AMERICAN FEDERATION OF GOVERNMENT EMPLOYEES, AFL-CIO

Dr. Everett B. Kelley
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March 15, 2019

Honorable Adam Smith
Chairman
House Armed Services Committee
2120 Rayburn House Office Building
Washington, DC 20515

Honorable Jim Inhofe
Chairman
Senate Armed Services Committee
228 Russell Senate Office Building
Washington, DC 20510

Honorable Mac Thornberry
Ranking Member
House Armed Services Committee
2126 Rayburn House Office Building
Washington, DC 20515

Honorable Jack Reed
Ranking Member
Senate Armed Services Committee
228 Russell Senate Office Building
Washington, DC 20510

Dear Chairmen and Ranking Members:

On behalf of the American Federation of Government Employees, AFL-CIO, (AFGE) which represents more than 700,000 federal employees who serve the American people in 70 different agencies, including approximately 300,000 in the Department of Defense (DoD), we appreciate your support of a strong national defense and your recognition of the importance of a professional, apolitical civil service supporting our uniformed warfighters.

We are very concerned about some recommendations made by the Section 809 Panel for Streamlining and Codifying Acquisition Regulations that might, to some, appear as well-reasoned streamlining and reform to the Department of Defense acquisition process. Nothing could be farther from the truth. In actuality, if these changes were implemented, they would compound the effects of previous misguided "reform" and result in large unnecessary costs. This would, while increasing contracting profits, predictably decrease funds that otherwise could have been targeted toward compelling needs such as military readiness, support to our uniformed volunteers and their families, and the replacement of aging war-fighting equipment.

Section 833(i) of the Fiscal Year 2019 National Defense Authorization Act (NDAA) established a delayed implementation date for the recently enacted expansion of commercial items definitions pending input on an implementation plan from the Defense Business Board, Defense Science Board, the Section 809 Panel for Streamlining and Codifying Acquisition Regulations and the Under Secretary of Defense for Acquisition and Sustainment.

- The January 2019 report from the Section 809 Panel recommends further limitations of Defense-unique requirements with a framework relying primarily on "readily available" and "readily available with customization" of products and services in the commercial market place.

- The Section 809 Panel couples this expanded "commercial buying" framework with recommendations to revamp the Department of Defense requirements process in the planning, programming and budgeting system through a "portfolio management" process, giving greater authority to the acquisition community to determine the actual requirements, as well as to reprogram funds across programs within a so-called "portfolio," with less authority afforded to the Military Departments in defining requirements and less oversight by Congress over programs.

- The Section 809 Panel additionally makes recommendations that would restructure cost accounting standards (CAS) to allegedly minimize the "burden" for government and contractors.

- Finally, the Section 809 Panel recommends Congress repeal and replace the inventory for contractor services based on its alleged reporting burdens on contractors and the alleged uselessness of the information.

A recent Department of Defense Inspector General audit, "Review of Parts Purchased From TransDigm Group, Inc." dated February 25, 2019, determined that "TransDigm earned excess profit on 46 of 47 parts purchased by the DLA [Defense Logistics Agency] and the Army, even though contracting officers followed the FAR and Defense Federal Acquisition Regulation Supplement (DFARS) procedures when they determined that prices were fair and reasonable for the 47 parts at the time of contract award . . . [o]nly one part purchased under one contract was awarded with a reasonable profit of 11 percent. The remaining 112 contracts had profit percentages ranging from 17 to 4,451 percent for 46 parts . . . TransDigm was the only manufacturer at the time for the majority of the parts competitively awarded, giving TransDigm the opportunity to set the market price for those parts . . . The FAR enables sole-source providers and manufacturers of spare parts to avoid providing uncertified cost data, even when requested, because of the less stringent requirements for awarding small dollar value contracts and commercial item contracts . . . DoD could continue paying excess profits on parts purchased from sole-source manufacturers and providers of spare parts if statutory and regulatory requirements continue to discourage contracting officers from requesting uncertified cost data and allow contractors to avoid providing uncertified cost data when requested."

AFGE predicted this outcome in a letter we sent to the Armed Services Committees on May 3, 2018 where we stated:

"This proposed change [in the definition for "commercial items"] simply highlights the real purpose of even having a definition for so-called "commercial items" – to exempt defense and other government contracts and contractors from the putative requirement to provide Truthful Cost or Pricing Data (10 USC §2306a and 41 U.S.C. Chapter 35). It is no secret that major defense contractors desire to bypass this important pricing law, as well as the related Cost Accounting Standards, and these seem to be the key drivers behind the revised definition [of "Commercial Items").

"These recommendations [of the Section 809 Panel] would "[fundamentally weaken the ability of the Department of Defense to make informed contract pricing decisions by wrongly attributing 'burdens' placed on contractors to CAS; and adopting the use of amorphous 'accepted commercial [accounting] standards and practices' which would return us to a world where contractors would adopt their own accounting practices for the depreciation of capital assets, accounting for the cost of deferred compensation, and the allocation of direct and indirect costs (to use only a few examples)."

The Section 809 Panel's discussion of CAS is superficial at best, and does not even consider the advantages that uniform cost accounting principles provide to the government in the negotiation, pricing and administration of contracts. The Panel's report simply asserts "burdens" and makes false claims that "commercial" accounting standards are more than adequate. This is the same contractor canard offered up when the Comptroller General chaired the CAS Board, and was soundly rejected then, as it should be now. Illustrating the Panel's simple and unsupported claims is the pressure that the Panel has already placed on the CAS Board to repeal CAS 409, Depreciation of Tangible Capital Assets. This is despite the fact that after personnel costs, depreciation costs are the largest element of contractor costs. This situation is identical to the one that pertained when the CAS Board promulgated CAS 409. Industry claimed the standard wasn't necessary and forced a Congressional hearing. Fortunately, recognizing that depreciation could be manipulated in various ways under Generally Accepted Accounting Principles, and also recognizing that accelerated depreciation schemes under the tax code could leave taxpayers vulnerable to outrageous contract costs, Congress left CAS 409 intact.

The 809 Panel's attack on CAS is simply a re-hash of previously repeated *non-sequiturs* and falsehoods concerning government contract cost accounting. Contractors want the government to accept whatever costs or prices they offer with little review or recourse for overpricing, regardless of contract type or the level of competition involved. As one well-known former government official has stated, "Acquisition reform" *(sic),* including calls to repeal or reduce CAS coverage, is about buying from contractors the way a seller would prefer rather than from the perspective of any sophisticated or intelligent buyer purchasing from a major supplier.

In addition, the Section 809 Panel has not made the business case for granting additional reprogramming authority to re-program for so-called "portfolio managers" covering multiple programs. The Section 809 Panel has not made the operational case for forcing the Department to let the so-called "dynamic market place" determine operational requirements. Doctrine, Organization, Training, Materiel, Leadership, Command, Personnel and Facilities must all be looked at holistically and not merely through an acquisition filter from the perspective of industry selling goods and services to DoD. Products from a "commercial" or "dynamic market place" may be more vulnerable to Cybersecurity risk than products or services fulfilled as military-unique requirements. Human factors integration in training and operating weapon systems and equipment should be considered based on tactical and operational environments and not simply the requirements as defined in the so-called "commercial market." Equipment standardization and interoperability considerations are competing goals to that of letting the commercial marketplace determine requirements. The Section 809 Panel is populated with industry and former procurement officials and does not include expertise from the requirements

and total force management communities of the DoD and is therefore biased solely to favor expanding procurement opportunities with the private sector.

The Section 809 Panel's recommendations to repeal and replace the inventory for contracted services based on its alleged reporting burdens on industry and lack of utility of the data does not accurately document and account for the full record reflected in Departmental testimony to Congress, several Government Accountability Office (GAO) and DoD Inspector General (IG) reviews, which we separately accounted for in detail in a letter to the Armed Services Committees dated May 5, 2017. That letter and the referenced testimony and audits should be reviewed when assessing the Section 809 Panel recommendations.

- The Section 809 Panel ignores Army testimony on March 29, 2012 before the Subcommittee on Contracting Oversight, Committee on Homeland Security and Governmental Affairs, where, consistent with earlier Army Posture Statements, the Army testified that it averaged 30 percent savings when it in-sourced, using its contractor inventory review process to identify costly or high risk contracts performing "critical functions" or "closely associated with inherently governmental" functions. And, when the Army curtailed its insourcing program and implemented a civilian Full Time Equivalent (FTE) cap, it testified how contractor spending escalated out of control. The Section 809 Panel claim that the contractor inventory is "useless" is further belied by the fact that the Department of Defense Instruction 7041.04, "Estimating and Comparing the Full Costs of Civilian and Active Duty Military Manpower and Contract Support" (July 3, 2013) cites the Army's contractor inventory data collection as a mature and authoritative source of cost information on direct labor costs and various indirect costs. Because this Army data showed indirect costs (including profit) that often were double direct labor costs or higher, it is evident the Section 809 Panel merely wants to suppress the collection of this kind of information by the Government. So much for the Section 809 Panel's misleading claim that the contractor inventory is useless information.

- Although the Section 809 Panel cites some of the GAO studies on the contractor inventory, it misleadingly characterizes the findings and recommendations. In particular, the Section 809 Panel tries to discredit the contractor inventory as "duplicative" because of its reliance on authoritative data sources from the accounting system for financial data and from the Federal Procurement Data System-Next Generation (FPDS-NG) for data describing the type of contract action and other types of procurement data, but then fails to acknowledge the shortcomings of FPDS-NG detailed by the GAO that the contractor inventory remedies. For example, FPDS-NG does not account for actual costs incurred by the Government from contracting (only estimated planned obligations), lacks the detailed fund cite information included in DoD accounting systems, and tracks contracts by contracting activity and not the true customer known as the "requiring activity."

- Finally, after malicious implementation by opponents of the inventory at the Office of the Secretary of Defense (OSD) level, instead of using the Army methodology described in the March 29, 2012 testimony to Congress for collecting the data to minimize reporting burdens and ensure quality control over the data collection, OSD opted to use a rigid DFARS clause to purport to "collect" the data. The Army had collected the data through its requiring activities by modifying statements of work rather than a contract reporting clause, and had established a help desk to assist contractors in using their own payroll systems to provide the data in the least burdensome manner possible, also performing quality control on the data when it was proactively collected in this way.

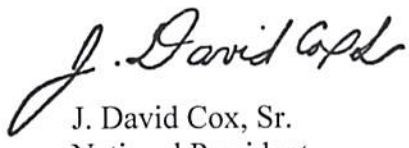
- When opponents of the contractor inventory successfully engaged with SASC to gut the contractor inventory statute in section 812 of the National Defense Authorization Act for Fiscal Year 2017, the DoD admitted in its February 25, 2018 submission that the scope of contract services covered by the contractor inventory had been reduced to 25 percent or $42 billion of the total $160 billion plus spent for contracted services at that time due to these statutory changes. HASC language in the FY2019 NDAA would have returned the contractor inventory to a viable statute covering the full scope of contractor services, but in conference this was only partly remedied by requiring the contractor inventory to include "closely associated with inherently governmental" functions for a subset of "services portfolios" above a $3 million reporting threshold.

- There seems to have been bi-partisan consensus within the Armed Services Committees that DoD lacks a meaningful and comprehensive contract services budget. For example, Ranking Member Thornberry when he was Chairman accepted the GAO finding that "Unfortunately, DoD – and Congress—have limited insight into how and where this [contract services] money is spent." , Unfortunately, Congress has deferred requiring this fidelity until October 1, 2021, and absent a comprehensive contractor inventory review process, we are skeptical that the Department will have a meaningful way to assess the credibility and completeness of its projected contract spending in the revised budget submission. Absent complete contract inventories and contract budgets, the $194 billion annually spent on contract services has to a great degree become the Department's slush fund and continuing to provide these funds to DoD is a blank check for the Pentagon.

We urge that all these recommendations from the Section 809 Panel be rejected and that the current delay in implementing the changes to "commercial items" definitions be extended pending the outcome of additional DoD IG and GAO reviews regarding the impact of these changes on costs and readiness; that the contractor inventory be properly scoped consistent with the recent reforms for a comprehensive contract services budget; and that the implementation of the contract services budget be made effective upon enactment of this NDAA holding the Under Secretary of Defense, Comptroller and Director, Cost and Program Evaluation fully accountable.

Thank you for considering these concerns. Should you or your staff have any questions, please contact John Anderson, (202) 639-6485, john.anderson@afge.org, or Richard Loeb, (202) 639-6466, richard.loeb@afge.org.

Sincerely,



J. David Cox, Sr.
National President

cc: SASC Committee Members
HASC Committee Members
SAC-D
HAC-D