



THE SECRETARY OF DEFENSE
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MEMORANDUM FOR THE SECRETARIES OF THE MILITARY DEPARTMENTS
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SUBJECT: ACQUISITION REFORM

The Department of Defense (DoD) faces unprecedented challenges in preserving force effectiveness in light of a radically changed threat, substantially declining defense budgets, and rapidly changing technology. The existing acquisition system will not be, and in some cases already is not, capable of responding to customer needs in this new environment. The fact is -- the world in which DoD must operate has changed beyond the limits of the existing acquisition system's ability to adjust or evolve -- it must be totally re-engineered.

Acquisition reform is consistent with many of our most important national goals: saving the taxpayer money; reinventing Government; strengthening our military; and improving our economy. To meet these goals in today's environment DoD must:

- Be able to rapidly acquire commercial and other state-of-the-art products and technology, from reliable suppliers who utilize the latest manufacturing and management techniques;
- Assist in the conversion of U. S. defense-unique companies to dual-use production;
- Aid in the transfer of military technology to the commercial sector;
- Preserve defense-unique core capabilities (e.g., submarines, armored vehicles, and fighter aircraft);
- Integrate, broaden, and maintain, a national industrial base sustained primarily by commercial demand but capable of meeting DoD's needs;

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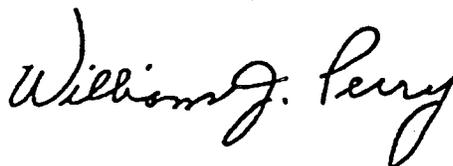
- Be able to adopt business processes characteristic of world class customers and suppliers (including processes that encourage DoD's suppliers to do the same); and
- Be free to stop applying Government-unique terms and conditions on its contractors to the maximum extent practicable.

As you know, to facilitate the Department's acquisition reform efforts, I have established a new office, that of the Deputy Under Secretary of Defense for Acquisition Reform (DUSD(AR)). The DUSD(AR) will be responsible for fundamentally restructuring and improving the acquisition process by directing the conception, development, adoption, implementation, and institutionalization of new and innovative acquisition policies and processes. I know that representatives of your offices have been playing an active part in the acquisition reform efforts to date as part of the Acquisition Reform Senior Steering Group. I want to thank you and your staffs for your tremendous support, and quick turnaround of proposed actions being coordinated by the DUSD(AR).

I also know that you each have a number of acquisition reform studies and initiatives ongoing internally within your organizations. I applaud those efforts and encourage you to continue to pursue them. I would ask, however, that you coordinate your efforts with the DUSD(AR) to ensure the Department as a whole is getting the most out of our combined efforts to change the acquisition process. I am firmly convinced that fundamental reform will not occur unless those who are part of the existing system participate in developing and implementing the changes. DoD will not succeed in fundamentally re-engineering the acquisition system unless those "on the front line" of the acquisition process embrace this effort. I know they are the experts, not those of us sitting in the Pentagon. I have directed the DUSD(AR), and encourage you in your efforts, to include these experts on any Process Action Teams or working groups that are formed to develop re-engineering plans. I also am committed to seeking the advice of industry and Congress as we proceed along this path. They are partners in this process, and their views are critical.

Attached is a copy of my paper: "*Acquisition Reform -- A Mandate for Change.*" It summarizes my beliefs on how the Department should approach acquisition reform, and it identifies goals for a re-engineered system. I urge you to give this paper wide dissemination within your acquisition organizations. It is important that all know what direction I am charting for DoD so that you can shape your policies accordingly.

The Administration, beginning with the President, followed closely by the Vice President, and myself, are dedicated to change and to improving the way Government functions. We need your active support to succeed. Reform of the acquisition system must be a number one priority for all of us.



Attachment



Acquisition Reform
A Mandate For Change

February 9, 1994

Honorable William J. Perry
Secretary of Defense

THE PROBLEM – WHY CHANGE IS NECESSARY

The Post-Cold War era poses a new set of political, economic, and military security challenges for the United States: regional or limited conflicts; proliferation of weapons of mass destruction, both nuclear and non-nuclear; risk to its economic well-being; and the possible failure of democratic reform in the former Soviet Bloc and elsewhere. The President and Secretary of Defense are committed to maintaining the U.S. military's edge over opponents. That means maintaining superior people, training, logistics, and weapons system technology -- the advantage the U.S. now has that allows us to deter aggression, and to prevail quickly with minimum casualties when required to employ force. The President and Secretary of Defense are committed to maintaining a lean, high-tech, agile, ready-to-fight military force during a time in which: the threats are changing and unpredictable; by Fiscal Year (FY) 1997 defense spending will have declined in real terms by over 40% from FY85; and advanced technology is increasingly available to the world.

The Department of Defense's (DoD) Bottom-Up Review provides the vision, and the blueprint, for meeting the security challenges of the post-Cold War world -- responding to threats anywhere in the world where U.S. interests are at risk. In today's environment the current process will not always be able to meet the Department's need. DoD will not be able to carry out this blueprint, without dramatic changes in its acquisition processes -- from determining what the Department needs, to logistics support and reutilization requirements.

Examples of the Need for Change

It is not difficult to see why change is imperative. Stories illustrating the need for reform abound. For example:

DoD is Often Unable to Acquire State-of-the-Art Commercial Technology. A commercial company was planning to introduce a radio with special encryption features sought by DoD. Because the item had not been sold in substantial quantities to the public, it could not qualify for an exemption to DoD's requirement that the company provide cost data. Since the company did not generate such information for their commercial customers, it would have had to set up a new accounting system to track and verify the information if it wanted to sell the radios to DoD. It couldn't afford to do that. The result was that DoD was stuck buying old technology while commercial customers bought the new, more capable radios.

DoD is Often Unable to Buy from Commercial Companies -- Even When Their Costs are Cheaper or DoD Must Buy a Commercial Product Because it is the Only One They Can Get. A military hospital wanted to buy aspirin. The low bid was \$3.98 per unit. DoD ended up having to buy from the next lowest bidder -- for \$4.40 per unit, because the low bidder was a commercial company that refused to disturb its long-standing subcontractor relationships to fulfill DoD requirements that a certain percentage of its subcontractors were small, disadvantaged businesses. The additional cost to DoD was \$107,000 over the life of the contract.

The Air Force attempted to negotiate a new contract with an aircraft manufacturer to supply spare parts for its military version of a commercial aircraft. The company was only manufacturing the spares in its commercial division, which did not meet the requirements for doing business with the Government. In January, 1988, the company first notified the Air

Force that it would need a commercial item exemption in order to provide these spares. It took until June, 1992 -- four and one half years -- until the Air Force and the company were able to agree on contract terms and conditions. During that time countless hours were spent by the contractor, the Air Force, and OSD personnel attempting to determine which of the 278 clauses in the Air Force contract could be waived. They finally received waivers on approximately 11 clauses.

Commercial divisions of a major defense electronics company simply refuse to do business with the Government. They cite several reasons: their commercial division accounting systems cannot provide the cost data required by DoD; they don't want to incur the added cost of complying with Government-unique terms and conditions; they are wary of giving the Government the right to audit proprietary cost and financial information; and fear losing their commercial proprietary data and software. Because many of these requirements are required to be "flowed down" by a prime contractor to its subcontractor, and there is no exception for inter-company transfers, not only can these divisions not sell to DoD, but they cannot transfer their parts to divisions of the company that do sell to the Government without changing their commercial processes to accommodate the Government requirements. This means that the company either cannot use its own company's semiconductors, or cannot charge the Government for the components, because the semiconductor division of the company does not have an approved Government accounting system. One company projected it will have included over \$1,000,000 worth of semiconductors at no cost to the Government on just two current DoD programs.

DoD's Costs of Doing Business are Too Great. DoD sent out a solicitation for a quantity of ant bait expected to cost \$25,595, based on the last purchase made. This meant that DoD had to use the standard, lengthy solicitation procedures rather than existing streamlined procedures for "small purchases" -- those \$25,000 or less. The solicitation was 29 pages long, and it took 227 days to award the contract. As it turned out, the lowest bid came in under \$25,000. Had the threshold for "small purchases" been higher, the contracting officer would have been able to use simplified procedures at the outset, and the contract could have been awarded in 27 days instead of 227.

As a 1991 report by the Center for Strategic and International Studies, concluded, the existing acquisition system:

"[R]esults in higher prices to DoD (even when lower-cost commercial alternatives exist for the same requirements), loss of a broad domestic production base that could be available to defense for peacetime and surge demands, and lack of access to commercial state-of-the-art technologies. Additionally, the wall between engineers and scientists engaged in commercial and military work impedes the kind of shoulder-to-shoulder contact that is the essence of technology transfer and that is basic to achieving greater job stability and growth opportunities for the U.S. work force."

To meet the new National security challenges (political, economic, and military) DoD must --

- Maintain its technological superiority, and a strong, globally competitive National industrial base that can support the Nation's future defense needs, by being able to:

- Rapidly purchase commercial and other state-of-the-art products and technology from reliable suppliers who utilize the latest manufacturing and management techniques;
 - Assist in the conversion of defense-unique companies to dual-use production;
 - Aid in the transfer of military technology to the commercial sector; and,
 - Preserve defense-unique core capabilities.
- Reduce acquisition costs (including DoD's overhead costs) through:
 - The adoption by DoD of business processes characteristic of world-class customers and suppliers (including processes that encourage DoD's suppliers to do the same); and,
 - Relief from the requirement to impose Government-unique terms and conditions on its contractors to the maximum extent practicable.

Maintaining Technological Superiority and A Strong National Industrial Base

While DoD drove technology developments in many areas for years, today the pace of commercial technology advancement in many sectors far exceeds Government sponsored technology efforts. Commercial technology advancements are outpacing DoD sponsored efforts in the same sectors that are key underlying technologies for military superiority (e.g., computers, software, integrated circuits, communications, and advanced materials). The current development and production of DoD systems takes too long. The design cycle for commercial technology is approximately 3-4 years, in DoD it is 8-10 years. Many DoD systems are technologically obsolescent at the time they are fielded.

DoD must have unimpeded access to commercial technologies more quickly than other countries if it is to maintain its technological superiority. Yet, many current laws and regulations are barriers to DoD's purchase of state-of-the-art commercial items, the conversion of defense companies to making commercial products on a competitive basis, and the integration of the defense and commercial industrial bases.

The following are most often identified by industry as significant barriers:

- Unique laws and regulations imposed on Government contractors, such as: Government cost accounting standards; the requirement to provide product cost data; record keeping and reporting requirements; audit and oversight requirements; access to competitively sensitive financial data; socio-economic and mandatory source requirements; requirements for rights in technical data; security requirements; and DoD-unique product and process specifications and standards.

- The instability of the Department's requirements and budget which makes it difficult to predict the market.
- Imposition of Government-unique rules on commercial subcontractors.
- The Government's right to terminate contracts at will.
- Industry's perception there is a tremendous risk that a contractor will inadvertently fail to comply with a Government rule or regulation that will lead to criminal or civil penalties, and a loss of the company's good name in the commercial marketplace.

Companies that do both commercial and Government business often are forced to segregate their facilities to ensure they can track, monitor, and report compliance with Government requirements, and account for inventories of components traceable to Government progress payments and their manufacturing origin. If the facilities are not segregated, the need to ensure compliance with Government requirements adds to the company's overhead costs, typically for both military and commercial products, since once the facility has the compliance systems in place they are generally applied to the entire facility. These additional costs, of course, make the company's commercial and military products less competitive in the global marketplace.

In the past many companies were willing to accept these additional costs because of the large volume of sales to DoD, and the fact that the Government reimbursed them for the costs on products it purchased. However, as DoD's share of many contractors' sales continues to shrink, the companies are often no longer willing to accept the additional costs and production inefficiencies associated with complying with Government administrative requirements. The cost is too high in today's competitive environment.

The semiconductor market is a perfect example of this situation. In 1965 DoD accounted for over 75% of all U.S. semiconductor purchases. By 1995, the Semiconductor Industry Association predicts that sales to DoD will be around 1% of all U.S. company sales. When DoD sales are such a small part of their market, companies are less willing to let the Government dictate to them the terms and conditions under which they will sell their product. They would rather concentrate on their commercial business or sell their products to the Government through third parties as a means of avoiding the unique Government rules and regulations.

In addition, with a procurement budget that has declined more than 60% in real terms since FY85, DoD and the Nation can no longer afford the luxury of maintaining a totally unique defense industrial base. The sharp decline in defense business, and the resultant mergers, acquisitions and bankruptcies of defense companies, is causing a dramatic shrinkage in the defense industrial base. Defense companies that are now supporting our existing weapons systems may not exist when we need them in the future. A reconstituted or larger defense production and logistics capability, if necessary, would have to be based on a National industrial base composed primarily of companies producing commercial or dual-use products, many of whom do not or will not do business with DoD because they will not alter their traditional business practices to comply with Government-unique rules and regulations.

Finally, the burden of defense reductions is felt most sharply by those companies who rely heavily on DoD for the majority of their sales, and small businesses. Those companies

who are most dependent on defense business are laying off hundreds of thousands of employees. This is not a temporary layoff pending an up-swing in the economy. These jobs are gone for good unless the company can convert to producing for a commercial market that will make up for the decline in defense business, or adopt another strategy to accommodate reduced defense expenditures while remaining a DoD-only supplier. Small businesses not only disproportionately feel the loss of business revenue, but also the unique burdens placed on Government suppliers. They least of all can afford to bear the spillover of additional overhead costs of doing business with the Government -- the additional employees to ensure compliance, lawyers to explain Government-unique laws and regulations, and the legal risks associated with an inadvertent failure to comply with a rule foreign to commercial business practice, but required when selling to DoD -- onto their commercial products. We must do everything in our power to remove these burdens.

Reducing Acquisition Costs Through Adoption of Business Practices Characteristic of World Class Suppliers

The Carnegie Commission on Science, Technology and Government, using an indirect measure of the cost of the DoD regulatory system, calculated that the overhead, or management and control costs, associated with the DoD acquisition process were about 40% of the DoD acquisition budget, as compared to 5% to 15% for commercial firms. *A Radical Reform of the Defense Acquisition System* (December 1, 1992). This figure includes both the Government's internal costs, and the costs borne by DoD contractors and ultimately reimbursed by the Government.

An Office of Technology Assessment study pegged the costs of DoD's regulatory maze at \$15 to \$75 billion, and concluded that the benefits could not be worth this additional cost. *Holding the Edge: Maintaining the Defense Technology Base, Volume II Appendix, CCGPO* (April 1989). Other studies have indicated that DoD contractors incur additional costs on Government contracts, for identical items being sold to commercial customers, of about 30% over their commercial contracts (e.g., *Integrating Commercial and Military Technologies for National Security: An Agenda for Change*, Center for Strategic and International Studies (Washington, D.C., April 1991)).

The problem is that DoD's acquisition system is a complex web of laws, regulations, and policies, adopted for laudable reasons over many years. For example:

- Military specifications were adopted to ensure DoD got a quality product that would meet the user's needs while using a procurement process that would allow it to buy from the lowest bidder; and to ensure standardization to enable ease of logistics support;
- Cost or pricing data requirements were established to ensure the Government received the same information the contractor had, for use in negotiating a fair and reasonable price;
- Cost Accounting Standards were adopted to provide accounting criteria that would result in comparable costs for like circumstances within a company and to ensure contractors properly allocated costs to DoD contracts;

- Checks on the Government's authority were established to in essence "protect the people" (in this case suppliers), from certain Government demands, such as the inappropriate use of fixed-price research and development contracts;
- Rights in Technical Data have been requested to ensure the Government can operate, repair and maintain its equipment without fear of being held hostage to a sole-source supplier for spare parts and to obtain additional equipment and spare parts at reasonable prices through competition; and,
- Laws such as the Davis-Bacon Act, requirements to use small businesses, and buy only American-made products, were adopted to further a particular public interest.

While each rule individually has (or had) a purpose for its adoption, and may be important to the process as a whole, it often adds no value to the product itself, and when combined, contributes to an overloaded system that is often paralyzed and ineffectual, and at best cumbersome and complex. If there were any doubt that the current system exacts a significant cost in terms of performance, quality, innovation, and prices the Government pays, one need only ask the Government's senior acquisition executives. In a recent U.S. Merit Systems Protection Board survey, a majority of Senior Executive Service members in the Federal Government stated "that the procurement process frequently results in procurement decisions that are neither cost effective nor in the best interests of the Government." *Workforce Quality and Federal Procurement: An Assessment (July 1992).*

There are other problems that must be solved. The existing DoD acquisition system -- not unlike that of many companies in the U.S. and around the world -- can best be characterized as an "industrial era bureaucracy in an information age." DoD and many of its suppliers are still practicing many management techniques and philosophies that were fundamentally developed by Adam Smith and Alfred Sloan. These philosophies are based on the following:

- Specialization, which led to economies of scale, as the most efficient way to produce products;
- Rigid lines of authority and reporting;
- Creation of rules or practices to address every contingency, if possible;
- Extensive paperwork to document that appropriate actions occurred;
- Detailed design and "how-to" specifications as the only way to ensure an acceptable product, and to ensure a "level" playing field for competition;
- In-process inspections, audits and reviews as the most effective means to assure compliance with the system; and,
- Programming people to conform to established procedures ensured that systems would be predictable, workable, and safe.

The result of these philosophies, however, as authors Michael Hammer and James Champy noted in their book, *Reengineering the Corporation: A Manifesto for Business Revolution*, is a system that is less than perfect in today's world. Systems of this type:

- Create functional stove-piping in which no one person is accountable for an entire process;
- Result in so many hand-offs during staffing that errors and waiting time dominate the system; and,
- Make the ability of any one person to change the process small if not impossible.

This system is at least partially to blame for the characterization by one senior service acquisition official that the DoD acquisition hierarchy had an unquenchable appetite for data and paperwork, was quick to second-guess decisions, and worse yet, revisited decisions endlessly.

People are encouraged to conform -- to follow the rules, to document their actions, and to avoid risk, rather than innovate and use good business judgment. The system rewards those who follow the rules and avoid risk. And it allows everyone to point the finger at someone else in the process -- Congress points to DoD's management, DoD points to Congress, and people within the services point to OSD leadership.

The layer upon layer of organizations, legislation, regulations, policies and oversight, is an impediment to DoD's adoption of business processes that are characteristic of world-class customers and suppliers today. Most companies have begun to recognize that in today's world flexibility and agility are more important than efficiencies achieved by specialization and other benefits attributable to the old management techniques.

DoD is unlike most commercial companies. It is populated by military and civil service personnel who have a different personnel system than most companies. Senior political appointees rotate frequently. There is generally no competition or threat to the organization's continued existence. There is no profit and loss sheet -- no "bottom line." No commercial company is scrutinized like DoD is scrutinized by Congress and the general public. And no commercial organization utilizes the acquisition process to achieve social goals to the extent required of Government agencies.

Yet the critical management issues are the same:

- There are too many people in the organization;
- There are too many regulations;
- There is resistance to change and a suspicion of process management; and,
- There is considerable "stove-piping" of functions and personnel, and massive coordination requirements.

Thanks to the ability and dedication of the thousands of acquisition professionals in the Department of Defense, and the assistance of many contractors, DoD has been able to develop and acquire the best weapons and support systems in the world. DoD and contractor personnel accomplished this feat not because of the system, but in spite of it. And they did so at a price -- both in terms of the sheer expense to the Nation and eroded public confidence in the DoD acquisition system. It is a price the Nation can no longer afford to pay.

While there have already been reductions in the acquisition workforce, continuing reductions in both military and civilian personnel (active duty reduced by 520,000; civilians by 200,000) and the need to reduce DoD's infrastructure mean that there will be further reductions in the acquisition workforce. DoD cannot accommodate these reductions without making changes in the current acquisition process. It must reduce the cost of the acquisition process by the elimination of activities that, although being performed by many dedicated and hardworking personnel, are not necessary or cost effective in today's environment.

No one is suggesting that there be a wholesale deletion of safeguards that have been designed to ensure the integrity of the Government acquisition process, nor the wholesale removal of laws intended to further the social policies of this great Nation. Rather, DoD must advocate a balancing of the risk associated with reducing oversight and the cost to both industry and the Government of compliance. In the case of social programs, the costs of maintaining records to ensure compliance must be balanced against: the contribution to be made by requiring compliance when making small purchases; and, the lost opportunities when commercial companies and small businesses are unwilling to change their standard business practices and contractor relationships in order to comply with a Government socio-economic policy imposed only on Government contractors.

CONCLUSION

Acquisition reform shares a common border with many of our most important goals: saving the taxpayer money; reinventing Government; strengthening our military; and improving our economy. To meet these goals in today's environment DoD must:

- Be able to rapidly acquire commercial and other state-of-the-art products and technology, from reliable suppliers who utilize the latest manufacturing and management techniques;
- Assist in the conversion of U. S. defense-unique companies to dual-use production;
- Aid in the transfer of military technology to the commercial sector;
- Preserve defense-unique core capabilities (e.g., submarines, armored vehicles, and fighter aircraft);
- Integrate, broaden, and maintain, a National Industrial base sustained primarily by commercial demand but capable of meeting DoD's needs;

- **Be able to adopt business processes characteristic of world class customers and suppliers (including processes that encourage DoD's suppliers to do the same); and**
- **Be free to stop applying Government-unique terms and conditions on its contractors to the maximum extent practicable.**

Removing requirements that are uniquely imposed on Federal contractors is the single most important step DoD, the Administration, and Congress can take to help defense contractors compete successfully in today's global commercial marketplace, to ensure DoD will have access to a National industrial base that can meet its needs, to ensure DoD will have access to the latest state-of-the-art technology, and to assist DoD in reducing its acquisition costs.

THE SOLUTION – A VISION FOR THE FUTURE

The Clinton Administration has proposed the first steps in a broad plan to re-invent the Federal acquisition system. The National Performance Review, led by Vice President Gore, provided Federal agencies with the following guidelines for their procurement systems:

- **Move from rigid rules to guiding principles (encourage innovation).**
- **Get bureaucracy out of the way (adopt pilot programs; raise the simplified acquisition threshold; change Government-unique laws to exempt certain types of acquisitions).**
- **Give line managers more authority and accountability (reward results, not just compliance with rules; focus on the customer).**
- **Give line managers expanded access to competitive sources of supply (use purchase cards).**
- **Foster competition, commercial practices, and excellence of vendor performance (increase reliance on the commercial marketplace; integrate the industrial base; increase use of electronic commerce; increase use of contractor past performance).**

These guidelines go hand-in-hand with the President's plan for economic development in the technology sector -- an issue critical to the maintenance of a National industrial base that can provide DoD with state-of-the-art technology. *Technology for America's Economic Growth, A New Direction to Build Economic Strength*, tasks the Federal Government to reform its procurement policies by:

- **Giving priority to commercial specifications and products.**
- **Investing in new technologies to facilitate their commercialization.**
- **Procuring innovative products and services incorporating leading edge technologies.**
- **Evaluating bids and proposals on a life-cycle basis rather than initial acquisition price.**

- Limiting Government acquisition of rights in technical data.
- Using performance based contracting strategies that give contractors design freedom and financial incentives to be innovative and efficient.

Using these guidelines, and the recommendations of the *Advisory Panel on Streamlining and Codifying Acquisition Laws (Section 800 Panel)* -- which are the cornerstone of DoD's legislative proposal -- as well as recommendations from the Defense Science Board, numerous commissions, and experts within the Department, DoD has developed its vision of a re-engineered acquisition system. This vision cannot be achieved through process improvement only. Because the world in which DoD now must operate has changed beyond the limits of the existing acquisition system's ability to adjust or evolve -- the system must be totally re-engineered. If DoD is going to be capable of responding to the demands of the next decade, there must be a carefully planned, fundamental re-engineering or re-invention of each segment of the acquisition process.

HOW TO RE-ENGINEER THE ACQUISITION SYSTEM (FOCUS AREAS)

The re-engineering process is optimally viewed through the framework of: how DoD determines what to buy; the acquisition process as a whole (with emphasis on major systems acquisition); how DoD procures or buys items; and, under what terms and conditions DoD negotiates with its suppliers. These issues must be considered in terms of DoD's need to maintain the United States' technological superiority and a strong, globally competitive National industrial base, while reducing its acquisition costs.

The following is an outline of the goals for the re-engineered system, listed in declining level of priority within each category -- in terms of the benefit to be achieved by changing the process, and the ease or difficulty in addressing the issue successfully. Following the goal are processes that must be examined or initiatives to be pursued, specific problems that have been raised, and any proposed solutions to achieve the goal that have been identified. This list is illustrative, not exclusive, and the priorities will likely change over time. Charters and schedules will be developed for Process Action Teams or Working Groups to address each of these and the many other issues which will require attention as the acquisition process is fundamentally restructured.

Requirements Determination and Resource Allocation (what to buy)

- Strengthen and enforce the preference for commercial items and ensure that requirements for systems, sub-systems, and non-systems acquisitions (including services) are stated in terms of required performance; and ensure that DoD-unique product specifications that inhibit the purchase of commercial items (either systems, sub-systems, components, or services) or dictate to a contractor how to produce a product or provide a service are not used, unless DoD-unique product or process specifications or standards are the only practical way to ensure the user's needs are met.

- Ensure the translation of mission needs/requirements into stable, affordable, environmentally sound, technically feasible, and best value solutions to a deficiency in current military capability or an emerging need, through a reexamination of the way DoD allocates its resources and establishes its needs/requirements. This process necessarily encompasses an assessment of cost, schedule, and performance risks, as well as National industrial base considerations.

- Analyze the PPBS, DAB, JROC, DPRB, and overall requirements determination processes (including an assessment of the use of simulation as a tool to facilitate formulation and re-evaluation of requirements during the acquisition process).

- Provide for the timely infusion of new technology so that new and existing systems are fielded with the latest technology available.

- Utilize prototyping and limited fabrication of advanced systems to determine producibility and operational effectiveness; and, evolutionary development and infusion of new capabilities in long-term stable production programs where contractor capacity is minimized, and lean, agile, production processes are encouraged.

- Provide for the appropriate participation of potential suppliers in DoD process action teams and working groups beginning at the earliest point in the cycle -- when establishing the system requirements.

- Allow DoD to leverage its investment with that of the private sector (a critical factor given the reduction in the defense budget).

- Support increased use of dual-use technologies and sharing of technology with the commercial sector (improve DoD's ability to develop and transfer technology from defense laboratories to commercial companies).

- Increase purchases of commercial products.

DoD Acquisition Process (how we buy)

- Streamline the acquisition process, focus on continuous process improvement, and ensure that the acquisition process is responsive to customer needs in a timely fashion.

- Ensure that DoD organizations (with the exception of those organizations whose mission is to perform inspection), are value-added team participants, not inspectors, both in relation to other organizations in the Department, and with respect to DoD's suppliers.

- Shift from a management philosophy that attempts to achieve high quality and performance through after-the-fact inspections, to one that prevents defects through controlling its processes, and reviewing the process controls of its contractors (focus on process control rather than hands-on inspections).

- Ensure that oversight, testing, and inspection (both internal and external), when necessary to ensure compliance with enunciated policies or requirements, are

performed in the least obtrusive manner necessary to add value to either the overall process or the particular acquisition, consistent with the risk of impact to the Government in the absence of such oversight.

- Ensure that reporting requirements, when necessary to ensure compliance with policy, include requirements for data that already exists and can be collected without undue additional administrative burdens, to the maximum extent practicable.
 - Ensure that policies and processes are structured so that the fewest number of people are involved in a given process, and the need for reconciliation or coordination is minimized.
 - Be able to balance the need for a particular policy or law to protect or further a Government interest with the need for efficiency and cost savings, and with the need to innovate and manage risk rather than avoid it (DoD cannot afford to maintain a "perfect" system).
- Provide incentives for acquisition personnel to innovate, while providing appropriate guidance and the benefit of "lessons learned" in the past.
 - Tailor acquisition policies and processes to the type of acquisition (e.g., commercial items, research, development, major systems acquisitions with little risk, with significant technical risk), rather than the current "one-size-fits-all" or "menu" approach, provide "alternative acceptable approaches" rather than mandatory policies (to ensure acquisition decision makers are provided additional guidance on appropriateness of certain clauses and requirements), and provide as much guidance as possible in the FAR or DFARS rather than individual organizational supplements.
 - Increase teamwork and cooperation to ensure sharing of "lessons learned" and prevent "reinventing the wheel" within the Government and industry.
 - Be more flexible and agile to be able to respond to the constantly changing threat and the pace of technology advancements. DoD needs to develop the most efficient, timely, and effective means of acquiring state-of-the-art goods and services to meet its needs at the best value to the Government (in the most cost-effective manner, over the life-cycle of the product or service), while protecting the public trust, and enhancing certain Government socioeconomic goals -- such as increased small and disadvantaged participation in the DoD marketplace.
 - Adoption of new acquisition strategies not geared toward full-rate production of all systems in research or development (e.g., limited production, roll-over plus, silver bullet strategies; lean production; concurrent engineering; flat production rates; and integrated product and process development).
 - Provide more funding stability and flexibility to manage programs in the best manner possible.
 - Develop innovative methods of funding that would alleviate inappropriate impact on program management (e.g., limiting use of concurrent engineering) caused by rigid rules regarding utilization of funding sources (e.g., anti-deficiency rules; "color of money" issues; etc.).

- Reduce unexpected program budget changes.
- Encourage innovation in products and practices, both in Government and industry , even if it will result in occasional mistakes.
 - Switch from serial design and production to a concurrent processes with integrated functional teams, through increased use of Integrated Product and Process Development, concurrent engineering, agile manufacturing techniques, information technology, statistical process control, and other commercial practices).
 - Encourage risk management rather than risk avoidance.
- Ensure that reductions in the acquisition infrastructure, including personnel and organizational changes, are made on the basis of changes in the acquisition process, rather than to reach arbitrary targets.
- Substantially reduce the time it takes to acquire products and services.
 - Streamline the source selection process for major systems.
- Make maximum use of technology to facilitate and enable re-engineering of the acquisition process.
- Establish clear measurements of system responsiveness.
- Eliminate functional stove-pipes and replace them with integrated decision teams that provide the necessary cross section of functional expertise to address and resolve program issues at the lowest possible management level.
- Empower people by providing appropriate education and training, moving decisions to the lowest level possible, and providing appropriate guidance, not rules.

Contract Terms and Conditions

DoD Must:

- Adopt the principle that, to the maximum extent practicable, the Government shall not impose on its contractors or subcontractors any law, regulation, policy, practice, process, or procedure, standard, specification ("terms and conditions"), that is unique to the Government, when purchasing a commercial item.
- Adopt the principle that, to the maximum extent practicable, the Government shall impose on its contractors and subcontractors no Government-unique terms and conditions, **unless:** that particular aspect of the buyer-seller relationship is not adequately "regulated" by market forces; the financial and ethical integrity of the Government acquisition process is not adequately protected; or, the furtherance of National domestic policies justify the use of a Government-

unique term or condition. If so, there should be a balancing of the Government's interests with the cost to the Government and industry of applying the Government-unique provision.

- Ensure that it buys on the basis of best-value and rewards past contractor performance.
- Avoid cost analysis and utilize market-based tools other than direct competition between like products, to determine a fair and reasonable price (e.g., comparison of price of new breakthrough technology with cost of technology that would be replaced; or comparison with alternative options to satisfy a need other than through the acquisition of that particular item). Transition from a cost-based system (primarily focused on justifying costs, not reducing them) to a price- or value-based system (price based on value to the customer -- whatever the market will bear) to the maximum extent possible.

MAKING REFORM A REALITY

Because of its complexity, a major overhaul of the acquisition system can not happen overnight. Many before have tried to fundamentally change the system and failed. The key to success is, that in addition to identifying the need for change, developing proposals for change, and enunciating the guiding principles for a new acquisition system, DoD's current senior leadership is committed to ensuring that changes will be accepted and institutionalized.

A Deputy Under Secretary of Defense for Acquisition Reform (DUSD(AR)) has been appointed to be the focal point for the development and implementation of a coherent and practical step-by-step plan for re-engineering each and every segment of the acquisition system. The DUSD(AR) has a small dedicated professional staff to lead and coordinate efforts to address the priority change areas identified by the Department's senior management. The Office of the DUSD(AR) will also follow-up to ensure implementation of recommended changes. The staff is purposely small to foster reliance on integrated decision teams made up of individuals who are actively involved in the day-to-day acquisition process, and who are in the best position to develop specific plans for change.

The DUSD(AR) chairs a DoD Acquisition Reform Senior Steering Group, comprised of the Vice Chairman of the Joint Chiefs of Staff; the DoD General Counsel; the DoD Comptroller; the Director, Defense Research and Engineering; the Director, Program Analysis and Evaluation; the Assistant Secretary for Command, Control, Communications and Intelligence; Director of the Defense Contract Audit Agency; the DoD Inspector General; the Directors of Defense Procurement and Acquisition Program Integration; the Service Acquisition Executives; the Director, Defense Logistics Agency (or individuals authorized to act on their behalf in representing the position of their organization). The Steering Group members make recommendations on proposed acquisition reform goals and objectives, further identify areas for change, assist in establishing priorities, designate experts from their activities to serve on process action teams and working groups, make recommendations to the DUSD(AR) on issues that could not be resolved by the teams, coordinate proposed actions within their organizations, and ensure implementation of final plans of action within their organizations.

Members from other organizations with acquisition authority or interest have been invited as advisors to the Steering Group, including: other DoD agencies with acquisition authority; the Assistant to the Secretary of Defense (Legislative Affairs); the Assistant to the

Secretary of Defense (Public Affairs); the Defense Systems Management College; the Director, Defense Performance Review; the Director, Acquisition Education, Training and Career Development; the Director of Operational Test and Evaluation; the Director, Test and Evaluation; the Assistant Secretary (Economic Security); the DUSD (Environmental Security); the DUSD (Logistics); and, the Director, CALS and EDI. By invitation, the following organizations will be asked to participate when common interests converge: representatives from other interested DoD activities; Heads of Contracting Activities; Program Executive Officers and Program Managers; Commanders of the Service Commodity Commands (e.g., ESC, ASC, TACOM, MICOM, NAVSEA, SPAWAR); other Federal Agencies and entities (such as the Office of Federal Procurement Policy, the National Economic Council, and the National Performance Review Team); and Congress.

Process Action Teams (PATs) and working groups, which will be utilized to develop re-engineering plans, and are key to the success of the acquisition reform effort, will be integrated decision teams -- cross-functional, cross-service and cross-agency. They will be responsible for:

- Analyzing a current practice;
- Identifying the costs (money, time, personnel) associated with that practice;
- Identifying "interested or affected parties" and consulting with them about the practice, alternative approaches, preferred solutions, etc.;
- Identifying alternative approaches consistent with the principles of the new acquisition system;
- Identifying incentives to encourage change to the new practice or process;
- Recommending the best option for addressing the issue, after identifying the ease or difficulty of adoption of a preferred option;
- Developing any new legislative, regulatory, policy, or administrative changes required to implement proposed options;
- Developing measures of success in making the changes so DoD can track progress;
- Developing specific implementation plans (specific actions; time in which to complete them, etc., including training of DoD personnel; and
- Developing a process for follow-up to ensure the changes have been institutionalized (in particular to identify incentives and other mechanisms to ensure change to, and compliance with, the new processes and procedures, as well as an organizational structure to supervise implementation of the plan).

The process action teams and working groups will include operational experts and staff advisors (as identified by the DoD Steering Group) from OSD, the Military Departments, and the Defense Agencies. The teams will also seek advice and participation from other Federal Agencies, Congressional offices, and industry as appropriate.

Finally, while the DUSD(AR) examines ways to re-engineer DoD's business processes, other DoD components will continue to pursue changes in policies, practices, and regulations to make the existing system function more effectively. These efforts will be coordinated with the DUSD (AR), either directly or through their Steering Group member, to ensure changes are consistent with the approaches being pursued by the Acquisition Reform office.

IMPLEMENTATION

DoD began the process of reform by targeting certain segments of the acquisition system that promise to yield immediate and substantial improvements in the critical areas outlined above. Acquisition reform priorities will evolve as DoD continues to interface with other organizations and entities conducting related efforts, such as the Vice President's National Performance Review, the National Economic Council (working defense conversion), and the Defense Science Board Task Force on Acquisition Streamlining, among others, and as the DUSD(AR) consults with the DoD Acquisition Reform Senior Steering Group.

Many of the DoD initiatives will also require coordination with and support from other agencies, such as the Department of Labor, the Small Business Administration, and various interest groups, such as industry, labor unions, and minority businesses. In addition, many of the initiatives could affect the entire Federal Government. DoD will work with the Office of Management and Budget, the Office of Federal Procurement Policy, and other Federal agencies with major procurement responsibilities, including National Aeronautics and Space Administration, General Services Administration, and the Department of Energy to ensure that, when appropriate, acquisition reform initiatives are applied consistently throughout the Government.

The first initiative was to develop a DoD position on all of the recommendations for legislative change contained in the 1800 page Section 800 Panel report (chartered by Congress in Section 800 of the National Defense Authorization Act for Fiscal Year 1991, P.L. 101-510). Given the number and complexity of the issues, developing that consensus as soon as it was accomplished is a tribute to the interest and dedication to acquisition reform of personnel throughout the Department.

DoD placed particular emphasis on two Section 800 proposals: the removal of impediments to the acquisition of commercial products by waiving Government-unique legislative requirements; and, streamlining the acquisition process by increasing the small purchase threshold to \$100,000, while also raising to \$100,000 thresholds for application of legislative provisions that apply only to Federal contractors. The remainder of the recommendations fall within the following categories: Contract Formation; Contract Administration; Major Systems and Testing Statutes; Defense Trade and Cooperation; Intellectual Property Rights; Contracting for Commercial Activities; Service Specific Acquisition Laws; and, Standards of Conduct.

After reaching a consensus internally, DoD began working with the Office of Management and Budget (OMB), the Office of Federal Procurement Policy, the General Services Administration, and Vice-President Gore's National Performance Review (NPR) staff on developing proposed legislation expanding the Section 800 recommendations to include all

Government agencies, and including legislative acquisition proposals from the NPR report. To avoid confusion, the Administration decided not to introduce its bill, but instead, to work within the framework of the bills that had already been introduced or were ready for introduction at the time -- S. 1587 and H.R. 2238. The process of exploring proposed alternative solutions to various issues in the legislative proposals (now including H.R. 3586, S. 1598, and the proposed Conyers/Clinger amendment to H.R. 3400) is proceeding. Hearings are scheduled in various House and Senate Committees throughout February 1994.

In addition, Congress had requested the submission of pilot program candidates in Section 809 of the National Defense Authorization Act for Fiscal Year 1991, Public Law 101-510, and in hearings during 1993. A proposed Pilot Program bill encompassing seven programs, was approved by the Administration and sent to Congress a few weeks before the end of the last session. The candidates proposed are: Commercial Derivative Aircraft (CDA); Commercial Derivative Engines (CDE); certain troop support items at the Defense Personnel Support Center (DPSC); Joint Primary Training Aircraft System (JPATS); Joint Direct Attack Munition (JDAM); Fire Support Combined Arms Tactical Trainer (FSCATT); and Global Grid.

The pilot programs are critical because they would "jump start" acquisition reform by allowing DoD to immediately buy certain commercial and commercial-like items using commercial practices (while awaiting implementation of the larger legislative effort). It is essential that DoD continues to press for adoption of pilot program authorization because the proposed bill requests legislative relief that is unique to the systems acquisition process, and has not been considered to the extent other recommendations have been (these laws were not reviewed by the Section 800 panel). Finally, even if the "Section 800" broader reform package is enacted, it will take some time for regulations to be revised and personnel to be trained. Putting the pilot programs in place now will achieve savings earlier while also keeping the momentum for change. In the interim OSD is reviewing and approving (to the maximum extent appropriate) recommendations from the program offices or organizations for regulatory relief to assist them in utilizing commercial products and processes.

DoD also participated in the National Performance Review (NPR) effort by developing its strategy and action plan relating to Acquisition Reform high priority issues. This was done as part of the Defense Performance Review. The report is expected to be released by the White House in the very near future.

Finally, DoD formed two PATs, composed of a cross-functional and cross-service and agency, mix of individuals. The first PAT developed a time-phased plan for a 6-month, 12-month, and 24-month implementation of a standard Electronic Commerce/Electronic Data Interchange system for DoD small purchases. The plan provides "one face to industry," and utilizes commercially available software, for processing contract actions under the small-purchase threshold. This system will allow vendors to connect with commercial Value Added Networks, that will access the entire DoD system at one primary and one backup site, and receive data on all planned purchases. The vendor will be able to provide a quote electronically, and the Government to make an award electronically. Individual systems already in place in the Services and DLA have shown tremendous improvements in productivity, prices, and small business participation. DoD-wide implementation will begin in February 1994. DoD is also co-chair, with GSA, of the Government-wide EC/EDI team established by the Administrator of OFPP pursuant to the President's October 26, 1993, Executive Memorandum. This will assure DoD and other Federal agency EC/EDI efforts are accomplished in a complementary fashion.

The second PAT is addressing the issue of military-unique product and process specifications and standards. This issue is one of the most difficult and complex issues facing DoD. The team was tasked to analyze why Government specifications and standards continue to be preferred despite the current (at least three year old) policy preference for commercial standards, and develop a plan to implement a preference for commercial and performance standards and specifications unless a Government-unique product specification or process standard is the only practical alternative to ensure a product or service will meet the user's needs. The PAT's draft report, which includes a detailed and forward-thinking plan of action, is being circulated within DoD for comment. Resolution of all comments, and presentation of the final report, including recommended actions, to the Under Secretary of Defense (Acquisition & Technology), will be accomplished by the end of February.

Additional PATs and working groups will be formed throughout 1994 to address other issues critical to re-engineering of the acquisition process.

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