

GAO Highlights

Highlights of [GAO-13-566](#), a report to congressional committees

Why GAO Did This Study

Since the 1990s, federal law has placed a limitation, or cap, on the amount of employee compensation that contractors can charge to federal contracts. The cap increased by 63 percent in real terms since first use of the current approach in 1998. The cap was set at \$693,951 in 2010 and \$763,029 for 2011 and 2012.

The National Defense Authorization Act for Fiscal Year 2013 directed GAO to provide information on the effect of reducing the cap to the salary of the U.S. President or Vice President. GAO identified, among other things, (1) estimates of the number of employees of a sample of DOD contractors whose compensation would have exceeded a cap set at the salaries of either the U.S. President or Vice President and the amount of compensation that would not have been allowable and (2) the views of government and contractor representatives on potential effects of a reduction in the cap. GAO collected data from a nongeneralizable, stratified random sample of 10 large-tier, 10 mid-tier, and 10 small-tier contractors; reviewed relevant laws and regulations, and interviewed government and contractor representatives. Data on the number of employees affected by the cap was received from 27 of the 30 contractors; the three largest contractors in GAO's sample did not provide these data.

GAO is not making any recommendations in this report. DOD and OMB commented on a draft, noting the need to pay reasonable compensation costs. DOD also cited the need for more research given GAO's sample size. GAO believes this analysis provides valuable insights into potential effects of cap changes.

View [GAO-13-566](#). For more information, contact Timothy J. DiNapoli at (202) 512-4841 or tinapoli@gao.gov.

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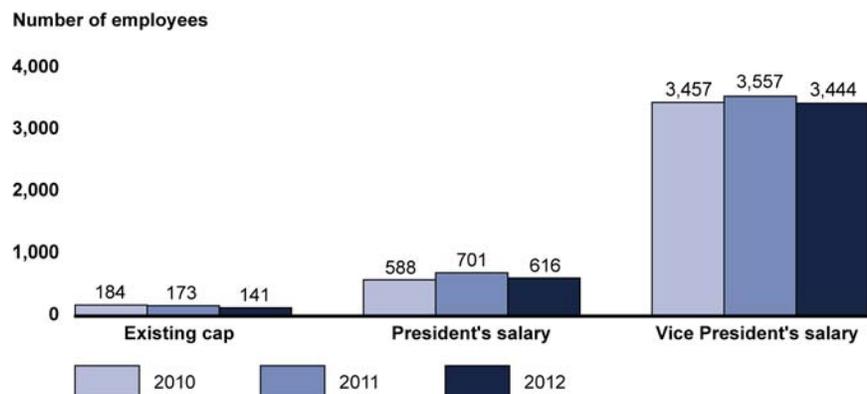
DEFENSE CONTRACTORS

Information on the Impact of Reducing the Cap on Employee Compensation Costs

What GAO Found

Reducing the cap to the President's salary (\$400,000) or the Vice President's salary (\$230,700) would have substantially increased the number of employees with compensation costs exceeding the cap in 2010-2012 (see figure).

Estimated Number of Employees with Compensation Costs in Excess of Each Cap Level for 27 of the 30 Contractors Sampled Who Provided Data



Source: GAO analysis of contractor-supplied data.

For 2010-2012, contractors identified over \$180 million per year in compensation costs that would have exceeded a cap set at the President's salary, and at least \$440 million per year if set at the Vice President's salary. Most affected employees were at large-tier companies; few small-tier companies had employees exceeding these caps. While employees with compensation costs in excess of the existing cap were all identified as executives by the contractors, reducing the cap would have increasingly affected compensation costs for individuals below the executive level.

Government representatives generally supported reducing the cap as a means to reduce the costs of Department of Defense (DOD) contracts, whereas industry representatives and most contractors identified negative effects that could result from reducing the cap. The Office of Management and Budget noted the growth in the cap has outpaced inflation and the rate of growth of federal salaries. DOD noted that it fully supported the principle of paying only reasonable compensation costs and some DOD officials supported reducing the cap, though DOD cautioned that there are limited data on the potential impacts of doing so and that the impact on the defense industry would need to be carefully monitored and assessed. Industry associations and contractors representatives noted that the compensation they offer to their employees is generally based on market surveys of compensation paid by private sector companies. While acknowledging that a reduced cap would not preclude them from compensating their employees above the cap, contractor representatives noted that doing so would come at the expense of company profits, which in turn may result in challenges in attracting capital from the financial markets. They also noted that reducing the cap may affect companies' ability to attract and retain top talent and, over the long term, lead companies to reassess their business and staffing models and potentially shift work or personnel from government business to their commercial sector.