

# Issue Brief for Congress

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## **Defense Acquisition Reform: Status and Current Issues**

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## Defense Acquisition Reform: Status and Current Issues

### SUMMARY

The end of the Cold War and its impact on defense spending has created a strong need to reform Department of Defense's (DOD) acquisition system. With procurement spending down, DOD expects to depend on savings from acquisition reform to help finance future force modernization. Policymakers believe that DOD should use more commercial products because, in many instances, they cost less and their quality is comparable to products built according to DOD military specifications. Many such reform proposals are based on recognition that DOD regulatory barriers and a Cold War acquisition "culture" have inhibited the introduction of commercial products.

The need to encourage greater interaction between the defense and commercial industries is considered vital to keeping U.S. military technology the best in the world — a major objective of U.S. defense policy. Many high-technology commercial products (e.g., electronics) are state-of-the-art and changing so fast that DOD's military specifications, or "milspecs," system cannot keep pace. Congress has passed several important reforms, among them the Federal Acquisition Streamlining Act of 1994, Federal Acquisition Reform Act of 1996, Defense Reform Act of 1997, and the Federal Activities Inventory Reform Act of 1998. DOD has lowered or abolished regulatory barriers; experts agree, however, that more work is required to make the system responsive to U.S. defense needs.

*Restructuring DOD's acquisition organization:* Enacted reforms will mean greater freedom to innovate, make quicker decisions, and improve DOD program development — running DOD more like a private

sector operation. At issue is just how to change DOD personnel management policies, and introduce DOD's acquisition reform initiatives to the private sector.

*Privatizing DOD's functions through outsourcing:* Although DOD had begun outsourcing some functions, expanding its use has been a major goal. Success stories and studies estimated that outsourcing could reduce costs and increase efficiency. Basic questions include (1) how much can be saved over the long-term and how will savings be measured; (2) can DOD's structure effectively manage the new outsourcing proposals; (3) do outsourcing proposals go beyond the "proper" limits of DOD's mission to protect U.S. national security; and (4) can outsourcing harm DOD's military readiness or war-fighting capability?

*Oversight of reform initiatives:* Congress will continue to exercise a strong oversight role because of its longtime interest in streamlining DOD's acquisition processes. Its attention will be directed at several congressionally mandated DOD reports on acquisition reform issued in 1996. Important topics will include how DOD is streamlining and restructuring its acquisition processes, practices and infrastructure; increasing efficiencies in acquiring defense maintenance and repair services; and outsourcing DOD support functions that are considered commercial in nature. Congress will rely on the recommendations of several reports, including the Task Force on Defense Reform, Defense Science Board Task Force on Procurement Reform, and the Section 912 (c) report on streamlining acquisition processes, workforce and infrastructure.

## **MOST RECENT DEVELOPMENTS**

*The Floyd Spence National Defense Authorization Act for 2001, P.L. 106-398, directed the Comptroller General to convene a panel to study the process used by the federal government to make sourcing decisions and report to Congress by May 1, 2002.<sup>1</sup> The Commercial Activities Panel, chaired by the Comptroller General, was comprised of representatives from DOD, OMB, federal labor organizations, and private industry. The mission of the Panel was “to improve the current sourcing framework and processes so that they reflect a balance among taxpayer interests, government needs, employee rights, and contractor concerns.”*

*On May 1, 2002, the Commercial Activities Panel released its final report. The report has four recommendations: 1) Adopt ten sourcing principles as a benchmark against which to measure sourcing decisions; 2) Abolish OMB Circular A-76 and replace it with an “integrated competition process” that combines elements of the Circular with the Federal Acquisition Regulations (FAR)<sup>2</sup>; 3) Implement limited changes to the Circular that do not require legislation; and 4) Develop federal agencies into “high-performing organizations” (HPOs). Adoption of the Panel recommendations for DOD competitive sourcing policy would require that Congress repeal 10 U.S.C. 2462, which requires DOD to make contracting decisions based on lowest cost, not best value.*

## **BACKGROUND AND ANALYSIS**

Since the late 1980s, a number of important factors have converged to create a strong need to reform DOD’s acquisition system, a system that has been periodically studied, and altered, over the last 50 years. First, defense procurement spending has declined every year since 1987. This decline has forced policymakers to examine how DOD buys military equipment, and look for ways to reduce costs in DOD’s acquisition system. Second, there has been a realization that more commercial products should be used by DOD. These products, in many cases, are now cheaper and of comparable quality to similar products produced according to DOD’s military specifications (“milspecs”). Indeed, many high-technology commercial products, particularly in the electronics industry, are state-of-the-art, and they are changing so fast that DOD’s milspec system cannot keep pace with private sector advancements. Third, it has become common knowledge that DOD’s regulatory barriers and its acquisition culture have not only resulted in higher costs, but also kept commercial products from being used in the defense sector. As a result, policymakers are now seeking to make DOD’s acquisition system more (1) cost effective; (2) interactive with commercial industries; and (3) committed to procuring state-of-the-art technology for DOD weapon systems on a timely basis.

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<sup>1</sup> Public Law 106-398; see Section 832 at [<http://www.gao.gov/A76panel/sec832.html>].

<sup>2</sup> Federal procurement policy is defined in the Federal Acquisition Regulation system, more commonly referred to as the FAR. DOD’s procurement rules are defined in the Defense FAR, or DFAR.

Policymakers have faced difficulty revamping a DOD acquisition system; however, the budgetary need to do so has become more and more apparent. Former Secretary of Defense Perry had stated that DOD was depending on substantial savings from acquisition reform to finance a significant portion of future force modernization. In this regard, he had expressed the importance of achieving greater integration of defense and commercial industries, as this was the only way the United States can maintain its technological leadership — a major element of U.S. defense policy.

Over the last 7 years, Congress has enacted a number of important reforms in the acquisition process. DOD has taken steps of its own to reduce or eliminate regulatory barriers, as well as to encourage use of commercial products in military systems. In the view of many experts, however, a great deal more work will be needed in the future to achieve the efficiency and responsiveness required of DOD's acquisition process.

## **DOD Acquisition Strategy for the New Era**

The end of the Cold War produced a significant decline in U.S. defense spending, particularly in the acquisition of weapon systems. Procurement spending has declined 59% in real terms from FY1987 to FY1997. The decline in DOD procurement spending during the Bush Administration resulted in termination of some major weapon programs. It also prompted development of a new acquisition policy, refined by the Clinton Administration, that emphasized upgrading existing systems rather than initiating new ones. The new policy also supported more spending for defense research and development (R&D) and less for weapons production. The logic of the decision was that, although there would be a reduction in the quantity of new weapons produced, the need to maintain technological superiority, (a key combat multiplier), required increased efforts to develop new and innovative technology. DOD also began altering the way it did business with the defense industry, looking for ways to reduce costs. U.S. companies embarked on a variety of strategies to adjust to the new spending environment and the inevitable consolidation of the defense industry.

**Table 1** lists national defense budget outlays, FY1962-2002. The outlay deflators represent the inflation factor; the "CY\$" are current year dollars and are based on the cost of goods and services in terms of prices current at the time of purchase; constant dollars in the third column refer to the cost of goods or services adjusted to eliminate the effect of inflation.

Another change in DOD procurement policy included increased interaction between the defense industry and commercial, non-defense industries. Due to the plight of the defense industry (increasingly affected by cutbacks), the 102nd Congress initiated a defense economic adjustment program that included funding for commercializing military technology. This program was designed to help U.S. defense companies diversify their operations; firms were encouraged to produce so-called "dual-use" products that could also be sold in the commercial sector. It also included incentives for DOD to form partnerships with industry to develop cutting edge, dual-use technology that would be mutually beneficial. In 1993, the Clinton Administration proposed additional initiatives; the 103rd Congress supported and expanded them to help with the defense transition. These initiatives promoted highly-skilled jobs in non-defense and dual-use technology areas, commercial-military interaction, and conversion opportunities to invest in new civilian technology.

**Table 1. DOD Procurement, FY1962 - FY2002**

| Year | Outlays, Deflators<br>FY1998 Base | Outlays<br>(CY\$ in millions) |        | Outlays<br>(FY1998 \$ in millions) |        |
|------|-----------------------------------|-------------------------------|--------|------------------------------------|--------|
|      |                                   | Proc.                         | RDT&E  | Proc.                              | RDT&E  |
| 1962 | 0.1601                            | 14,532                        | 6,319  | 90,768                             | 39,469 |
| 1963 | 0.1612                            | 16,632                        | 6,376  | 103,176                            | 39,553 |
| 1964 | 0.1671                            | 15,351                        | 7,021  | 91,867                             | 42,017 |
| 1965 | 0.1700                            | 11,839                        | 6,236  | 69,641                             | 36,682 |
| 1966 | 0.1816                            | 14,339                        | 6,259  | 78,959                             | 34,466 |
| 1967 | 0.1921                            | 19,012                        | 7,160  | 98,969                             | 37,272 |
| 1968 | 0.2016                            | 23,283                        | 7,747  | 115,491                            | 38,428 |
| 1969 | 0.2088                            | 23,988                        | 7,457  | 114,885                            | 35,714 |
| 1970 | 0.2239                            | 21,584                        | 7,166  | 96,400                             | 32,005 |
| 1971 | 0.2376                            | 18,858                        | 7,303  | 79,369                             | 30,737 |
| 1972 | 0.2575                            | 17,131                        | 7,881  | 66,528                             | 30,606 |
| 1973 | 0.2744                            | 15,654                        | 8,157  | 57,048                             | 29,727 |
| 1974 | 0.2964                            | 15,241                        | 8,582  | 51,420                             | 28,954 |
| 1975 | 0.3308                            | 16,042                        | 8,866  | 48,495                             | 26,802 |
| 1976 | 0.3546                            | 15,964                        | 8,923  | 45,020                             | 25,164 |
| 1977 | 0.3810                            | 18,178                        | 9,795  | 47,711                             | 25,709 |
| 1978 | 0.4089                            | 19,976                        | 10,508 | 48,853                             | 25,698 |
| 1979 | 0.4404                            | 25,404                        | 11,152 | 57,684                             | 25,322 |
| 1980 | 0.4938                            | 29,021                        | 13,127 | 58,771                             | 26,584 |
| 1981 | 0.5532                            | 35,191                        | 15,278 | 63,614                             | 27,617 |
| 1982 | 0.6069                            | 43,271                        | 17,729 | 71,298                             | 29,212 |
| 1983 | 0.6343                            | 53,624                        | 20,554 | 84,540                             | 32,404 |
| 1984 | 0.6592                            | 61,879                        | 23,117 | 93,870                             | 35,068 |
| 1985 | 0.6852                            | 70,381                        | 27,103 | 102,716                            | 39,555 |
| 1986 | 0.7026                            | 76,517                        | 32,283 | 108,905                            | 45,948 |
| 1987 | 0.7227                            | 80,744                        | 33,596 | 111,725                            | 46,487 |
| 1988 | 0.7463                            | 77,166                        | 34,792 | 103,398                            | 46,619 |
| 1989 | 0.7774                            | 81,620                        | 37,002 | 104,991                            | 47,597 |
| 1990 | 0.8019                            | 80,971                        | 37,453 | 100,974                            | 46,705 |
| 1991 | 0.8442                            | 82,180                        | 34,549 | 97,347                             | 40,925 |
| 1992 | 0.8647                            | 72,727                        | 34,556 | 84,107                             | 39,963 |
| 1993 | 0.8920                            | 67,317                        | 36,923 | 75,467                             | 41,393 |
| 1994 | 0.9133                            | 60,400                        | 34,751 | 66,134                             | 38,050 |
| 1995 | 0.9306                            | 54,253                        | 34,590 | 58,299                             | 37,170 |
| 1996 | 0.9511                            | 48,535                        | 36,493 | 51,030                             | 38,369 |
| 1997 | 0.9746                            | 45,531                        | 36,034 | 46,718                             | 36,973 |
| 1998 | 1.0000                            | 43,125                        | 34,645 | 43,125                             | 34,645 |
| 1999 | 1.0220                            | 44,647                        | 35,152 | 43,686                             | 34,395 |
| 2000 | 1.0456                            | 47,616                        | 33,960 | 45,539                             | 32,479 |
| 2001 | 1.0699                            | 51,641                        | 33,158 | 48,267                             | 30,992 |
| 2002 | 1.0948                            | 55,399                        | 33,552 | 50,602                             | 30,647 |

**Source:** CRS, based on DOD data; excludes Desert Shield/Desert Storm costs and receipts.

## Path to Reform

As defense spending continued to decline and defense acquisition strategy evolved, congressional policymakers directed DOD to undertake a comprehensive review and study of its acquisition system, and present reform recommendations. Called the “Section 800” report (after the pertinent section in the Defense Authorization Act of 1991, P.L. 101-510), its purpose was not to replicate the work of previous studies, like the Packard Commission Study (1986) and Defense Management Review (1989), but to take their findings and prepare a workable set of recommended changes to acquisition laws. The study, once completed, would serve as a major resource for the National Performance Review and the Clinton Administration’s efforts to reinvent government, including the acquisition system.

The first package of congressional reforms, many of which were noncontroversial recommendations of the “Section 800” report, was passed in the Federal Acquisition Streamlining Act, or FASA, P.L. 103-355. The legislation revised more than 225 statutory rules, encouraged federal agencies to buy commercial, off-the-shelf products, and simplified government procedures for procuring those products. Key provisions included the following: (1) raising from \$25,000 to \$100,000 the threshold for waiving many statutes governing defense procurement; (2) streamlining the bid-protest process to prevent costly delays that could result when contractors protest procurement contract awards; (3) raising to \$500,000 the cap that would allow bidding defense contractors to bypass special accounting systems requirements, and avoid providing lengthy cost and pricing data to the government; (4) raising from \$25,000 to \$100,000 the value of contracts that could be reserved for small business; and (5) creating unified federal procurement statutes for executive branch agencies.

This legislation promoted performance-based contracting in DOD, as well as the use of acquisition reform “pilot” programs to test the effectiveness of some reform initiatives; one such example is mission-oriented program management. Performance-based contracting defines work to be performed in measurable, mission-related terms — in contrast to the heretofore procedure of defining the work in broad, imprecise terms through a “statement of work”. This approach was intended to reduce government costs and improve contractor performance by encouraging more innovative and efficient approaches to government contracts. Examples of such programs include joint direct-attack munitions (JDAM), commercially-derived aircraft and engines, and a fire-support tactical trainer (see **Oversight of Reform Initiatives.**)

A second package of reforms, called the Federal Acquisition Reform Act (FARA) of 1996, was passed as part of the FY1996 Defense Authorization Act. FARA made changes in the acquisition process in the areas of competition, commercial items, certification requirements and the Federal Acquisition Computer Network (FACNET). FASA II (called FARA) was passed during the first session of the 104th Congress. It built upon the earlier FASA legislation, and was included in the FY1996 DOD Authorization Act (P.L. 104-106). The newest reform provisions sought to (1) simplify procedures to procure commercial products and services, and at the same time preserve the concept of full and open competition; (2) reduce barriers to acquiring commercial products by eliminating the requirement for certified cost and pricing data for commercial products; and (3) streamline the bid protest process by providing for all bid protests to be adjudicated by the General Accounting Office (GAO). To reflect the projected efficiencies of acquisition reform and the broader manpower reductions occurring at DOD, FASA directed DOD to reduce its

acquisition workforce by 15,000 personnel during FY1996, and to report to Congress on how to implement an overall 25% reduction during the next 5 years (from October 1, 1995). In addition, the “procurement integrity” provision consolidates and clarifies the standards of conduct for federal officials in the acquisition process, to ensure consistent treatment of such personnel on a government-wide basis.

The FY1996 Defense Authorization Act changed federal procurement of information technology through the establishment of the Information Technology Management Reform Act of 1995 (ITMRA). First, it eliminated the central procurement authority of GSA, making each federal agency responsible for its own information technology procurement and investment. Second, it directed agencies to appoint a chief information officer whose responsibilities would include ensuring that information technology expenditures conform to budget and program management decisions. Third, it combined both protest processes for information technology and federal procurement under GAO’s authority. (For a discussion of current federal policies on information technology, see CRS Report 98-845, *Federal Government Information Technology Policy: Selected Issues*, updated January 5, 1999.)

Revisions to Part 15 of the Federal Acquisition Regulations (FAR)<sup>3</sup> went into effect on September 30, 1997. Part 15 streamlines the source selection and negotiation requirements to promote better communication between the government and potential contract bidders. The new rules encourage early and open dialogue, narrow the range of competitive bidders to those with a “reasonable chance” of winning the contract award, and promote “modular contracting,” which allows large projects to be broken down into smaller, more manageable parts, giving bidders a chance to focus on their particular expertise rather than take on the entire project. The revised acquisition regulations was a factor in the Department of Energy’s sale of Elks Hills Naval Petroleum Reserve for \$3.65 billion, which represents the largest divestiture of federal property.

## **DOD Promotes Reform**

Former Secretary of Defense Perry and his deputies were active in introducing acquisition reforms to foster greater efficiency, cost effectiveness, and military-civilian industrial interaction. In 1994, DOD leadership began introducing and promoting a number of new concepts, among them: 1) the single process initiative (SPI); 2) integrated product teams (IPT) to develop and build weapons systems; and 3) “cost as an independent variable,” a concept that would increase the priority of cost considerations in weapon system decisions. Each of the military services had also introduced reforms to service-specific parts of DOD’s acquisition system. DOD and the services are now in various stages of implementing these concepts.

In June 1994, Secretary Perry introduced a major acquisition reform directive reversing the traditional DOD preference for milspecs in favor of performance specifications and commercial standards. The directive required preference changes in purchasing new systems as well as modifications of existing systems. As a result, special waivers are now needed to

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<sup>3</sup> The Defense Federal Acquisition Regulation mirrors the Federal Acquisition Regulations, at [<http://www.arnet.gov/far/>].



use milspecs and will be granted in special cases only — a rule that used to apply to performance specifications and commercial standards. The plan to implement this policy directive was the SPI, which required U.S. companies to establish a common plant-wide process and performance standard for new and existing defense contracts. It forced contractors to consolidate, or eliminate, multiple processes, specifications, and standards for a particular product whether it be for commercial or defense use within different services. Over the next 12 to 18 months, DOD would modify all contracts at a given facility at the same time, instead of on a contract-by-contract basis.

In another important policy decision, DOD decided in May 1995 that the IPT approach would be used to develop and build weapon systems. The IPT concept, an increasingly common practice in the commercial world, would link representatives of the weapon maker, the military service purchaser, and the office of the defense secretary. Members of the team stay in constant communication, addressing problems and negotiating changes to the program's development as they arise, rather than working at arm's length through a formal process (such as through the Defense Acquisition Board). The IPT concept was intended to transform historically adversarial relationships, such as between headquarters staff organizations and program office teams, into productive partnerships, and place renewed emphasis on the importance of working as a cross functional team to maximize overall performance. Success has been achieved by the IPT approach in a few new programs; one example is the JDAM program (see next section). Encouraged by its results, DOD has begun widening the IPT concept to many other programs, both new and existing; one such effort, to review past performance in the source selection process, has resulted in policy and procedural changes in federal acquisition policy (see "Issues in the 105<sup>th</sup> Congress").

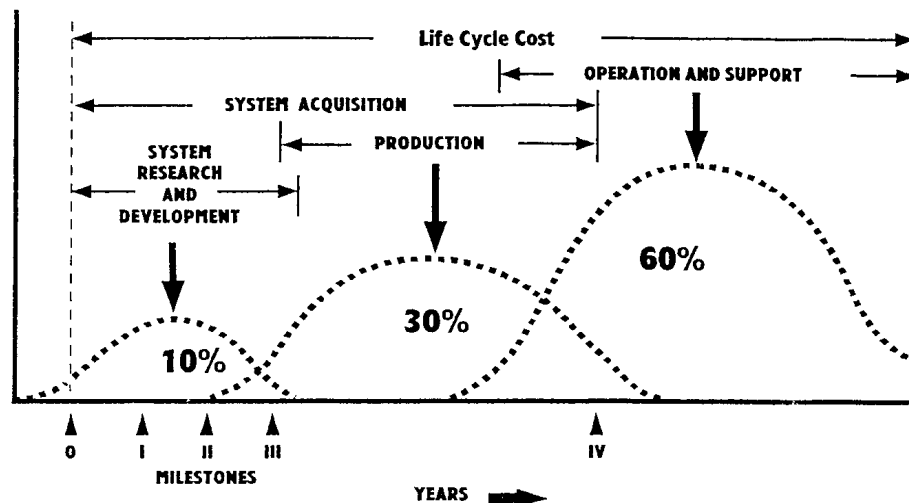
In one of the latest, potentially far-reaching decisions, DOD has begun a policy of increasing the importance of "cost" as a factor in deciding on the acceptable performance level of a weapon system. It is likely to force decision-makers to consider trading away some system performance to achieve greater cost savings. The policy, called CAIV, would attempt to move away from a major tenet in the Cold War culture of trying to achieve the best level of weapon performance at almost any cost. With the goal of lower costs and shorter schedules, the policy would require DOD program managers to examine the weapon system's entire life-cycle — including research and development, production, operation and support — and its cost patterns and objectives (see **Figure 1**).

The program manager would have to think about cost-related factors such as budgetary resources, unit costs of comparable or fielded systems, mission effectiveness, technology trends, innovative manufacturing techniques, and commercial business practices. DOD intends to give its program managers and contractors more freedom to make the trade-offs and meet cost targets; however, a significant challenge to implementing CAIV will be to persuade DOD and industry managers to become more innovative, accepting larger risks to achieve breakthroughs in cost and performance. The objective is to not penalize failures that might occur, despite management's best efforts (see the section on restructuring DOD's acquisition organization).

One of the most controversial of the acquisition reform initiatives is called "best value." Best Value is a process used in competitive contracting to select the most advantageous offer by evaluating and comparing several factors, including 1) technical competence; 2) proven past performance; 3) management capability; 4) life cycle costs, not just the initial price; and

5) quality. The “best value” may not be the lowest bid offered; in fact, a Navy contract award based on “best value” resulted in the awarding of a \$1.5 billion dollar contract (to build three LPD-17 amphibious assault ships) to a bidder that was \$100 million more expensive than the lowest bidder. (For additional information, see CRS Report 96-346, *Navy San Antonio (LPD-17) Class Amphibious Shipbuilding Program: Background Information.*)

Figure 1. **Typical Life-Cycle Cost Distribution**



Source: Defense Systems Management College

## Potential Impact of Reform Actions

Perhaps the most often-asked question about acquisition reform is how much DOD will save from the ongoing initiatives. Although many are hopeful, history shows that many past DOD efforts have resulted in only minimal savings. Past disappointments included the projected, but unrealized, savings associated with the 1989 Defense Management Review. A chief obstacle has been a residual inertia on the part of the U.S. government, particularly in DOD — a clinging to the culture of the Cold War. Some experts argue, however, that this time will be different because the defense procurement budget has declined so dramatically (see Table 1, DOD Procurement), and there is little hope of the budget increasing enough in the foreseeable future to finance projected U.S. needs for modernizing its force structure. Former Secretary Perry had made it clear that DOD was depending on “substantial” savings from acquisition reform, as well as from base closings and privatization of some of DOD’s functions, to help finance “critical” defense modernization.

It is difficult, at this point, to predict what DOD will achieve in the way of savings from its acquisition reform effort. More time is needed to complete implementation of the new initiatives, and to establish a system that accurately measures the savings. Fairly reliable estimates, however, exist for a few of the ongoing individual efforts. For example, the SPI

could result in significant cost reductions. In 1995, a study by Coopers & Lybrand found that 1.7% of the cost of DOD acquisitions resulted from milspecs and standards, and that government-imposed material management and accounting systems added another 0.6% to costs. DOD estimates that about half of those costs, or \$400 million, could be saved through reform. Experts also believe that by applying the IPT approach to program development and the CAIV concept to spending on weapons performance, potential costs savings could be in the billions of dollars — a preliminary estimate at this point.

The most definitive estimate of cost savings, when SPI, IPT, CAIV, and other such acquisition initiatives are applied to DOD programs, was offered by Secretary Perry. In introducing DOD's budget request for FY1997, he cited three DOD programs. The first of these was the "Smart T" program — the Army's tactical communication terminal for MILSTAR. After reexamining the costs of certain levels of performance and streamlining the specification and data requirements, the original programs' cost estimates were reduced from \$800 million to \$250 million, for a net saving of \$550 million. The second estimate of costs savings cited was for the Air Force and Navy JDAM program. The Air Force has reported that using the IPT approach has shortened the JDAM acquisition cycle by 4 years, eliminated numerous complexities, and significantly reduced the program's original cost projections.

Using the accelerated acquisition plan, as well as off-the-shelf components and other commercial practices, the original cost estimate would drop from \$42,000 per unit to \$14,000, a 67% savings estimated at \$2.9 billion. The third estimate of costs savings cited by Secretary Perry was for the C-17 program. After instituting the IPT approach, rethinking some performance requirements using CAIV, reducing reporting requirements some 3 years ago, and reaching an agreement to a multi-year procurement plan, DOD has estimated that it will save \$5.3 billion over the life of the program. Furthermore, the Air Force has identified \$13 billion in potential savings, or cost "avoidances," for 24 programs that include the C-17 and JDAM programs.

## **The Competitive Sourcing of DOD Functions**

For a long time, DOD has sought to competitively source its functions through public-private competitions through the OMB Circular A-76. U.S. policymakers will confront a number of questions, the answers to which will help determine the success or failure of outsourcing initiatives. First, does the initiative really reduce DOD costs over the long-term, and how will DOD measure those savings? It is known that DOD has experienced problems with its cost accounting and billing systems, important components in tracking cost savings. Second, will DOD's management structure be able to "manage" the initiative to make sure its operation becomes more efficient? Experts point out that some private sector companies have run into outsourcing problems because they failed to make necessary changes in their management structure. Third, does the initiative fit into the current policy of encouraging the closer integration of the U.S. defense and commercial industrial bases? Finally, does the initiative go beyond the "proper" limits of privatization at DOD, whose first and foremost mission is to protect U.S. national security, not to maximize savings? In other words, does the initiative adversely impact DOD's war-fighting capability?

## Oversight of Reform Initiatives

Congress has faced important oversight responsibilities because of changes taking place in defense acquisition policy. The success or failure of these changes will be determined by how quickly and effectively DOD acts to implement them. On March 15, 1996, DOD gave final approval to a major revision of DOD Directive 5000.1 and DOD Regulation 5000.2-R, both of which contained new policy changes and procedures based on FASA and FARA legislation. The former 900-page set of regulations has been reduced to a 160- page volume and is available via an on-line database. FASA has required the Comptroller General to evaluate the effectiveness of implementing the final FASA regulations, and submit a report to the Congress within eighteen months; FARA further broadened the scope.

The various congressionally mandated acquisition reform reports issued, and those to be issued later, require attention and, perhaps, subsequent action. For example, and in addition to the reports previously cited, the FY1996 DOD Authorization Act required another report that would enable DOD to improve the performance of depot maintenance and repair of U.S. weapon systems. On April 4, 1996, DOD issued its report, "Policy Regarding Performance of Depot-Level Maintenance and Repair Workload." It advocated reforming the laws regulating how DOD allocates its maintenance workload between the public and private sectors. It stated that such legal requirements prevented DOD from (1) taking full advantage of lower cost opportunities through outsourcing to the private sector, and (2) restructuring its public depots to provide the military only necessary "core" capabilities. The report drew mixed congressional reactions, and the allocation of DOD's maintenance workload has become a subject of debate.

When the House passed the FY1997 DOD authorization bill (H.R. 3230), it voted to maintain current DOD depot maintenance and repair policy (60% government, 40% private). The Senate voted to increase the "private" share, from 40% to 50%. In the 1997 DOD conference report, the House and Senate both receded; the conference report does not contain any of these provisions. The conferees agreed not to take any action regarding these issues that year; thus, the DOD depot maintenance and repair policy remained unchanged. The FY1998 Defense Authorization (P.L. 105-85) establishes a new definition of what constitutes "depot maintenance and repair;" it will require that DOD, in the course of conducting such competitions, clearly satisfy a number of congressional requirements during the source selection process, and requires that the Secretary of Defense provide an annual report to the Congress, detailing the public/private percentages of depot maintenance and repair workloads. This report would be reviewed by the Comptroller General to determine whether DOD had complied with requirements of Section 2466 of the U.S. Code.

The Senate Armed Services Committee's Subcommittee on Readiness recommended a revision of the laws relating to the performance of DOD depot maintenance, including 1) an increase in the private share to 50%; 2) adjusting the law so that work performed by private companies at public depots will be counted as public sector depot maintenance, rather than private sector depot maintenance; 3) requiring the efficient operations of the remaining public Air Logistics Centers (ALC) prior to the implementation of any "privatization in place" at former ALC locations; and 4) requiring DOD to preserve a core depot capability that could maintain the types of weapons systems that have been identified as "mission essential." The effect of these provisions would have been to prohibit privatizing Air Force maintenance work at McClellan ALC, Sacramento, California and Kelly ALC, San Antonio,

Texas. By November 6, the House and Senate had both reached a compromise on the FY1998 Defense Authorization Conference Report, adjusting the public/private depot maintenance and repair workload from 60/40 to 50/50; however, a number of new provisions were included, such as directing DOD to begin integrating public depot work. (See P.L. 106-259, the FY2001 Defense Appropriations Bill.)

On March 2, 1999, in a hearing before the Subcommittee on Military Readiness, Deputy Undersecretary of Defense (for Acquisition Reform) Stan Z. Soloway reported that DOD acquisition reform initiatives had experienced measurable success within the Joint Air-to-Surface Standoff Missile Program (JASSM), Joint Direct Attack Munition (JDAM) Program, Fire Support Combined Arms Tactical Trainer (FSCATT) Program, Joint Primary Aircraft Training System (JPATS), and the F-117 Tactical Air Program. Here are excerpts of his March 2, 1999 testimony before the House Subcommittee on Military Readiness.

The Joint Air-to-Surface Standoff Missile, or JASSM, a next-generation air launched cruise missile that will provide the Air Force and Navy a standoff capability greater than currently exists, has made major gains from acquisition streamlining. Estimated program costs have been reduced 44%. JASSM will also have a complete "bumper-to-bumper" 15-20 year warranty.

The Joint Direct Attack Munition, or JDAM, a strap-on guidance kit to enhance the delivery accuracy of 1000 and 2000 pound bombs, employed acquisition reform to achieve lower development and production costs, faster schedules, and lower unit costs. The JDAM team reduced unit cost by approximately 60% below the estimated requirement costs. Overall, cycle time for JDAM was reduced 35% with a 30% reduction in program staffing. JDAM reduced projected O&M (Operation and Maintenance) Costs by \$49.4 million (86.8%) through the use of a 20-year warranty.

The Fire Support Combined Arms Tactical Trainer (FSCATT) program has achieved a 33% reduction in cycle time with a 13.5% reduction in estimated contract cost and 27% reduction in program staffing.

## **Issues in the 105<sup>th</sup> Congress**

Issues in the 105<sup>th</sup> Congress included 1) reviewing congressionally mandated reports, the findings of which will aid Congress in identifying further cost cutting strategies for reducing infrastructure costs savings in the Department of Defense; 2) integrating the assessments and recommendations of various defense panels charged with assisting the Secretary of Defense in changing the business culture within the Defense Department; and 3) assisting DOD in its implementation of acquisition workforce reductions as well as refinements and other changes to federal acquisition regulations.

### **Review of Congressionally Mandated Reports**

The continuing acquisition reform debate in the 105<sup>th</sup> Congress focused on a number of congressionally mandated reports, the findings of past and current reports of the Defense Science Board, and the changes that Secretary Cohen has announced as part of his Defense Reform Initiatives. The first was a study of major defense acquisitions programs, called the "Report of the Defense Science Board's Task Force on Defense Acquisition Reform."

Phase II of the report was issued August, 1994; Phase III was published in August 1996. Under the requirements of FASA, DOD was asked to reduce the average time that it took to field “emerging technologies,” starting from the baseline of October 13, 1994. At that time, it would take over 16 years to field the next generation’s weapon system; one of the study’s objectives was to reduce this by upwards of 50%. In the Secretary of Defense’s Annual Report for FY1996, the average time was reduced to about 9 ½ years.

The second study was chartered to develop recommendations for DOD on how to effectively use outsourcing to create a funding mechanism for future force modernization needs. The Task Force issued a lengthy final report, stating:

...The Task Force believes that all DOD support functions would be contracted out to private vendors except those functions which are inherently governmental, are directly involved in war fighting, or for which no adequate private sector capability exists or can be expected to be established...

The third study was chartered to develop ways to improve the organization of acquisition processes and personnel. The goal of the panel is to help DOD define a new acquisition system that can reduce weapons procurement, both costs and cycle time.

## **Assessments and Recommendations of Defense Panels**

In keeping with his desire to change the way that the Pentagon conducts business, often characterized in the press as a “revolution in business affairs,” Secretary Cohen announced a number of Pentagon management and organizational reforms. These reforms were recommended by the Task Force on Defense Reform, a public/private partnership which studied ways to improve business practices within DOD. The “Tail-to-Tooth” Commission and the Task Force on Defense Reform operated in parallel, and a number of their recommendations were used by the Secretary to develop his Defense Reform Initiatives. They include 1) reducing the size of the Office of the Secretary of Defense, the Joint Staff and defense agencies, from 141,000 to 111,000 staff members; 2) realigning functions within the Department of Defense, consolidating and eliminating duplicate functions; 3) increasing public-private competitions to outsource non-core maintenance and support work; and 4) establishment of a senior-level Defense Management Council to monitor compliance. Cohen has also proposed base realignment and closure (BRAC) rounds for the years 2001 and 2005 to further reduce defense infrastructure.

## **Changes in Federal Acquisition Legislation**

Another significant policy change that evolved in the 105<sup>th</sup> Congress was the interpretation of the use of past performance in the source selection process. Dr. Paul Kaminski, Dr. Gansler’s predecessor, instituted the Past Performance Integrated Product Team (IPT) to take a look at the evaluation of the use of past performance within the defense contract industry. As a result of the IPT’s recommendations, Dr. Gansler issued a new set of guidelines on past performance in the source selection process, to become effective on February 1, 1998. These guidelines changed federal acquisition regulations and the Defense Acquisition Regulation (DAR) Supplement; all defense agencies are required to adopt them. The purpose of the new guidelines was to establish consistency and standardization in how DOD contracting officials define and collect information about defense contractors. Among

defense contractors, the lack of consistency in the use of past performance information had been an ongoing source of criticism; the new policy will help defense contractors to understand the kind of information that will be evaluated, rather than be evaluated on factors known only to DOD. The new policy guidelines are to spell out a common management policy among the services (previously Army, Navy, and the Air Force each had unique approaches for collecting and evaluating contractor past performance information), and the unified policy will make it easier to evaluate and compare contractor performance. Past performance information (PPI) will be automated and, along with other efficiencies, will make the information more accessible. The information will be made available to the general public, at some future time. DOD has implemented a pilot study; a status report is expected.

## Issues in the 106<sup>th</sup> Congress

The 106<sup>th</sup> Congress had an important oversight role in defense acquisition reform, especially in monitoring DOD reports to Congress on many of its acquisition reform initiatives (such as progress in reducing the size of the acquisition workforce) or in defining governmental activities subject to managed competition and outsourcing alternatives.

OMB published the proposed rules to implement the Federal Activities Inventory Reform (FAIR) Act of 1998 (P.L. 105-270) through the use of OMB Circular A-76. The OMB Circular A-76 policy was first issued in 1966. The policy, supplemental handbook, and accompanying policy memoranda were revised and re-issued on June 14, 1999. Authority for the OMB Circular A-76 originated in the Budgeting and Accounting Act of 1921 (31 U.S.C. 1 et seq.) and the Office of Federal Procurement Policy Act Amendments of 1979 (41 U.S.C. 401 et seq.) Legal or procedural challenges to the policy or procedures were discussed in the Supplemental Handbook. Copies of updated versions can be found on the Internet at [<http://www.whitehouse.gov/OMB/circulars/index-procure.html>].

FAIR outlined a way for federal agencies to decide who was best to perform work activities — whether the work should be performed in-house or contracted out (called outsourcing) to another public or private group. FAIR included a definition of what was generally considered an inherently governmental function, although agencies can argue for inclusions/exclusions to the lists. Lists may be challenged by interested parties, as defined in the legislation. Activities or functions not inherently governmental in nature are considered commercial and may be subject to a managed, competitive outsourcing process; however, the legislation did not require agencies to contract out commercial activities.

The FAIR Act required federal executive agencies to submit annual inventory lists of government activities “not inherently governmental” in nature; ultimately, the lists would be made available to Congress and the general public. In accordance with the FAIR Act, DOD released its final 2000 inventory of federal jobs that could be performed by private sector companies. Reportedly, out of some 452,807 civilian jobs that could be performed in the private sector, approximately 39% of those jobs are likely candidates for outsourcing.<sup>4</sup>

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<sup>4</sup> Saldarini, Katy. “Final Round Of Outsourcing Lists Released.” *Government Executive*. February 12, 2001.

## Issues in the 107<sup>th</sup> Congress

The 105<sup>th</sup> and 106<sup>th</sup> Congresses passed a number of defense reform provisions that supported, if not encouraged, DOD's outsourcing and privatization initiatives. In the 107<sup>th</sup> Congress, Congress may seek the answers to three important questions: (1) do DOD outsourcing and privatization initiatives save money, in the long term? (2) do DOD outsourcing and privatization initiatives produce a smarter, more efficient and more accountable government? (3) if not outsourcing and privatization, then what other alternative strategies may produce similar, if not better, costs savings? The answers to each question will be critical; DOD is faced with the prospect that 50% of its defense acquisition workforce may be eligible to retire by 2005. As a result, Congress and DOD will need to work together to reshape and redefine the size and scope of the future workforce.

The 107<sup>th</sup> Congress will examine the results of three studies and one report, mandated by the FY2001 Defense Authorization Bill (P.L. 106-398), and one report mandated by the FY2000 Defense Authorization Bill (P.L. 106-65), which may provide statistical and other data to determine whether certain efficiencies in defense operations have been achieved. First, the Comptroller General is mandated to conduct two studies: 1) the use of "contract bundling" in military construction contracts (report was due February 1, 2001) and 2) the policies and procedures governing the transfer of federal commercial activities from the public sector to the private sector (report due May 1, 2002). Second, the Secretary of Defense is directed to conduct a study on the impact of purchasing military parts, components, and materials from foreign sources (report due October 30, 2001). Third, Section 343 of P.L. 106-65 requires the Secretary of Defense to provide data on the (1) number of contractors employed by DOD; (2) types of contractors; and (3) how (source of appropriation) and where (DOD organizational element) contractors were funded (report due, March 1, 2001). Fourth, DOD continues to reform various aspects of its management practices and business operations to become more efficient and cost-effective in building and maintaining the nation's military force.

DOD is trying to reduce its infrastructure costs to achieve savings that could help finance future weapons and military equipment modernization. The new Undersecretary of Defense for Acquisition, Technology, and Logistics has announced DOD's four priorities for acquisition reform: 1) improving the credibility and effectiveness of the acquisition and support process by reducing the acquisition cycle time and costs (the time and cost of building new weapons systems) and including the real acquisition costs in the defense budget; 2) improving the quality and morale of the acquisition workforce through the use of special hiring authorities, granted by Congress, to recruit acquisition experts; 3) aligning weapon systems and infrastructure with a new strategy currently under development by the new Secretary of Defense; and 4) advocating for next-generation technologies that will ensure military dominance.

Competitive sourcing studies between public and private sectors through the OMB Circular A-76 and the requirements of a closely-related initiative, the FAIR Act {Public Law (P.L.) 105-270}, are viewed as efforts to improve the efficiency of DOD business practices while streamlining operational capabilities to produce budgetary savings. However, there is conflicting evidence as to whether such competitions produce significant savings, in the long term. The 107<sup>th</sup> Congress will likely face increased calls for continued debate and proposals to study federal outsourcing efforts, as well as review legislation introduced during



the 106<sup>th</sup> Congress that, if enacted, would ban future outsourcing initiatives unless savings could be demonstrated. Another important development will be the recommendations of a congressionally-mandated panel focused on federal competitive sourcing policy through OMB Circular A-76. Section 832 of P.L. 106-398 mandates that GAO convene a panel to study the policies and procedures governing the transfer of commercial federal activities from government personnel to federal contractors. The Panel issued its report on April 30, 2002 (See *Major New Developments* section).

## 107<sup>th</sup> Congress: Key Public Law

P.L. 107-117. Authorizes appropriations for fiscal year 2002 for military activities of the Department of Defense, for military constructions, and for defense activities of the Department of Energy, to prescribe personnel strengths for the Armed Forces, and for other purposes. Introduced in the Senate September 19, 2001. Passed Senate (text of S. 1438) with Amendments (99-0), October 2. Received in the House, October 4; the House struck all after the enacting clause and inserted in lieu thereof of the provisions of a similar measure, H.R. 2586; bill passed without objection. Senate disagreed to House amendment, agreed to conference, October 17. Conference report, H.Rept. 107-333, passed House (382-40) December 13; passed Senate (96-2) December 13. Signed into law December 28, 2001.

## 106<sup>th</sup> Congress: Key Public Laws

**P.L. 106-65 (S. 1059, H.R. 1401).** Authorizes appropriations for FY2000 for military activities of Department of Defense, for military construction, for defense activities of Department of Energy, and for other purposes. Passed Senate, amended (92-3), May 27, 1999. Conference report passed House (375-45) September 15, 1999; passed Senate (93-5) September 22, 1999. Signed into law October 5, 1999.

**P.L. 106-79 (H.R. 2561, S. 1122).** Makes appropriations for FY2000 for Department of Defense and for other purposes. Passed House, amended (379-45), July 22, 1999. Passed Senate by unanimous consent, amended, July 28, 1999. Conference report (H.Rept. 106-371) filed October 8, 1999. Conference report passed House (372-55) October 13, 1999; passed Senate (87-11) October 14, 1999. Signed into law October 25, 1999.

**P.L. 106-259 (S. 2593, H.R. 4576).** Makes appropriations for FY2001 for the Department of Defense and for other purposes. Prohibits 1) the conversion of DOD functions from government to contractor performance, unless a “Most Efficient Organization” analysis is completed and certified to House and Senate Defense Appropriations Committees, and 2) the purchase of welded shipboard anchor and certain mooring chain, unless both are manufactured in the United States from components that are substantially manufactured in the United States. Authorizes public-private competitions for depot maintenance and repair work, under certain conditions, and exempts such competitions from the requirements of OMB Circular A-76. Reported to House (H.Rept. 106-644) May 25, 2000. Passed House (367-58) June 7, 2000. Senate took up H.R. 4576 and substituted the text of S. 2593 as reported by the Senate Appropriations Committee, June 8, 2000. Passed Senate, amended (95-3), June 13, 2000. Conference report (H.Rept. 106-754) filed

July 17, 2000. Conference report passed House (367-58) July 19, 2000; passed Senate (91-9) July 27, 2000. Signed into law August 8, 2000.

**P.L. 106-398 (S. 2549, H.R. 4205).** Authorizes appropriations for FY2001 for military activities of the Department of Defense and for military construction, to prescribe military personnel strengths for FY2001, and for other purposes. Reported to House (H.Rept. 106-616) May 12, 2000. Passed House (353-63) May 18, 2000. Senate took up H.R. 4205, substituted the text of S. 2549, as amended, and passed H.R. 4205 (97-3) July 13, 2000. Conference report (H.Rept. 106-945) passed House (382-31) October 11, 2000; passed Senate (90-3) October 12, 2000. Signed into law October 30, 2000.

## **FOR ADDITIONAL READING**

U.S. Department of Defense. *Commission on Roles and Missions of the Armed Forces. Directions for Defense.* May 1995.

## **CRS Reports**

CRS Report RL30776. *The Berry Amendment: Requiring Defense Procurement to Come from Domestic Sources*, by Valerie Bailey Grasso.

CRS Report RS20943. *Contracting Out: Governmentwide Legislation in the 107<sup>th</sup> Congress*, by L. Elaine Halchin.

CRS Report RL31236. *Defense Outsourcing: The OMB Circular A-76 Policy*, by Valerie Bailey Grasso.

CRS Report RL30720. *The U.S. Defense Industrial Base: Trends and Current Issues*, by Daniel Else.