distinctions between cost analysis, price analysis, and cost realism analysis
- Cost estimating methods

You may be familiar with some or all of the information above but an overview would be beneficial.

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Objectives

At the end of this module, you will be able to:


- Identify the fundamentals of cost analysis
- Distinguish between cost analysis, price analysis and cost realism analysis
- Identify cost analysis terms and techniques used when developing a prenegotiation position

Sound good? All right, let's get started!

Select Next for a high-level overview of the content that will be presented in this module.

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Costs and Cost Analysis

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Overview - Cost Analysis

What is cost analysis? Cost analysis is the review and evaluation of the separate cost elements and proposed profit/fee of an offeror's certified cost or pricing data or data other than certified cost or pricing data.

It is important to evaluate the separate cost elements and proposed profit/fee to determine how the proposed costs represent the cost of the contract, assuming reasonable economy and efficiency.

RESOURCES PROPOSED				RATES AND FACTORS TABLE				COST BREAKDOWN SUMMARY			
	2008	2009	2010		2008	2009	2010		2008	2009	2010
Raw Material				Design Eng	\$50/hr	\$55	\$60	Material & SubK			
Sub Contracts				Test Eng				Material O/H			
Design Eng Hrs	2050	1025		Mfg (Fab)				Engineering			
Test Eng Hrs		1025	2050	Mfg (Assmbly)				Engineering O/H			
Mfg (Fab)				Mat Scrap				Manufacturing			
Mfg (Assmbly)				Escalation				Mfg O/H			
								(Etc.)			

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Overview - Government Pricing Objective

Contracting Officers are required to purchase supplies and services from responsible sources at fair and reasonable prices.

This requirement is based on the three elements that form the foundation of the government's pricing objective.

Review the graphic to the right to learn more.



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Overview - Government Approaches to Contract Pricing

In contracting, when you act as the government's buyer, your primary objective is to acquire supplies and services from responsible sources at fair and reasonable prices.

The three approaches acknowledged by the government to attain this objective are:

- Price analysis
- Cost analysis
- Cost realism analysis



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Overview - Terms and Techniques

It is critical that you understand techniques and terms of cost analysis. Terms that are important not only include cost analysis, price analysis, and cost realism analysis, but also terms such as direct costs, indirect costs, and other direct costs.

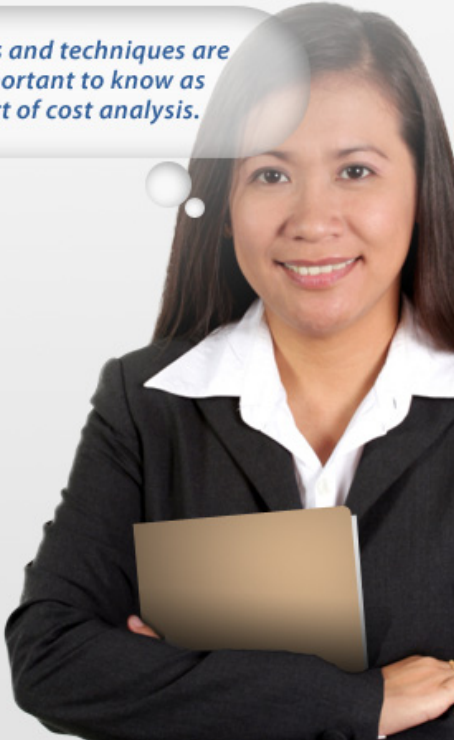
In addition, there are techniques with which you should be familiar. These include the various price analysis techniques and procedures that help the government to ensure a fair and reasonable price.

You may be responsible for selecting the techniques for comparison that are used to verify that the overall price that is offered is fair and reasonable.

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Terms and techniques are important to know as part of cost analysis.



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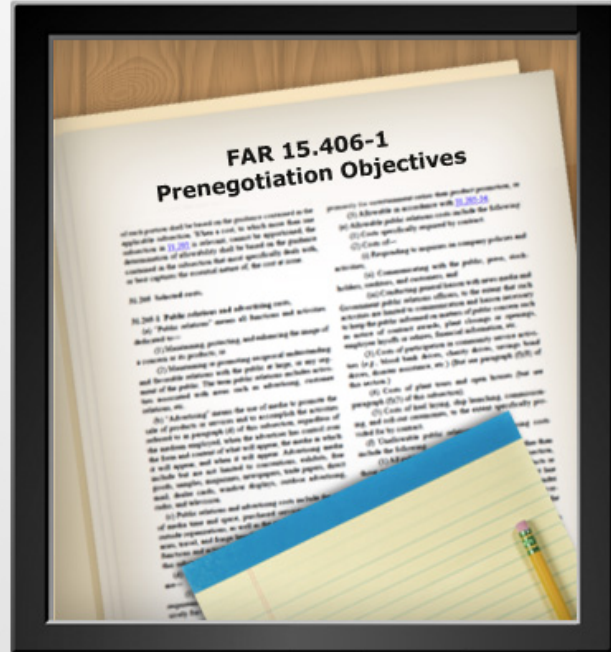
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Overview - Prenegotiation Position

In order to develop a prenegotiation position, you would analyze contract costs and price, utilizing contract analysis terms and techniques.

Prenegotiation objectives establish the government's initial negotiation position. The Contracting Officer establishes prenegotiation objectives before the negotiation of any pricing action.

Review FAR 15.406-1 to learn more about Prenegotiation Objectives.



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Overview - Cost Estimating Methods

There are many methods for estimating costs in an equitable and consistently applied way. Some cost estimating texts identify ten or more! The most common classification, however, identifies three methods:

- Round-table
- Comparison
- Detailed

Select the text below each image to the right to learn more about these three cost estimating methods.

**ROUND TABLE****COMPARISON****DETAILED**

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Overview - Cost Estimating Methods

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Round Table - Windows Internet Explorer

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Round Table

In a round table, experts are brought together to develop cost estimates by exchanging views and making judgments based on knowledge and experience. This method is most commonly used when there is little or no cost experience or detailed product information (e.g., specifications, drawings, or bills of material).


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ROUND TABLE



COMPARISON



DETAILED

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Overview - Cost Estimating Methods

Comparison - Windows Internet Explorer

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Comparison

With the comparison method, costs for a new item are estimated using comparisons with the cost of completing similar tasks under past or current contracts. Any differences are isolated and cost elements applicable to the differences are deleted from or added to experienced costs. Comparisons may be made at the cost element level or total price level. Adjustments may also be made for possible upward or downward cost trends.


This method is most commonly used when specifications for the item being estimated are similar to other items already produced or currently in production and for which actual cost experience is available.

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ROUND TABLE



COMPARISON



DETAILED

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Overview - Cost Estimating Methods


Detailed - Windows Internet Explorer

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Detailed

The detailed method is characterized by a thorough review of all components, processes, and assemblies. It requires detailed information to arrive at estimated costs and typically uses cost data derived from the accounting system, adjunct statistical records, and other sources.


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ROUND TABLE



COMPARISON



DETAILED

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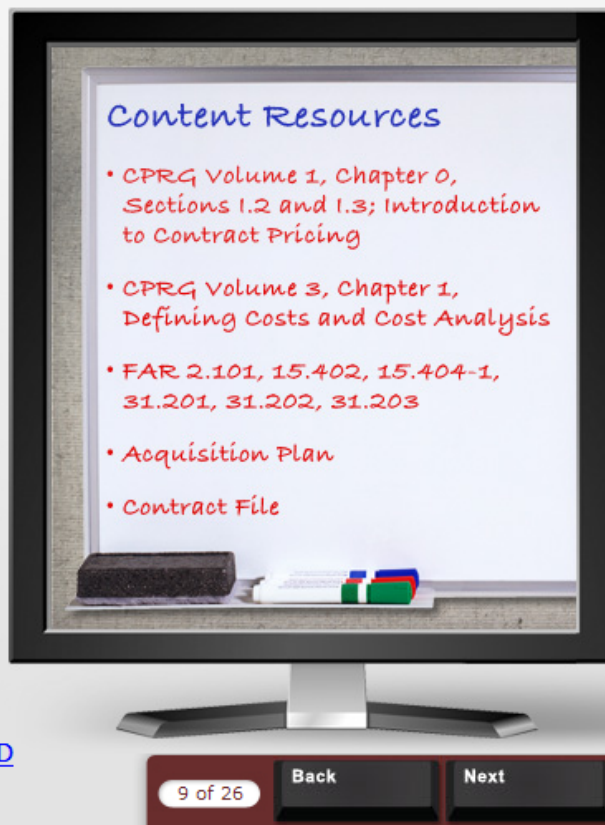
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Module Resources

Review the graphic to the right to see what specific resources are used as references for the content in this module.

It is strongly recommended that you review these resources before proceeding with the module. Doing so will put you "ahead of the game" and will help you to answer the challenge questions to come!

Select the Resources tab for links to these and other references.

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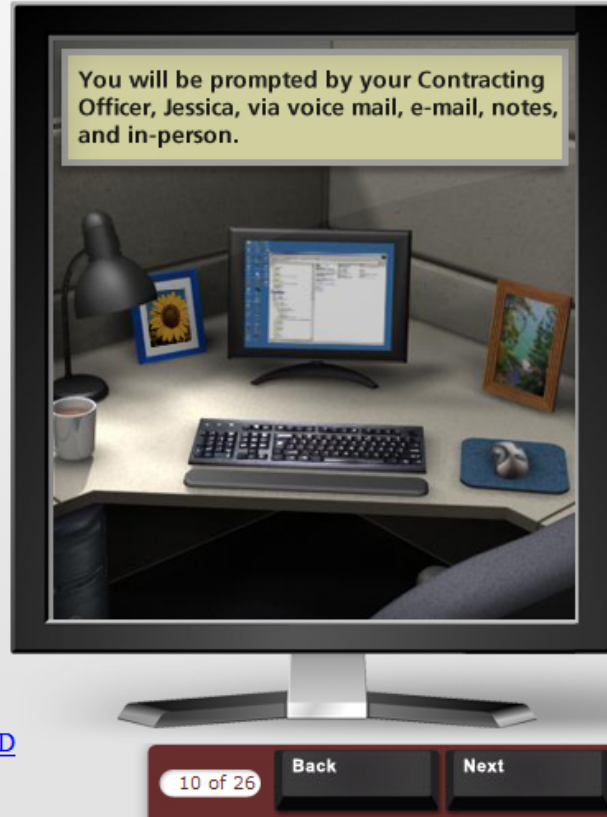
Simulation Overview

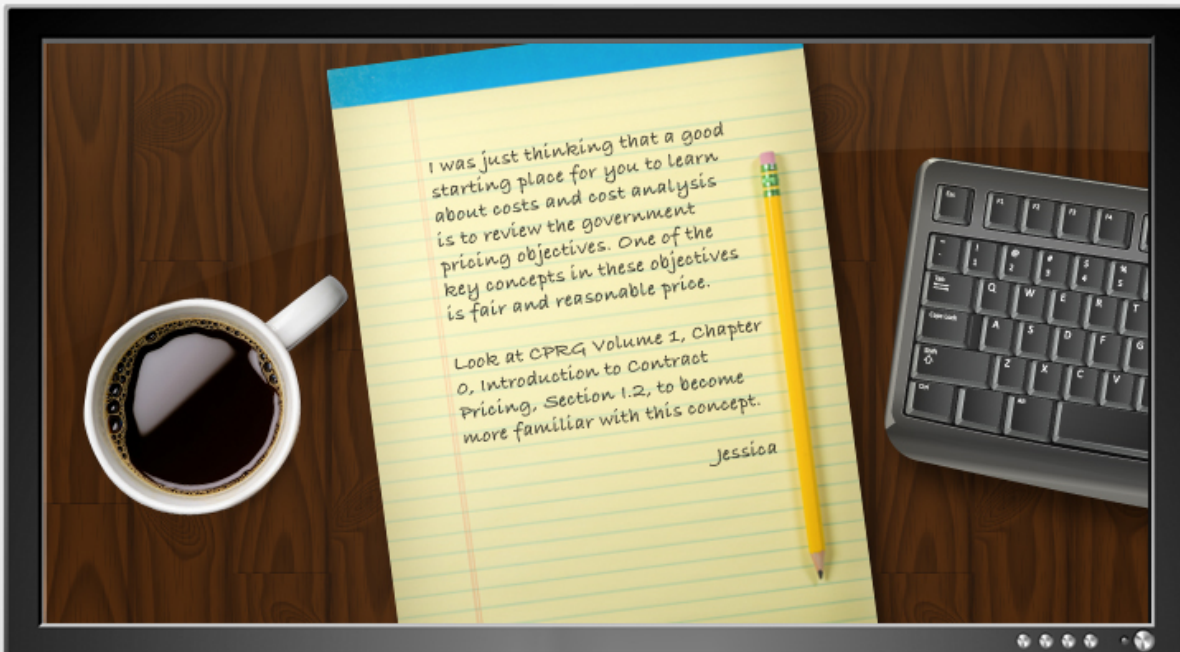
In this module, you are going to answer a series of Challenge Questions about costs and cost analysis. Do not worry if you miss a question - you will be directed to pertinent content and then given a chance to answer the question again.

Even if you get a question right the first time, it is strongly recommended that you elect to review the pertinent content by selecting the Review button. This review will help you answer the practice test questions at the end of the module.

Remember to use the Resources and Glossary tabs at any time during the simulation to access helpful information.

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Challenge Question #1

One of the elements of the government pricing objective is to ensure that contract prices are fair and reasonable.

Which of the following statements is true about "fairness to a seller" that involve concerns? Select all of the correct answers.

- ☐ A. Sellers need to be concerned about an unrealistic low price because of the risk.
- ☐ B. Sellers need to be concerned about the market implications of a price that is too high.
- ☐ C. Sellers need to be concerned about major mistakes in estimating costs.
- ☐ D. Sellers need to be concerned about recovering buy-in losses.

[Check Answer](#)

User Instructions: Select the correct answers and then select the Check Answer button.

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Fair to the Seller

What is a fair price to the seller?

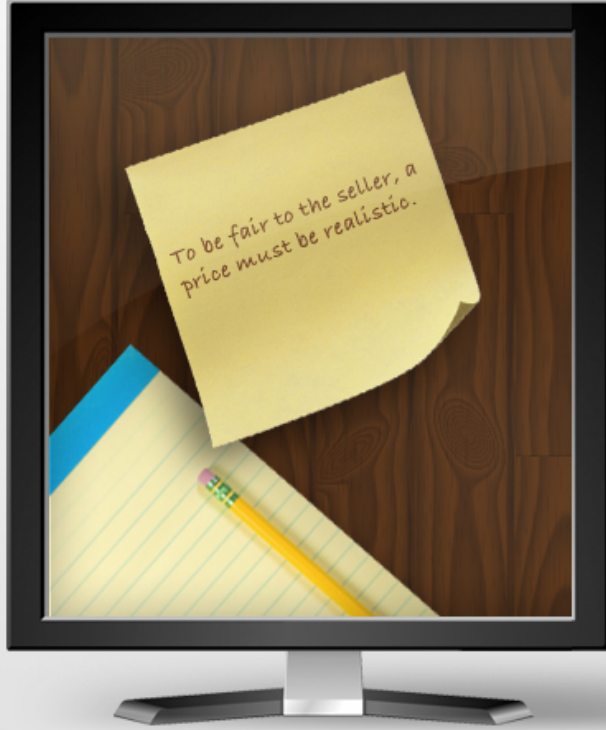
A fair price for the seller means that the seller will be able to satisfy the terms and conditions of the contract. An offer that is too low is considered unrealistic. Why does it matter if a low offer is unrealistic?

An unrealistic price puts the company's financial health at risk and the company may not be able to stay in business. In addition, the government's risk is that in order to minimize financial risks and stay in business the company may:

- Cut corners on the quality of the product,
- Deliver the product late,
- Default on delivery, forcing a time-consuming reprocurement, and/or
- Refuse to deal with the government in the future.

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Fairness to the Seller - Special Considerations

Fairness to the seller can be a concern in both competitive and noncompetitive situations. Below are situations for special considerations.

- Below-Cost Prices
- Mistakes
- Single-Source Procurements

First, let's look at **Below-Cost Prices**. Below-cost prices are NOT necessarily unfair to the seller. An offeror, for various reasons as part of business judgment, may decide to submit a below-cost offer. However, these types of offers are not invalid.

A company may be trying to enter a new market where they have no relevant past performance history. Or the company is attempting to cover their costs of performance even if they make little or no profit for a variety of business reasons.

Whether the awardee can perform the contract at the price offered is a matter of responsibility.

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Special Considerations - Mistakes

Mistakes are another special considerations for fairness to the seller.

The offered price may be unexpectedly low because the seller has made gross mistakes in estimating costs or is nonresponsive.

The award of a contract to a supplier based on lowest evaluated price alone can be false economy if there is subsequent default, late deliveries, or other unsatisfactory performance resulting in additional contractual or administrative costs.

A prospective contractor must affirmatively demonstrate its responsibility, including, when necessary, the responsibility of its proposed subcontractors.


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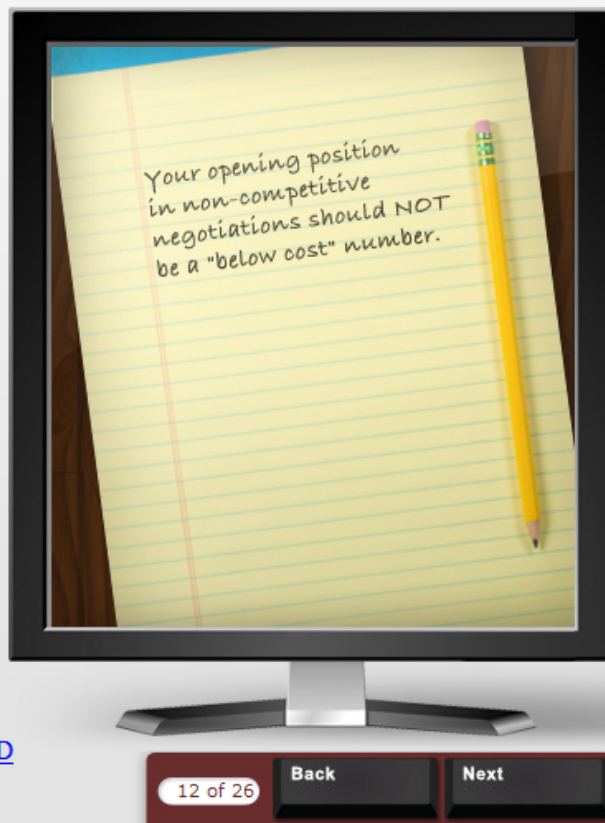
Special Considerations – Single-Source Procurements

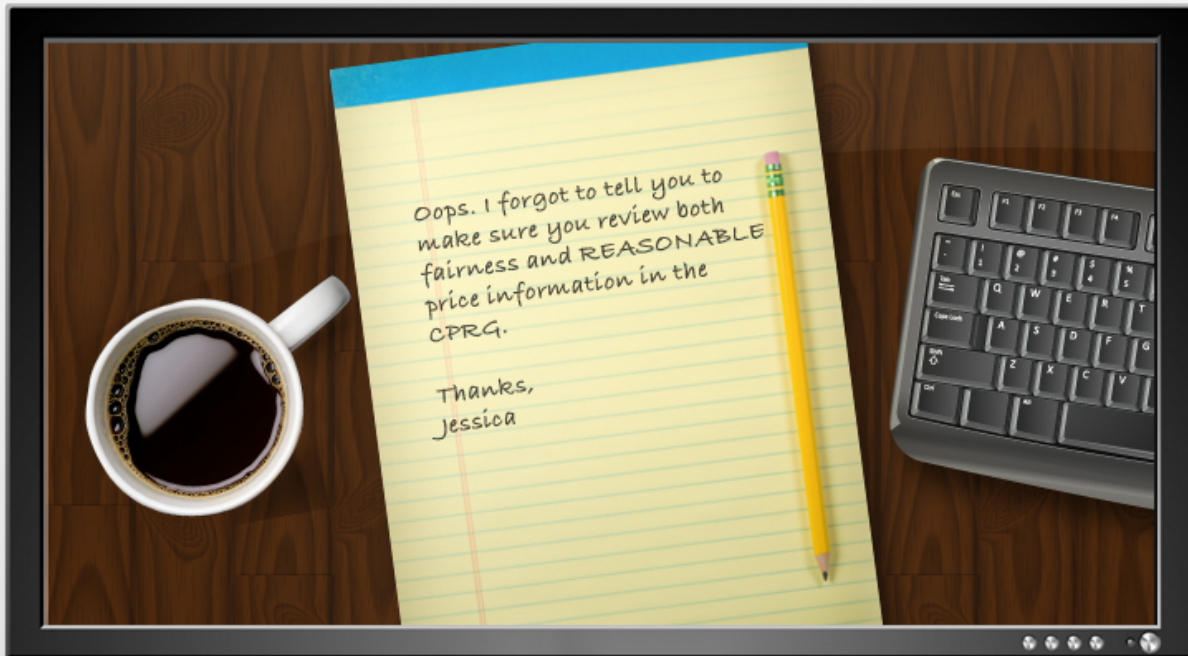
Single-source procurements are another special consideration. You need to remember that you CANNOT force a final price/cost that will be below cost on the offeror even if you believe that the offeror has the financial ability to absorb the probable loss.

So what should you do in that situation? Instead, negotiate a contract with a type and price that is likely to cover all allowable costs of performance, assume reasonable economy and efficiency, and provide a reasonable profit. Review [FAR 15.404-4](#) and [DFARS 215.404-4](#) on profit analysis.

Ensure your opening position is based on a more optimistic reading of the potential production improvements, risks, and costs of providing the contract deliverable rather than targeting price.

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Costs and Cost Analysis[Resources](#)[Glossary](#)[Help](#)**Fairness and Reasonable Price****User Instructions:** Select Next to continue.[D](#)

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Challenge Question #2

Which of the following are market conditions that affect a reasonable price? Select all of the correct answers.

- ☐ A. Competition
- ☐ B. Supply and Demand
- ☐ C. General Economic Conditions
- ☐ D. Market Entry/Exit
- ☐ E. Single Source Procurements

[Check Answer](#)

User Instructions: Select the correct answers and then select the Check Answer button.

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Reasonable Price

A reasonable price is a price that a prudent and competent buyer will be willing to pay, based on market conditions such as **supply and demand, general economic conditions, and competition.**

Let's look at each of these conditions.

SUPPLY and DEMAND	GENERAL ECONOMIC CONDITIONS	COMPETITION
<ul style="list-style-type: none">• Supply and demand can have a significant effect on product prices.• If demand is constant, a decrease in supply usually creates higher prices, and an increase in supply usually creates lower prices.• If supply is constant, a decrease in demand usually creates lower prices, and an increase in demand usually creates higher prices.	<ul style="list-style-type: none">• General economic conditions affect the prices of all products, but the effect will NOT be the same for every product.• Inflation and deflation affect dollar value. Conditions such as a boom, recession, and depression affect available production capacity.	<ul style="list-style-type: none">• When competition does not exist, supply and demand may not work effectively. The buyer or seller may have an advantage in the pricing decision process.

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Thanks for meeting me here. I wanted to go over the last two government objectives with you and see if you have any questions.

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The middle box, 'Price each contract separately', has two key components which are perspective and government contracting.

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Do you know what these two components mean as they relate to the government objective?

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Challenge Question #3

All of the following statements are true about government contracting as part of pricing each contract separately EXCEPT:

- ☐ A. Buyers and sellers usually have a good working knowledge of transactions between a contractor and the government.
- ☐ B. Business conditions can change the specifics of government contracting.
- ☐ C. Market forces like competition and supply and demand must be considered.
- ☐ D. Balancing of one contract against another contract in financial results is not allowed.

[Check Answer](#)

User Instructions: Select the correct answer.

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Price Each Contract Separately

The second element of the government's pricing objective is to **Price Each Contract Separately**. Two key components of this element are:

- Perspective
- Government contracting

Let's look at both of these components in more detail.



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Perspective

What is perspective? Perspective is how the buyer and the seller "see" a contract. Human nature encourages us to balance one contract against another in terms of financial results.

The **seller's position** might be that the firm lost money on the last contract so an effort needs to be made to make up for that loss on the next contract.

The **buyer's position** might be that the contractor made too much profit on the last contract so the next contract should be structured to restrict profit.

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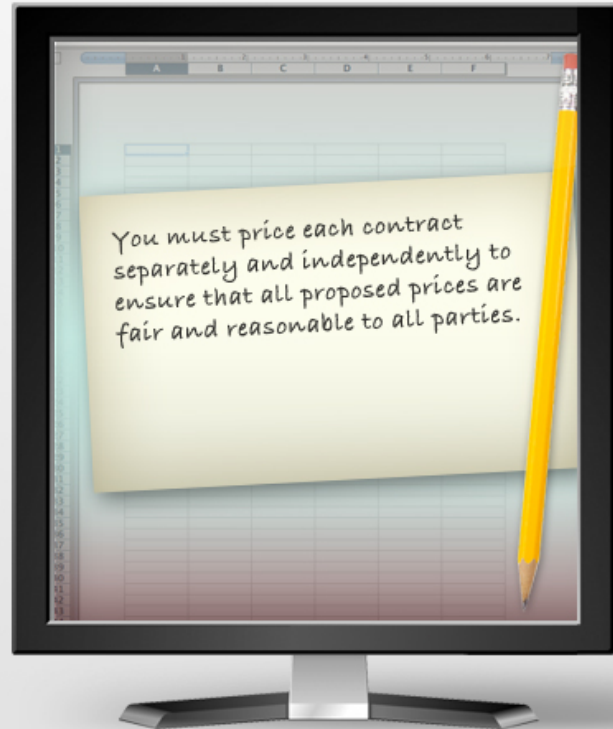
Government Contracting

What is government contracting?

Government contracting can be very complex. Although the buyer's perspective and the seller's perspective can be understandable in certain situations, these perspectives are not valid in government contracting.

Government contracting can be challenging when:

- Buyers and sellers do not have knowledge of all transactions that occur between a contractor and the government
- Market forces exist such as competition and changes in supply and demand
- Business conditions change



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Exclude Contingencies

The final government objective is **Exclude Contingencies**. This objective requires that contracts exclude contingencies that cannot be reasonably estimated at the time of the award.

You might want to review [FAR 15.402\(c\)](#) for more information.



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Costs and Cost Analysis[Resources](#)[Glossary](#)[Help](#)**Challenge Question #4**

Which of the following is the correct definition of a contingency in government contracting?

- ☐ A. Current event arising from known causes with the outcome almost certain
- ☐ B. Possible future event arising from unknown causes with the outcome almost certain
- ☐ C. Current event arising from unknown causes where the outcome cannot be determined
- ☐ D. Possible future event arising from known or unknown causes where the outcome cannot be determined

[Check Answer](#)

User Instructions: Select the correct answer.

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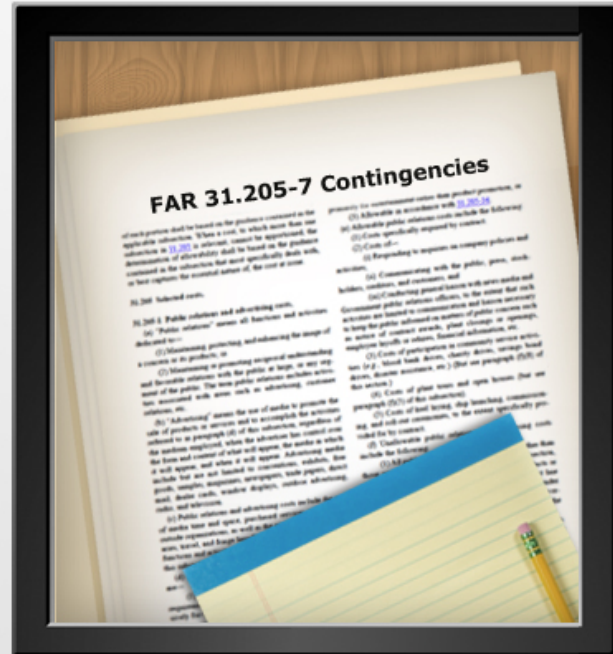
Contingency in Government Contracting

What is a contingency?

A **contingency** is a possible future event or condition arising from presently known or unknown causes and the outcome cannot be determined at the present time.

There are two types of contingencies that are important to government contracting. Review [FAR 31.205-7](#) to learn more.

1. Contingencies can arise from permanently known and existing conditions with the effects of these conditions to be foreseeable within reasonable limits of accuracy
2. Contingencies can arise from known or unknown conditions, where the effects **cannot** be measured to provide equitable results to the contractor and the government.



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Costs and Cost Analysis[Resources](#)[Glossary](#)[Help](#)**Contingency in Government Contracting (cont.)**

Let's look at some examples of how to handle each type of contingency based on the contract price.

EXAMPLE	TYPE OF CONTINGENCY	CONTACT PRICE
Cost of rejects/Cost of defective work	Foreseeable within reasonable limits of accuracy	Contingencies of this type should be included in contract cost estimates to make those estimates as accurate as possible.
Results of pending litigation / Costs of volatile material price changes	Cannot be measured so precisely as to provide equitable results to the contractor and to the government	Contingencies of this type should be excluded from the cost estimates under the several items of cost, but should be disclosed separately (including the basis on which the contingency is computed) to facilitate the negotiation of appropriate contract coverage.

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Contingency in Government Contracting (cont.)

Here are some final points on contingency and contract price.

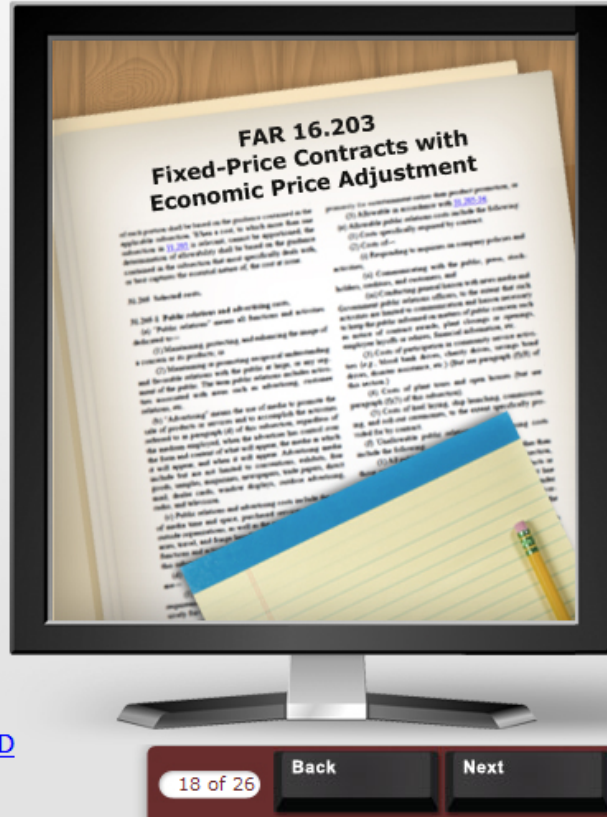
If you have extensive production experience with a given product, the contractor and the government can likely agree on the amount of scrap that can reasonably be expected during production. This type of contingency should be included in contract cost estimates.

In times of volatile material price changes, it would be unreasonable to both parties for an offeror to include a contingency to cover significant price increases when none may occur.

In this situation, you should consider use of a contract type (e.g., [Fixed-Price Contracts with Economic Price Adjustment](#)) that provides for separate consideration of volatile price changes. The use of a separate consideration can provide for better contract pricing and more effective competition.

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Contingency in Government Contracting (cont.)

Here are some final points on contingency and contract price.

If you have extensive production experience with a given product, the contractor and the government can likely agree on the amount of scrap that reasonably be expected during production. The amount of contingency should be included in contract estimates.

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In this situation, you should consider use of a contract type (e.g., [Fixed-Price Contracts with Economic Price Adjustment](#)) that provides for separate consideration of volatile price changes. The use of a separate consideration can provide better contract pricing and more effective competition.

Fixed-Price Contracts with Economic Price Adjustments

A fixed-contract with economic price adjustment provides for upward and downward revision of the stated contract price upon the occurrence of specified contingencies.

Economic price adjustments are of three general types: adjustments based on established prices; adjustments based on actual costs of labor or material; adjustments based on cost indexes of labor or material

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Types of Analyses

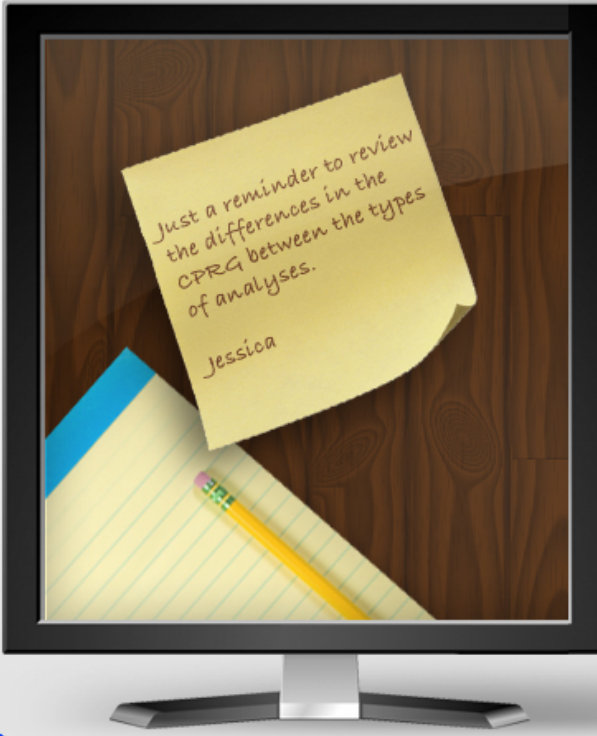
There are three types of analyses associated with analyzing contract costs. They are:

- Price Analysis
- Cost Realism Analysis
- Cost Analysis

See the note from Jessica about types of analyses.

Review the CPRG, Volume 1, Chapter 0, Section I, Identifying Government Approaches to Contract Pricing. This section of the CPRG discusses price, cost, and cost realism analysis.

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Challenge Question #5

You have been asked to procure seven high definition mobile cameras. You determine that this is a commercial item. The prices for these items range from approximately \$400,000 to \$650,000 each. You identify six vendors but you only receive one offer from Advanced Technology Solutions (ATS).

You contact ATS and they are willing to provide quantities, dates of sale, discounts offered, and prices offered to their other customers.

What analysis of ATS' offer should you use?

- ☐ A. Price analysis
- ☐ B. Cost analysis
- ☐ C. Cost realism analysis
- ☐ D. Price realism analysis

[Check Answer](#)

User Instructions: Select the correct answer.

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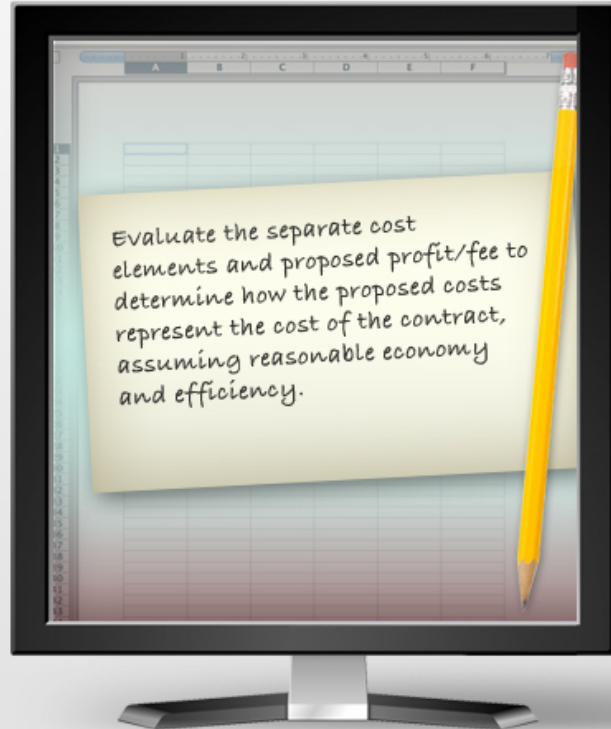
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Cost Analysis Considerations

What is cost analysis?

Cost analysis is the review and evaluation of the separate cost elements and proposed profit/fee of an offeror's certified cost or pricing data or data other than certified cost or pricing data.

In addition, cost analysis involves the judgmental factors that are applied in projecting from the data to the estimated costs.



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Using Cost Analysis

You **MUST** use cost analysis in the example on the left and you **MAY** use cost analysis in the example on the right:

When the Truth in Negotiations Act (TINA) applies and the offeror is required to submit certified cost or pricing data.

In this situation, the offeror must provide complete, accurate, and current data to support all proposed costs and profit/fee.

OR

When you require an offeror to submit cost data other than certified cost or pricing data to support your decision on price reasonableness or cost realism.

In this situation, require only the information necessary to determine price reasonableness or cost realism.

This may be required, for example, when you are comparing a proposed price to a price previously paid on a similar item. You may need cost information from the contractor to determine the impact, on the price, of the differences between the two items.

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Using Cost Analysis (cont.)

Is cost analysis a substitute for effective price analysis?

No! Cost analysis is not a substitute for effective price analysis. Cost analysis should provide insight into what it will cost the firm to complete the contract using the methods proposed.

However, cost analysis does not necessarily provide a picture of what the market is willing to pay for the product involved. You would need price analysis.



[Select here for an example.](#)



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Using Cost Analysis (cont.)

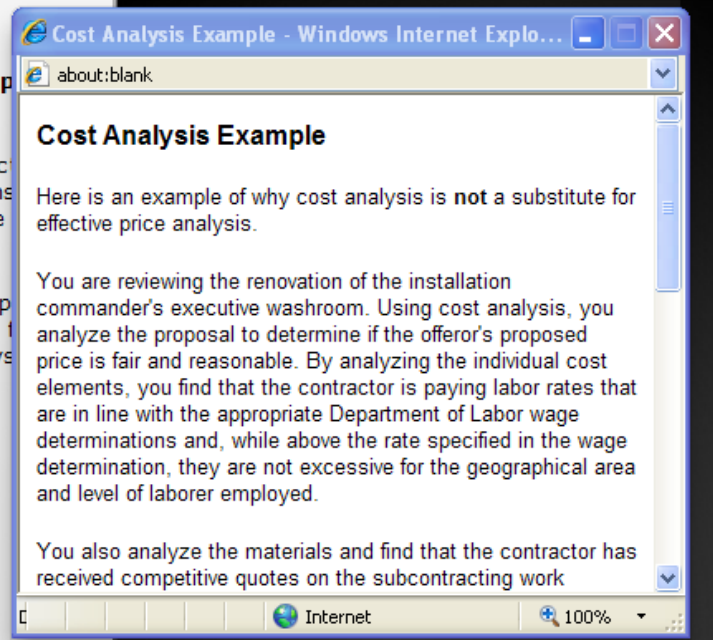
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[Select here for an example.](#)



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Using Cost Analysis (cont.)

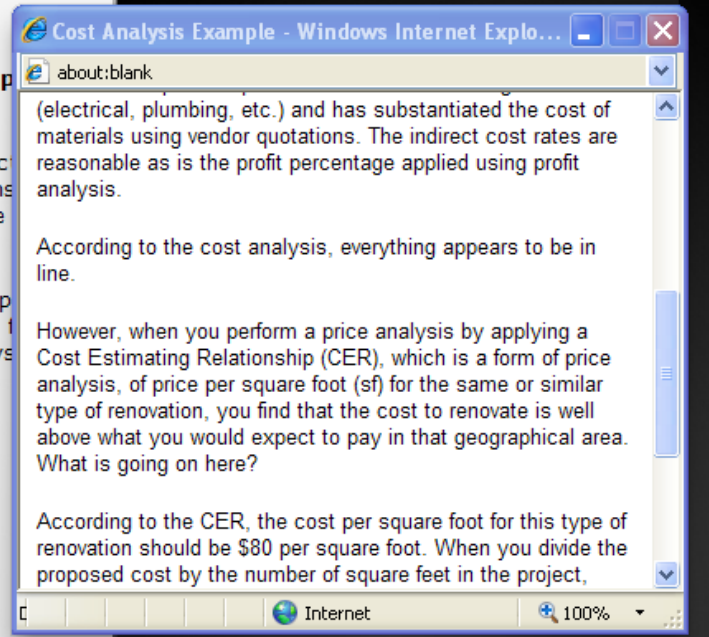
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[Select here for an example.](#)



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Using Cost Analysis (cont.)

Is cost analysis a substitute for effective price analysis?

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However, cost analysis does not necessarily provide a picture of what the market is willing to pay for the product involved. You would need price analysis.

[Select here for an example.](#)

User Instructions: Select Next to continue.

Cost Analysis Example - Windows Internet Explo...

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...type of renovation, you find that the cost to renovate is well above what you would expect to pay in that geographical area. What is going on here?

According to the CER, the cost per square foot for this type of renovation should be \$80 per square foot. When you divide the proposed cost by the number of square feet in the project, however, it is \$120 per square foot. That's a significant difference!

You closely examine the work statement and the labor and materials proposed by the contractor, and you find that the materials proposed — Italian marble, imported travertine tile, teak wood and gold plated bathroom fixtures — are excessive for a government contract using taxpayer dollars.

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Price Analysis Considerations

What is price analysis?

Price analysis is the process of examining and evaluating a proposed price to determine if it is fair and reasonable, without evaluating its separate cost elements and proposed profit. Price analysis may be, when necessary, supplemented by evaluation of cost elements.

You must use price analysis to determine if a price is fair and reasonable when an offeror is not required to provide certified cost or pricing data.

If an offeror is required to provide certified cost or pricing data, use cost analysis, not price analysis, to evaluate the reasonableness of individual cost elements.

While price analysis is not mandatory, it should be used to verify that the overall price is fair and reasonable.

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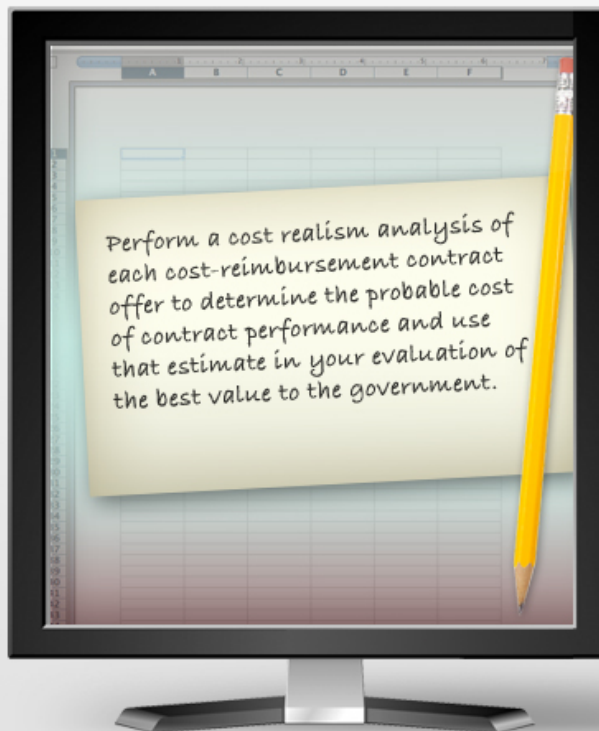
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Cost Realism Analysis

What is cost realism analysis?

Cost realism analysis is the process of independently reviewing and evaluating specific elements of each offeror's proposed cost estimate to determine whether the estimated proposed cost elements:

- Are realistic for the work to be performed
- Reflect a clear understanding of the requirements
- Are consistent with the unique methods of performance and materials described in the offeror's technical proposal



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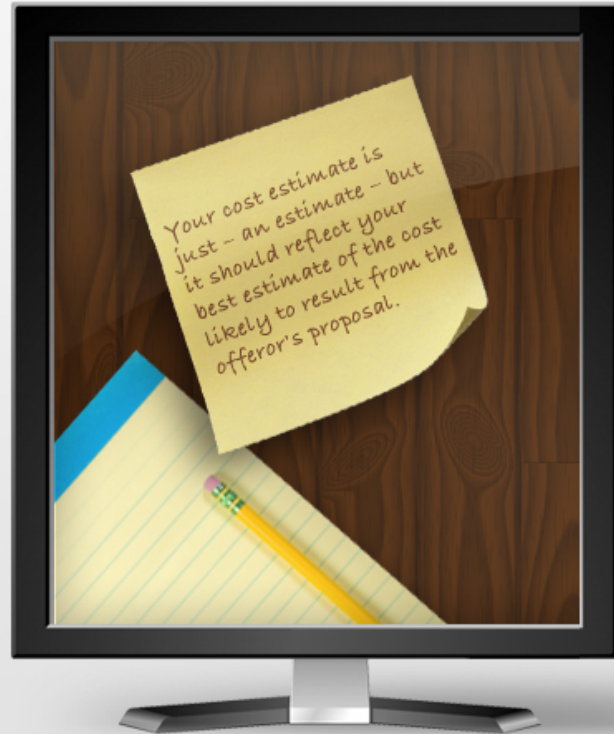
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Cost Realism Analysis (cont.)

One challenge you have as a Contracting Officer is that the probable contract cost may differ substantially from the proposed cost. How, then, are you supposed to determine the probable cost?

The probable cost is determined by adjusting each offeror's proposed cost, and fee when appropriate, to reflect any additions or reductions in cost elements to realistic levels based on the results of the cost realism analysis. Here's an example:

Offeror A proposes a cost of \$2.5 million. Offeror B proposes \$3 million. Your cost realism analysis on offer A, however, shows that the contractor underestimated the labor hours required and cannot perform the work for less than \$3.2 million. Your cost realism analysis on offeror B shows the offer of \$3 million to be realistic. Now you have an idea up front what you would realistically pay for the resulting contracts.

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Cost Realism Analysis (cont.)

Use cost realism analysis when evaluating offers for fixed-price contracts, especially when:

- The new requirements may not be fully understood by competing offerors
- There are quality concerns
- Past experience indicates that contractors' proposed costs have resulted in quality or service shortfalls

Remember that you may use the results of your cost realism analysis in performance risk assessments and responsibility determinations.

Note, however, that proposals must be evaluated using the criteria in the solicitation, and the offered prices must not be adjusted as a result of the analysis.




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REWIND PLAY CAPTIONS


Good morning. I wanted to stop by and provide a little encouragement as we look at cost analysis in more detail.

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I know that some of this information can be a little overwhelming but I know you will catch on quickly.

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A resource I think you should look at is the acquisition plan. It is one of your resources.

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Don't hesitate to call me with any questions.

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Costs and Cost Analysis[Resources](#)[Glossary](#)[Help](#)**Challenge Question #6**

In reviewing the acquisition plan, which form of proposal analysis do you think the Contracting Officer contemplated using prior to soliciting offers?

- ☐ A. Price analysis
- ☐ B. Cost analysis
- ☐ C. Cost realism analysis
- ☐ D. Cost estimating

[Check Answer](#)

User Instructions: Select the correct answer.

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Price Analysis Considerations

What is price analysis?

Price analysis is the process of examining and evaluating a proposed price to determine if it is fair and reasonable, without evaluating its separate cost elements and proposed profit. Price analysis may be, when necessary, supplemented by evaluation of cost elements.

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Techniques for Price Analysis

As stated in [FAR 15.404-1\(b\)](#), price analysis **always** involves some form of comparison with other prices. It is the process of examining and evaluating a proposed price without evaluating the separate cost elements and proposed profit.

The government uses various price analysis techniques and procedures to ensure a fair and reasonable price.


You may be responsible for selecting the techniques for comparison that are used to verify that the overall price that is offered is fair and reasonable.

The next screen describes some of these techniques.

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Is this price fair and reasonable?



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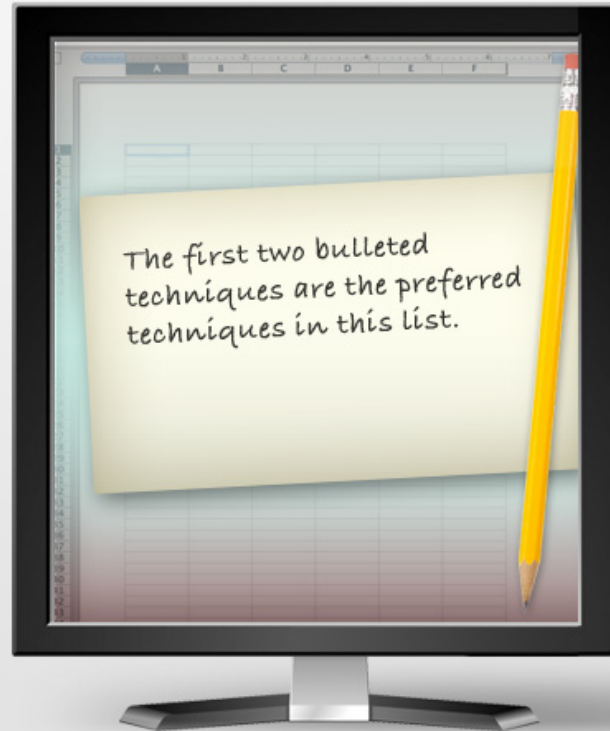
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Techniques for Price Analysis (cont.)

Some of these techniques include:

- Comparison of proposed prices that are received in response to the solicitation
- Comparison of previously proposed prices and previous government and commercial prices with current proposed prices for the same or similar items
- Use of parametric estimates or applications of rough yardsticks
- Comparison with
 - Competitive published price lists
 - Published commodity market prices
 - Similar indexes
 - Discount or rebate arrangements
- Comparison of proposed prices with independent government cost estimates
- Comparison of proposed prices obtained through market research
- Analysis of pricing information provided by the offeror



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Techniques for Price Analysis (cont.)

Additional techniques include:

- Comparison of previously proposed prices and previous government and commercial prices with current proposed prices for the same or similar items
- Use of parametric estimates or applications of rough yardsticks
- Comparison with
 - Competitive published price lists
 - Published commodity market prices
 - Similar indexes
 - Discount or rebate arrangements
- Comparison of proposed prices with independent government cost estimates
- Comparison of proposed prices obtained through market research

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Techniques for Price Analysis (cont.)


Some final techniques include:

- Analysis of pricing information provided by the offeror
- Comparison of previously proposed prices and previous government and commercial prices with current proposed prices for the same or similar items
- Use of parametric estimates or applications of rough yardsticks
- Comparison with
 - Competitive published price lists
 - Published commodity market prices
 - Similar indexes
 - Discount or rebate arrangements
- Comparison of proposed prices with independent government cost estimates
- Comparison of proposed prices obtained through market research
- Analysis of pricing information provided by the offeror

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What type of pricing information does the offeror provide?

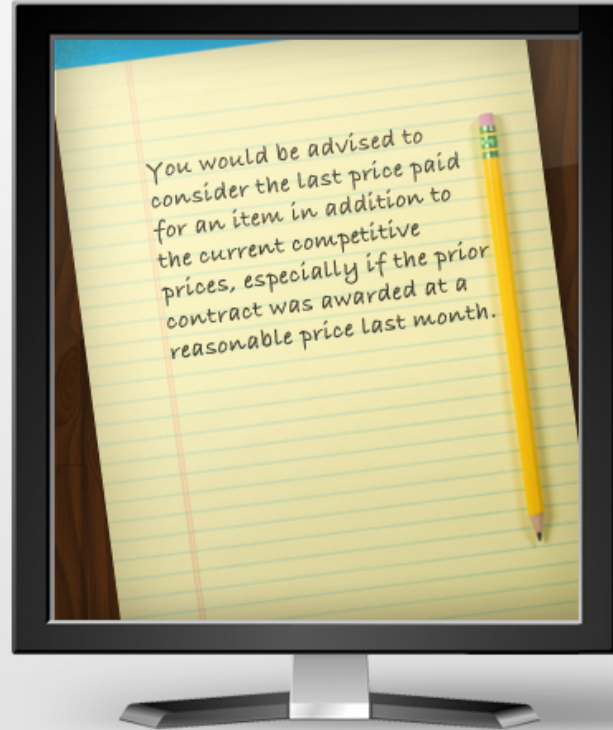
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Techniques for Price Analysis (cont.)

Remember these important points about techniques:

1. Comparisons with commercial catalog, market, or regulated prices can be just as desirable as comparisons with competitive offers. Prices of commercial products are defined by commercial market competition.
2. Independent government estimates are normally considered to be the least desirable comparison base for price analysis. In some cases, however, like construction, where the estimates are based on extensive detailed analysis of requirements and the market, the government estimate can be one of the best bases for cost analysis.
3. You should use all bases for which you have recent, reliable, and valid data.

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Evaluation and Documentation

Price analysis is a subjective evaluation. With any procurement, different bases for price analysis may give you a different view of price reasonableness.

Different buyers/contracting officers might make different decisions about price reasonableness even though they are reviewing the same information.

It is the cognizant contracting officer who must be satisfied that the price is fair and reasonable.

Remember to document the rationale you used in making the pricing decision. Otherwise, any individual who may review your file may not know or understand the factors that affected your decision.



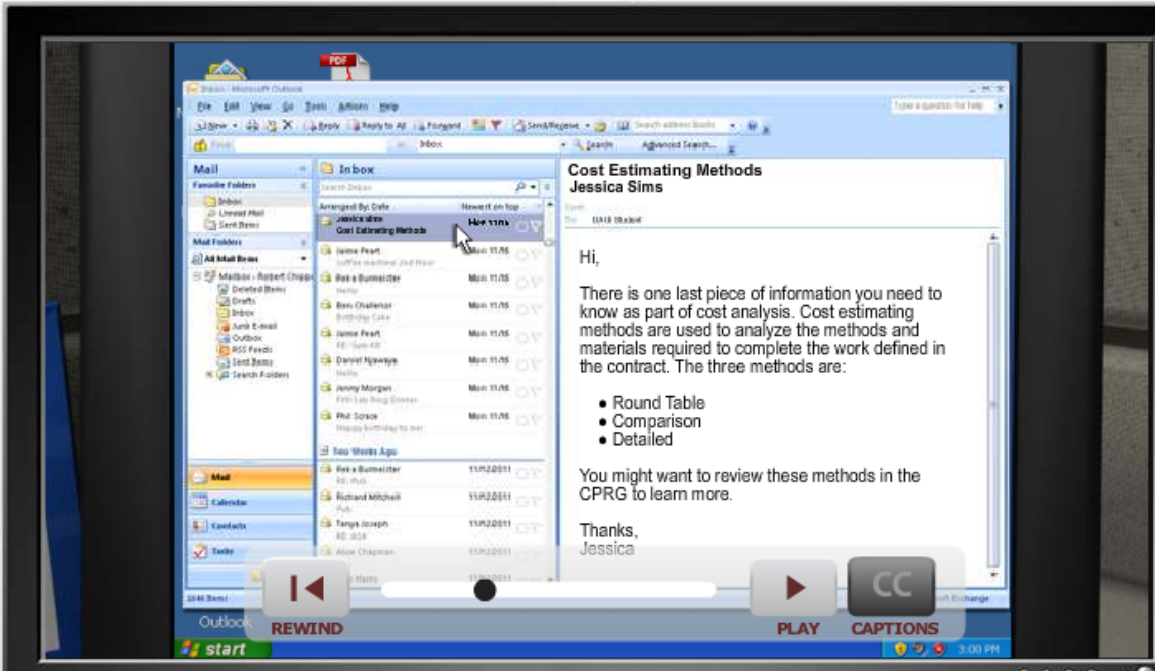
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The screenshot shows a video player interface. The main content is a screenshot of a Microsoft Outlook inbox. The inbox is titled 'Inbox' and shows a list of emails. The email 'Cost Estimating Methods' from Jessica Sims is selected. The email content is displayed on the right side of the Outlook window. The video player has a progress bar at the bottom with a play button and a 'CAPTIONS' button. The video player is set to 'PLAY' mode.

Cost Estimating Methods
Jessica Sims

Hi,

There is one last piece of information you need to know as part of cost analysis. Cost estimating methods are used to analyze the methods and materials required to complete the work defined in the contract. The three methods are:

- Round Table
- Comparison
- Detailed

You might want to review these methods in the CPRG to learn more.

Thanks,
Jessica

REWIND PLAY CAPTIONS

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Cost Estimating Methods
Jessica Sims

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Thanks,
Jessica

Cost estimating methods are used to analyze the methods and materials required to complete the work defined in the contract.

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The screenshot shows a video player interface. The main content is a screenshot of a Microsoft Outlook inbox. The inbox list shows several emails, with the top one titled "Cost Estimating Methods" from Jessica Sims. The email content is visible on the right side of the Outlook window. The video player has a progress bar at the bottom with a play button, a pause button, and a captions button. The text "REWIND", "PAUSE", and "CAPTIONS" are visible below the progress bar.

Cost Estimating Methods
Jessica Sims

Hi,

There is one last piece of information you need to know as part of cost analysis. Cost estimating methods are used to analyze the methods and materials required to complete the work defined in the contract. The three methods are:

- Round Table
- Comparison
- Detailed

You might want to review these methods in the CPRG to learn more.

Thanks,
Jessica

The three methods are: Round Table, Comparison, and Detailed. You might want to review these methods in the CPRG to learn more. Thanks, Jessica.

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Challenge Question #7

Which of the following estimating methods produces estimates based on an analysis of the methods and materials required to complete each element of the work required by the contract?

- ☐ A. Round Table
- ☐ B. Comparison
- ☐ C. Detailed
- ☐ D. Standard

Check Answer



User Instructions: Select the correct answer.

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Cost Estimating Methods

The contractor's cost accounting system provides the data required for cost estimating purposes. However, there is more than one method for estimating costs. **Which method should the offeror choose?**

In general, an offeror may use any generally accepted estimating method that is **equitable** and **consistently applied**.

Select each image to the right to learn more.



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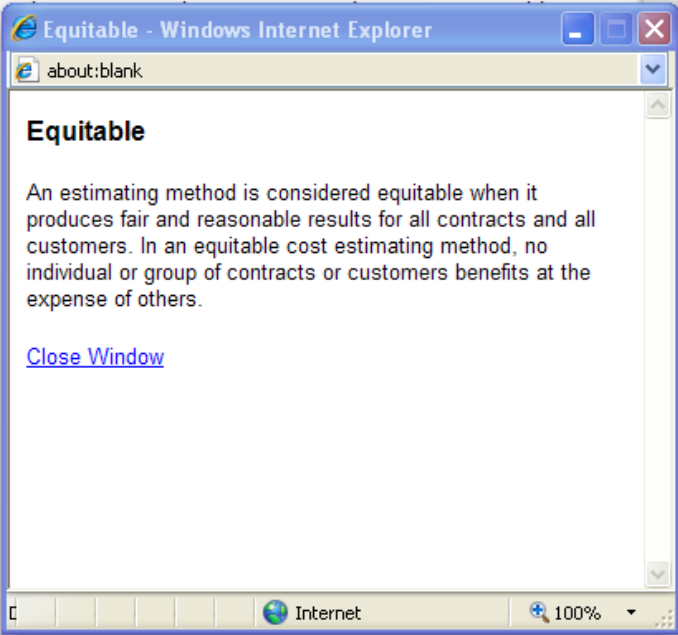
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Cost Estimating Methods



Equitable

An estimating method is considered equitable when it produces fair and reasonable results for all contracts and all customers. In an equitable cost estimating method, no individual or group of contracts or customers benefits at the expense of others.

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Cost Estimating Methods



Consistently Applied

A consistently applied cost estimating method is applied in similar estimating situations for all contracts and all customers of the firm. However, different estimating methods may be applied in different estimating situations. Differences may be related to such factors as:

- The relative dollar value of the estimate
- The firm's competitive position
- The definition of contract requirements
- The availability of cost information applicable to the same or a similar product/service.

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Equitable

Consistently Applied

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Cost Estimating Methods (cont.)

There are many methods for estimating costs in an equitable and consistently applied way. Some cost estimating texts identify ten or more! The most common classification identifies three methods: **round-table**, **comparison**, and **detailed**.

Select each image below to learn more about these three cost estimating methods.



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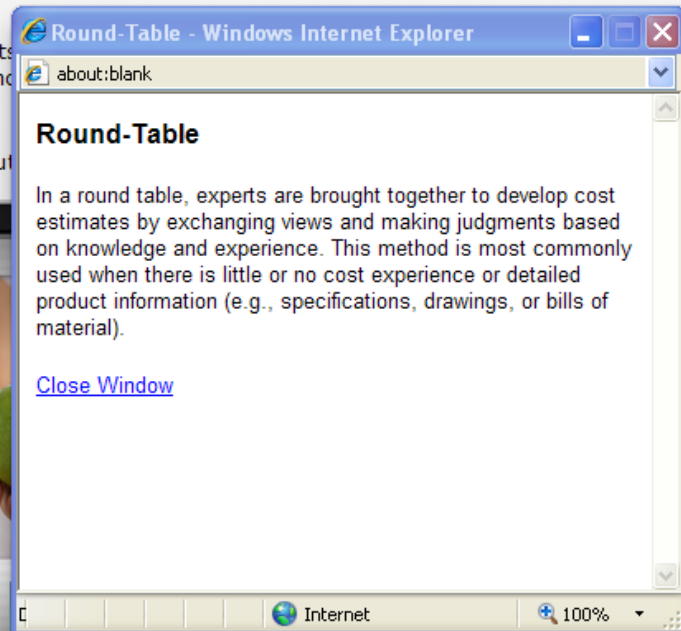
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Cost Estimating Methods (cont.)

There are many methods for estimating costs. The following texts identify ten or more! The methods are: **table**, **comparison**, and **detailed**.

Select each image below to learn more about



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Cost Estimating Methods (cont.)

There are many methods of cost estimating. Some cost estimating texts identify three methods: **round-**

Select each image below.

**ROUND**

**DETAILED**

Comparison

With the comparison method, costs for a new item are estimated using comparisons with the cost of completing similar tasks under past or current contracts. Any differences are isolated and cost elements applicable to the differences are deleted from or added to experienced costs. Comparisons may be made at the cost element level or total price level. Adjustments may also be made for possible upward or downward cost trends.

This method is most commonly used when specifications for the item being estimated are similar to other items already produced or currently in production and for which actual cost experience is available.

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Cost Estimating Methods (cont.)

There are three cost estimating methods. The most consistently applied way. Some cost estimating methods identify three methods: **round-**

Select

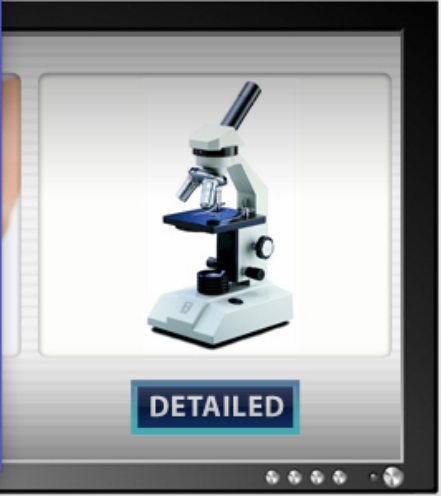
Detailed

The detailed method is characterized by a thorough review of all components, processes, and assemblies. It requires detailed information to arrive at estimated costs and typically uses cost data derived from the accounting system, adjunct statistical records, and other sources.

This method is most commonly used when the required information is available and future production potential warrants the cost of the detailed analysis required. It is the most accurate of the three methods for estimating direct cost. As you can imagine, it is also the most time consuming and expensive.

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estimating methods.



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Costs and Cost Analysis[Resources](#)[Glossary](#)[Help](#)**Cost Estimating Methods - Comparison**

The following table compares the three methods of cost estimating you just learned.

	Round-Table	Comparison*	Detailed
Relative Accuracy	Low — limited data are used	Moderate/High — depends on data, technique, and estimator	High — based on engineering principles
Relative Estimator Consistency	Low — different experts make different judgments	Moderate/High — depends on data, technique, and estimator	High — based on uniform principle application
Relative Development Speed	Fast — little detailed analysis required	Moderately Fast — especially with repetitive use	Slow — requires detailed design and analysis
Relative Estimate Development Cost	Low — fast development and limited data requirements allow low development cost	Moderate — depending on the need for data collection and analysis	High — detailed work design and analysis require time and increase cost
Relative Data Requirements	Low — based on expert judgment	Moderate — only requires historical data	High — requires detailed work design and analysis

*Warning: The comparison cost estimating method can project continuation of nonrecurring costs and cost inefficiencies experienced in past work.

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Combination Estimates

There is no one estimating method that is best in all situations.

In fact, most cost proposals will include different estimates made using different methods. All three methods may be used in the same proposal! Different methods may even be used as a cross-check in estimating a single cost element.

For example, let's say you are contracting for a unique research and development project. The offeror may use round-table estimates for many cost elements because similar research has never been conducted before.

However, the offeror may also use comparison estimates for other cost elements based on the costs incurred under other research and development contracts.

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Costs and Cost Analysis

Estimating Methods and Cost Analysis

So far we have discussed the cost estimating methods an offeror can use. Can you apply these cost estimating methods to your cost analysis? Yes!

Whenever you perform a cost analysis, consider the strengths and weaknesses of the estimating method used by the offeror in preparing the proposal.

You are not limited to using the method used by the offeror in developing their proposal. You can use any method that appears appropriate under the circumstances.

Select each page number at the bottom of the graphic to the right to learn more about the Round-Table, Comparison, and Detailed estimating methods and their corresponding strengths and weaknesses.

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Estimating Methods	Key Strengths/Weaknesses
Round-Table	Strength: Can be used with limited data
	Weakness: Lack of data increases variability between estimators and true costs

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Costs and Cost Analysis

Estimating Methods and Cost Analysis

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Estimating Methods	Key Strengths/Weaknesses
Comparison	Strength: Rapid development of estimates based on historical costs
	Weakness: Estimated based on historical costs can project historical inefficiencies

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Estimating Methods and Cost Analysis

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Estimating Methods	Key Strengths/Weaknesses
Detailed	Strength: Most accurate estimate
	Weakness: Requires complete information that may be expensive or impossible to obtain

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Summary

Congratulations! You have completed this module that discussed contract costs and cost analysis.

Review the graphic on the right to see the key points for this module.



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Summary (cont.)

Now that you have completed this module, you should be able to:

- Identify the fundamentals of cost analysis
- Distinguish between cost analysis, price analysis and cost realism analysis
- Identify cost analysis terms and techniques used when developing a prenegotiation position



User Instructions: Select the next module from the Table of Contents to continue.

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