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**STATEMENT BY
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**BEFORE THE
Senate Committee on the Budget
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Chairman Conrad, Ranking Member Gregg, Senator Warner, Senator Bunning, and Members of the Committee and Task Force on Government Performance: My name is Shay Assad and I am the Director of Defense Procurement and Acquisition Policy. I am also presently performing the duties of the Assistant Secretary of Defense for Acquisition, in the Office of the Under Secretary of Defense for Acquisition, Technology, and Logistics (AT&L).

After serving tours on board two Navy destroyers, I began my career in acquisition thirty-two years ago as a Naval Procurement Officer at the Naval Sea Systems Command. I left the Navy in 1978 and joined the Raytheon Company. Over my twenty-two year career at Raytheon I held a variety of contracting and operational positions ultimately serving as a Corporate Vice President, a Corporate Senior Vice President, and finally, as Corporate Executive Vice President and Chairman and Chief Executive Officer of one of its major subsidiaries. I retired from Raytheon in July 2000.

In 2004, I entered Government service as the senior civilian contracting official for the U.S. Marine Corps. In April 2006, I was selected to serve as the Director of Defense Procurement and Acquisition Policy.

Thank you for your invitation to appear before you today. The subject of today's hearing, "Responsible Contracting: Modernizing the Business of Government," is a matter that is one of Secretary Gates' highest priorities. He recently directed all echelons of the Department to take a "hard, unsparing look" at how we operate with the goal of cutting overhead costs to transfer those savings to force structure and modernization within the programmed budget. Just over two weeks ago, the Under Secretary of Defense for

Acquisition, Technology and Logistics, directed all DoD acquisition professionals to find ways to improve the way we conduct business in order to deliver better value to the taxpayer for the goods and services we acquire for our warfighters. Today, I will take this opportunity to outline how we intend to implement this direction.

First, as stated by Dr. Carter we should distinguish the present challenge of delivering better value from the concept of “acquisition reform.” Whereas acquisition reform has entailed a re-examination of acquisition processes, achieving better value through efficiency will require us to focus on execution and specific outcomes. The desired outcome is to find and realize more than \$100 billion in savings over the next five fiscal years starting in FY12. The objective of realizing better value in no way denigrates efforts that have been made and are being made to revise and improve our acquisition policies, such as implementation of the Weapon System Acquisition Reform Act last year; however, this different.

This efficiencies initiative is really about doing all we can do to make sure every dollar counts. In directing us to re-examine every aspect of how we do business, Secretary Gates has told us we must ask two questions. “First, is this respectful of the American taxpayer at a time of economic and fiscal duress? And second, is this activity or arrangement the best use of limited dollars given the pressing needs to take care of our people, win the wars we are in, and invest in the capabilities necessary to deal with the most likely and lethal future threats?” We recognize that the nation is at somewhat of a crossroads having devoted a significant amount of resources over the past decade toward defense spending. While it is our expectation that the Congress will continue to appropriate

sufficient funds for the defense budget, we are committed to root out inefficiencies so that we are able to attain two to three percent net annual growth in warfighting capabilities without a mirrored budget increase. We will seek to identify those unproductive or low-value-added overhead expenses that have prevented us from realizing optimal value for our nation.

Over the past two years, with Secretary Gates' unwavering leadership, over 30 difficult choices have been made to cancel or curtail major weapon system programs that were either performing poorly or simply exceeded our practical needs. While the Secretary will continue to challenge efforts to retain or restore funding for poor performing programs and unneeded systems, this efficiencies initiative requires us to look within the remaining programs and activities. In other words, we need to examine not only what we are acquiring, but also how we are acquiring these activities and programs. I realize American citizens would hear this and say, well of course, that's what we expect you to do. With that in mind, I will now expound upon the kinds of costs we expect to trim in order to realize this two to three percent net annual growth in warfighting capabilities and do more without more.

Nearly \$400 billion of the Department's annual budget is spent on contracts to acquire combat capability in the form of both goods and services. The business arrangements involved with over three and one-half million annual contract actions that execute these funds are primary focal points for this initiative. Each of these arrangements entails necessary and not so necessary overhead expenses on both the government and industry side.

Primarily, we will look prospectively at new contracts. We recognize that securing the desired amount of savings will take time. We seek to restore affordability of the goods and services we acquire. We are engaging senior leaders from the defense industry to help us understand where and how we can enhance and incentivize their efficiency and productivity.

Specifically, there are a number of actions we can and must take to infuse incentive arrangements into our contracts and motivate industry to achieve greater efficiency. We expect to reap the benefits of that efficiency as industry will share savings with the Government. While none of these emphasis areas are new per se, the difference now is a concerted push to adopt these practices across the Department. First, and at the core of all successful procurement in both the government and commercial sectors, is the unmatched value that is achieved when we leverage real competition. We pay a dear price for early program decisions that set us on a path to acquire goods or services from a single supplier or a directed source. There are actions we can take to avoid such situations. For example, we must maximize the use of technical data packages and open systems architecture to foster an environment that is favorable for future competitions. Recognizing the proliferation of multiple award indefinite quantity/indefinite delivery (IDIQ) contracts, we are beginning to more closely examine the extent to which these arrangements have yielded true competition for individual task or delivery orders amongst the contractors that hold these IDIQ contracts. We can and are emphasizing acquisition strategies that formulate service contract requirement sets into mission areas to improve the opportunities for meaningful competition throughout the course of the IDIQ contracts' period of performance.

Inside and outside the Department, there has been a significant degree of scrutiny placed on our utilization of the proper contract type for a given effort. There is no “one size fits all” solution and we will continue to use the various contract types as appropriate for each situation. Over the past two years, we have generally discouraged new cost plus award fee (CPAF) contracts because we have found that objective incentive arrangements enable us to better align contractor profitability with outcomes in the form of contractor-delivered accomplishments. We will restrict the use of pure award fee contracts to those situations where objective measures do not exist. We will seek authority from the Congress to employ multi-year contracts when significant savings are possible. We are working to reduce the backlog of undefinitized contracts and re-emphasize the fact that we get a better deal when we prospectively price and negotiate our contracts as opposed to authorizing work and postponing agreement on price. For system development and procurement contracts, we will look to structure contracts that require Government and industry to share equally in overruns and underruns (with overruns having analytically based ceilings). Although we will examine each and every opportunity to open up a requirement for competition, the reality is that a significant proportion of defense spending will be allocated to follow-on acquisitions of existing weapon systems in a “sole source” mode. Managing that requires adjustments to account for actual realized costs experienced under prior production lots. Such a searching examination must take place at all tiers (prime and subcontract). I am personally leading all the peer reviews for sole source contract awards valued at \$1 billion or more and I am directing contracting officers to obtain and utilize actual cost histories from all major suppliers when forming pre-negotiation objectives. This is an area that is

particularly ripe to achieve a significant amount of savings that will translate to enhanced buying power for the Department. The Government must do more to incentivize prime contractors to manage their subcontractors and reduce prime and subcontractor overhead costs.

We are certainly mindful of the fact that the Department spends more than 50 percent of its contracted dollars on a variety of support services which enable us to project power and sustain our warfighters. To acquire such services, we are essentially phasing out the use of time and materials (T&M) contracts because they lack cost controls and have often led to situations in which contractors have realized unconscionable actual profit rates. With the help of legislation from the Congress, we are significantly curtailing the use of single source IDIQ service contracts in favor of multiple-source, continuously competitive contracts.

Our structured method of computing objective profit and fee for contract negotiations entails a series of calculations we call the “weighted guidelines.” The policy behind the computation of objective profit and fee was developed during a time in which the prime to subcontractor ratio of work and associated allocation of risk was very different than we typically see today. Most major procurements for systems entail a far greater degree of effort that is subcontracted than in the past. We intend to re-examine that calculus to ensure we are recognizing risk and rewarding higher productivity with higher profits. We need a system that enables us to incentivize contractors to innovate. At the same time, we need to appropriately acknowledge the value contractors receive from improved cash flow. Additionally, we intend to challenge industry to reduce the gap we all too frequently see between proposed and actual rates in forward pricing rate agreements. We need to ensure

our contracting officers are anchoring their price fair and reasonable determinations on meaningful rate agreements.

In seeking inefficiencies to eliminate, we will look to target non-value added contract costs such as certain expenses in a contractor's general and administrative (G&A) cost pool or non-value added overhead expenses. We must act to curb the exorbitant costs we often pay contractors to prepare complex proposals for those systems we are acquiring on a sole source basis.

The Navy has established a pilot program to reward those suppliers with a proven and consistent track record of excellence. We will monitor that pilot closely and determine if it can be emulated at the Department level.

Finally with respect to initiatives relating to industry, we will look to maximize opportunities to tap into the efficiency, creativity and agility that are the hallmarks of small business suppliers. Particularly in the services sector, we will continue to influence up front acquisition strategies to carve out specific and appropriate mission segments to provide for small business participation.

In addition to those efficiencies that can be realized by incentivizing and influencing industry, there are a number of practices the Department's acquisition professionals must utilize to improve our own efficiency. Last year, Secretary Gates charted us on a path to restore the capability of the acquisition workforce. We will continue to augment our capacity and increase our skills to deliver value to the warfighter while at the same time leveraging the unique qualities that the non-profit federally funded research and

development centers (FFRDCs) and university affiliated research centers (UARCs) bring to bear.

Before embarking on new programs, we must first consider affordability. To the extent we have to shape requirements and designs to align to affordable programs, we will do so. The Department must adopt a mindset for managing programs to cost objectives based on “should cost” estimates. At the same time, our recent emphasis on restoring the organic government cost analyst capability within the Department will enable us to use historically-based independent cost estimates as “will cost” to inform the management of “should cost” estimates. Similarly, we must work to improve the consistency and quality of government audits that are used to support contracting officers preparing for contract negotiations. At the same time, we recognize the need to direct limited audit resources on those areas that will provide the most value added results.

Organizationally, the Department can achieve efficiencies by eliminating some of the redundancies within its warfighting portfolios to leverage those situations where similar programs are pursuing similar objectives. For acquisition of services, DoD components should look to emulate to some extent the model the Air Force has employed to manage and oversee that broad spectrum of contracts. Finally, in the research and development arena, the Department’s acquisition professionals can do more to protect the future by sustaining investment while focusing on high value-added work.

In the coming months, the Under Secretary of Defense for Acquisition, Technology and Logistics will issue final guidance to implement this initiative. I will conclude by stating that there is a significant opportunity for savings but the savings will only be realized

if we have a well-trained and sufficient workforce to implement the kind of change that is necessary. In that regard, I know I speak for the entire DoD acquisition workforce in expressing my gratitude to Secretary Gates, Deputy Secretary Lynn, Dr. Carter and the Congress in supporting the much needed growth and increased capability of our workforce. I thank you for this opportunity and I welcome your questions.