

Testimony

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DOD Acquisition Reform Efforts

Statement of
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Committee on Armed Services
United States Senate



Mr. Chairman and Members of the Subcommittee:

We appreciate the opportunity to appear before the subcommittee today to discuss Department of Defense (DOD) acquisition reform efforts. My testimony will focus on DOD actions to (1) analyze existing procurement laws and regulations, (2) streamline its acquisition organization, (3) reduce excessive and duplicative audit and oversight, (4) develop an integrated financing plan, and (5) make greater use of commercial products.

Before dealing with these specific issues, I would like to briefly comment on the recurring and systemic nature of the acquisition problems facing DOD. Complaints about complex procurement laws and regulations, multi-layered organizational structures, and an ineffective acquisition workforce are problems that have been associated with defense acquisition as far back as the 1949 Hoover Commission. Unfortunately, we face those same problems today.

Over the years, DOD has made a strong commitment to implement numerous reform initiatives--the latest being in response to the President's Blue Ribbon Commission on Defense Management (better known as the Packard Commission). Historically, the agency's initial sense of commitment has dissipated over time and the problems remain. We cannot afford to let that happen again. What is crucial to success is a strong and continuing top-level management commitment.

This subcommittee, through the Fiscal Year 1989 National Defense Authorization Act, recognized that DOD must place greater priority on streamlining and simplifying the procurement process. The Act encouraged DOD to make greater progress by requiring a report on its actions to improve the acquisition process. This reporting requirement was designed to enhance Congressional

oversight and ensure DOD attention to acquisition reform measures.

In December 1988, DOD, as required by the Act, reported numerous reform efforts. We support those efforts, but have concerns about DOD's progress in bringing about meaningful change in several areas. Let me briefly discuss them.

ANALYZING EXISTING PROCUREMENT LAWS, REGULATIONS, AND GUIDELINES

The Act requires the Under Secretary of Defense for Acquisition to comprehensively analyze how existing procurement laws, regulations, and guidelines affect DOD's capability to efficiently and effectively meet the country's national defense needs. The Act also requires the Under Secretary to recommend legislation considered appropriate to improve that capability.

DOD's report lists 20 laws enacted in the last 6 years that DOD believes have made major changes to the agency's procurement system. DOD provided no analysis of how the laws affected its capability but concluded that they burdened both government and industry, reduced the agency's flexibility, and complicated the procurement system. Rather than identifying specific problems with existing laws, DOD states that what is badly needed is a simplified procurement statute.

While there has been a proliferation of laws and regulations over the last several years, each law was enacted to deal with a particular problem. The comprehensive analysis required by the Act is necessary before any of those laws are changed or eliminated. Without such an analysis, it is difficult to identify what specific changes, if any, are needed.

DOD's report proposes 12 specific legislative changes to simplify the procurement process, but contains no analysis of how the proposed changes will improve DOD procurement procedures. The report's descriptions of anticipated improvements from the proposed changes are vague. In several instances, the report states that the proposed changes would reduce administrative leadtimes. In other cases, no specific benefits are identified.

For example, DOD proposed changing the legislation dealing with weapon system warranties by reducing the approval level for waiving warranties and reporting waivers annually instead of as they occur. Whether there is a problem and whether it stems from either the legislatively imposed approval level or reporting requirements is not clear. Our work has shown that there have been very few requests for waivers because the military services have been unable to show whether waivers are cost beneficial.

Another DOD proposal recommends that the heads of contracting activities rather than the Senior Procurement Executive approve using other than full and open competitive procedures on procurements costing between \$10 million and \$100 million. DOD believes this will significantly reduce administrative leadtime. Changing the approval level, however, does not reduce either the analysis needed to justify the decision or the documentation required. It is not clear from DOD's report how changing the level of approval will significantly reduce administrative leadtime. Furthermore, the report does not discuss whether the proposed change will continue to meet the purpose of the existing legislation.

STREAMLINING THE ACQUISITION ORGANIZATION STRUCTURE

In June 1986, the Packard Commission recommended substantial changes in the defense acquisition process in several specific areas including organization, decision-making practices, and

management. Among other things, the Commission recommended a streamlined acquisition organization with centralized policy making and decentralized execution at the program management level. The commission proposed reducing to two the number of levels and people between the Under Secretary of Defense for Acquisition and program managers for major programs. To accomplish this, Service Acquisition Executives and Program Executive Officers would oversee major acquisition programs, and the Service Acquisition Executives would report directly to the Under Secretary. This new organizational structure was meant to reduce the potential for intervention in program matters by officials outside the streamlined chain of command and strengthen the authority and responsibility of the individuals who play an extremely critical role in the acquisition process.

DOD has established the organizational structure recommended by the Packard Commission. However, our work and recent reports by the Project on Monitoring Defense Reorganization and Institute on Defense Analyses suggest that the new structure does not have the decision-making authority and control of resources envisioned by the Commission. Rather, the decision-making authority and control over resources remains with the pre-existing organizational structure. Thus, while the organizational structure has been modified, it has not substantially changed or clarified program managers' lines of authority and program managers see little change in their jobs.

REDUCING DUPLICATIVE AND EXCESSIVE OVERSIGHT

The Act requires the Under Secretary to report efforts to prevent duplication of audit and oversight and discuss the feasibility and desirability of several specific methods of meeting this objective.

DOD reported that it has taken, or is in the process of taking, several actions to use its audit and oversight resources more effectively. Actions include (1) raising the threshold for preaward audits from \$100,000 to \$500,000, (2) defining the roles and responsibilities of the various DOD organizations responsible for reviewing contractor systems and operations, (3) instructing contracting officers not to request cost or pricing data when adequate price competition exists, and (4) emphasizing the early use of should cost reviews and close coordination among should cost team members to preclude duplicate requests for contractor data.

While in many cases these actions are restatements or clarification of existing DOD policies, they should result in more effective use of DOD's audit and oversight resources.

We believe two of the initiatives, in particular, hold the greatest promise for using DOD audit and oversight resources more effectively. First, on June 10, 1988, the DOD Inspector General issued a new policy to improve coordination in DOD audits of contractor records. The policy provides that DOD audit organizations, including the Inspector General, the Air Force Audit Agency, the Naval Audit Service, and the Army Audit Agency will normally rely on the Defense Contract Audit Agency to review contractor records. Detailed implementing procedures for the policy were not issued until February 1989, and it is therefore too early to determine its actual effect.

The second significant initiative is the establishment of the Contractor Risk Assessment Guide program in November 1988. The program is designed to encourage contractors to develop more effective internal control systems and reduce DOD oversight in areas where contractors demonstrate adequate internal control systems. By assessing the validity of internal control systems

Instead of extensively auditing transactions, DOD can make better use of its oversight resources.

GAO has long supported the need for effective internal control systems. Accountability for compliance with applicable procurement statutes and regulations must start with industry. The first line of defense in controlling fraud, waste, and abuse is an adequate control system that is fully supported at all levels of a company. An adequate control system permits a company to institute preventative steps as opposed to reacting after the fact.

While the program is conceptually sound, cultural changes are required by both industry and government if the program is to succeed. Industry's incentive to voluntarily participate in the program is the prospect of reduced oversight. Whether oversight will be reduced or merely shifted to other areas remains to be seen. Industry has approached the program with caution. In fact, as of April 1989, less than a handful of contractors have volunteered to participate in the program.

Many of the corporations involved with long-term government contracts are subject to the provisions of the Securities and Exchange Act's recordkeeping and internal accounting control requirements. The recordkeeping requirements mandate records which are designed to accurately and fairly reflect the transactions and disposition of assets. The control provisions require that the company devise and maintain a system of internal accounting controls sufficient to provide reasonable assurances that certain specified objectives are attained. However, while companies must file annual reports and other information with the Securities and Exchange Commission, the control and reporting provisions do not specifically cover cost, price, estimating, billing, and performance measurement controls nor do they require reporting on such controls.

It may be time to consider legislation which would require annual management reports by defense contractors on their internal controls and an independent public accountant's opinion on management's representation. The Federal Manager's Financial Integrity Act of 1982 establishes a similar concept for federal agencies.

DEVELOPING AN INTEGRATED FINANCING PLAN

The Act requires the Secretary of Defense to develop and keep current a plan to ensure that DOD contract financing, profit, and risk-sharing policies are integrated to meet the agency's long-term needs for industrial resources and technology innovation. The Act requires the Secretary to review the plan annually and report the results of the review to the House and Senate Armed Services Committees in conjunction with submission of the Five Year Defense Program.

The Act recognizes that DOD policies must be adequately integrated to (1) stimulate efficient contract performance, (2) not discourage companies from seeking government business, and (3) promote investment to enhance productivity and provide for a sound and viable industrial base. DOD's 1985 Defense Financial and Investment Review, last year's industry sponsored study by the MAC group, and the recent study by the Aerospace Industries Association all recognize the need for integrating DOD's contract financing and profit policies.

DOD submitted its Five Year Defense Program this year without the required plan. DOD reported that it is "waiting for preliminary assessments from the advisory committee before proceeding with the integrated financing policy." The Act required DOD to establish an advisory committee to develop recommendations concerning methodology for measuring contractor profits.

We believe current and consistent contractor profit data is essential to an effective DOD assessment of how its financing and profit policies impact industry. However, DOD currently lacks such data. In the past, DOD has relied on ad hoc studies to assess how its policies are working to achieve profit levels that are equitable to industry and provide contractors sufficient incentive to invest profits into capital facilities. Reliance on ad hoc studies, however, has not provided DOD the management information needed for effective decisions. Such management information must be based on accurate and current data, and consistent and appropriate analysis.

In September 1987, we proposed a legislative action to establish a program to report contractor profitability. The program would require:

- a consistent and appropriate analytical methodology to evaluate profitability,

- a means for systematically establishing the integrity of the studies and the reliability of contractor-furnished data, and

- mandatory contractor participation.

Contractors and DOD are opposed to our profit reporting program. Despite that resistance, we remain convinced that our proposal would provide DOD the information needed to adequately assess how existing and pending policies impact industry. We also believe such a reporting program would provide DOD the information that is essential to developing an integrated financing plan as required by the Act.

DOD EFFORTS TO BUY COMMERCIAL PRODUCTS
AND USE COMMERCIAL-STYLE PROCUREMENT PROCEDURES

The Packard Commission made a number of recommendations designed to achieve a balance between high military capability and low, life-cycle costs. Among other things, the Commission recommended that DOD make greater use of commercial products and reduce excessive reliance on rigid military specifications.

We support the need for DOD to buy commercial products where feasible. Our recent work, however, shows that DOD has not placed the management emphasis needed to ensure that full advantage is taken of existing laws and regulations to procure commercially available items. We recommended that DOD expedite guidance, provide training, and collect data on the extent it buys commercial items.

The Commission also recommended that DOD increase the use of commercial-style procurement procedures that emphasize quality and performance as well as price. The Office of Federal Procurement Policy, with assistance from DOD, is developing a legislative proposal to establish streamlined, commercial-style, competitive procedures for buying commercial products. We plan to evaluate the proposal when it is finalized. It is not clear, however, which type or volume of products would be procured using procedures other than those currently available.

We support efforts to increase the value the government receives for its procurement dollar. We agree with those who contend that buying on the basis of price alone is often short-sighted and unwise. We do not agree, however, that such price-driven buying is mandated by current law, particularly the Competition in Contracting Act. We find nothing in current law that requires agencies to buy goods and services based on the lowest-cost,

technically acceptable offer, without considering quality and performance. Current law allows agencies to use whatever source selection criteria they believe strike the appropriate balance between price and technical factors.

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Mr. Chairman, that concludes my statement. We will be pleased to respond to any questions.