TESTIMONY
OF
SENATOR LAWTON CHILES
ON S. 1264
BEFORE THE
SENATE ARMED SERVICES COMMITTEE
SETPEMBER 22, 1978

I want to thank you for the opportunity to testify here today. More importantly, I want to commend this Committee on the interest it has shown in moving forward on procurement reform. Procurement is not the most interesting issue we handle up here: it's not the hottest issue. But it certainly is one of the most important. Last year the Federal government spent over $84 billion to buy everything from safety pins to submarines. If improved purchasing practices cut costs just 5%, we could save over $4 billion annually.

Before outlining the ways in which S. 1264 would change current purchasing practices, and laying out the essential features of S. 1264, it's worth taking a minute to review what the purposes and characteristics of any government purchasing system should be.

The first question we need to ask is: What are the features of a good government pruchasing system? Any system should be efficient and economical. The government should strive to get the best product or service available at the lowest cost. That is the fundamental objective of any purchasing system.

There is one important feature which distinguishes the government purchasing systems from ones in the private sector: the government is not spending its own money, its spending the taxpayers money. Thus, it seems fair or equitable, that the government should operate openly in its purchasing practices, and insure that all businesses have a chance to do business with the government. The United States is unique in this regard. Many other countries have no requirement that governing purchasing be conducted openly. Since the Revolutionary War however, the concept of public advertising has been a central feature of this country's government purchasing system.

It would seem at first that these two objectives - the need to run both an efficient and an equitable purchasing system would conflict. How can we buy the best product if we have to take all these equity considerations into account?

The dilemma is easily resolved by relying on a phenomenon which accomodates both of these objectives: open competition. Open competition allows each potential bidder the opportunity to compete for government contracts. It also allows the government to rely on the forces of competition among bidders to get the best product at the lowest price. I would like to say that this idea of relying on competition is a new concept I developed. It is not, however. From the time the Second Continental Congress established the Commissary General in 1775, this requirement for open competition has been the fundamental feature of the federal procurement system. Competition is not something which a procurement system can create; competition is a phenomenon of the marketplace. A good procurement system is one which is able to go into the marketplace and draw out the competitive forces which are there.

The purpose of S. 1264 is to establish such a system. These objectives are not different from the objectives which Congress has always set for the government purchasing system. S. 1264 recognizes that the size of federal purchasing has mushroomed and the nature of federal purchasing requirements has become complex since the laws which govern the federal purchasing system were enacted over 30 years ago. It further recognizes that many of the features of the current system which were designed to stimulate now hinder it.

At the outset, however, it's important to indicate in very simple terms what S. 1264 would do to the current procurement system. S. 1264 is premised on the concept that many features of the present system actually act to inhibit competition: today's system is complicated, confusing, and filled with paperwork. S. 1264 would do two things to overcome these problems. First, it eliminates many barriers to entry into the federal procurement system by simplifying and streamlining the system. Second, it requires the government to focus on activities prior to contract award. This emphasis on prepurchasing activities is designed to make the government do what any prudent consumer does - to carefully check out what it's buying before it acutally buys it. It is a feature which is sadly lacking in today's system.

S. 1264 was not drafted overnight. In the late 60's Congress was confronted with cost overruns on major weapons systems, and with examples of waste and inefficiency in federal pruchasing practices. These revelations spurred the Congress to mandate a high level review of the entire scope of federal purchasing practices by establishing the Commission on Government Procurement. The Commission, composed of members of Congress, the executive branch and the private sector, worked for 2½ years and in 1973 issues a six volume final report which contained 149 recommendations for changes. I served on that Commission, as did Senator Jackson, who sponsored the Senate bill establishing the Procurement Commission. I have made the implimentation of the key recommendations of that Commission one of my top legislative priorities. S. 1264 builds on the recommendations of the Procurement Commission. The bill was introduced in the 94th Congress, revised and reintroduced in this Congress. The Governmental Affairs Committee held 5 days of hearings on the bill last summer and passed the bill out of Committee last fall. Because of the size and importance of military procurement, the Committee agreed to refer S. 1264 to the Armed Services Committee in order to benefit from the experience and expertise this Committee has in procurement matters.

Now I would like to discuss some of the important features of S. 1264.

S. 1264 establishes one statute to govern all executive branch purchasing activities. Currently, military procurement practices are governed by the Armed Services Procurement Act of 1947, and civilian procurement by the Federal Property Act of 1949. Each statute has its own set of implementing regulations, and each statute has been amended at separate times without regard to the other one. The reason for this disjointed development of the law stems from the fact that Congress has not tried to focus on purchasing as a government wide activity. Past laws were usually patchwork solutions designed to cure specific abuses. The result has been a number of inconsistencies between the two laws; inconsistencies which have been magnified in the flowdown from statute to regulation to actual practice. This characteristic cripples the government by creating confusion and paperwork which act to inhibit many businesses, especially small ones, from competing for government contracts. S. 1264 would establish a single, simple regulation for procurement, applicable to the activities of all the executive agencies.

S. 1264 puts the responsibility for issuing and revising the single procurement regulation in the Office of Federal Procurement Policy of the Office of Management and Budget. That office, was established by Congress to provide a top level executive branch focal point for the development of procurement policies. Its enabling statute stresses the need for openness in developing policies including notification of Congress prior to issuing any important regulations. These reporting provisions, coupled with similar provisions in S. 1264 will facilitate effective Congressional oversight of the procurement process.

The benefits of a single simple procurement regulation for all government agencies are many.

(1) Efficiency is enhanced by eliminating inconsistent practices.
(2) Red tape and regulations literally are cut in half.
(3) Competition is increased by reducing barriers to entry for businesses; this is especially helpful for small businesses.

FUNCTIONAL SPECIFICATIONS

S. 1264 requires the government to state its purchase requirements in functional terms, that is to describe the problem to be solved rather than deciding in advance what specific product will best solve it. A purchase description sets the ground rules which will govern the competition for the contract. A restrictive, detailed purchase description will restrict competition;it can lead to favoritism in awarding contracts. Look at it this way: if you let me write the purchase description, as detailed as I would like to, I guarantee that I could award the contract to anyone I wanted to. The extensive use of detailed purchase descriptions, which is so prevalent in today's system, not only confuses businesses, but restricts competition.

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Detailed product descriptions have many other detrimental effects. Probably the worst thing is the ban on innovation. With detailed specifications, new products with improved design and performance and lower cost, cannot even be considered by the government. Detailed specs often run thousands of pages in length, are difficult to understand and expensive to update and maintain. Functional specifications on the other hand are short, simple and easy to understand. They allow different approaches to a problem to be considered, encourage innovation, and broaden competition.

S. 1264 does recognize that there will be times when the government will have to use detailed purchase descriptions, and provides for their use. In spare parts or standardization cases, for instance, S. 1264 allows the agency to use detailed purchase descriptions.

A major consideration in any purchase decision is what type of purchasing method will bring out competition and allow the government to buy the best product at the lowest price. The current system states a preference for sealed bidding, but allows negotiations to be used if a proposed purchase falls into one of 17 specific categories. The exception has become the rule in current practice, with the Defense Department using sealed bidding for less than 10% of its purchases.

(1) S. 1264 changes the current law by eliminating the 17 exceptions which allow for negotiations and replacing them with a description of those purchase consideratons which need to be present for sealed bidding to generate competition.

(2) Under the current system, many products which could be purchased through sealed bidding are not; they fall into one of the 17 exceptions.

(3) The essence of sealed bidding is that it calls for pure price competition to determine who wins the contract.

(4) Thus, S. 1264 makes it mandatory that sealed bidding be used whenever the nature of the product to be purchased allows for competition based on purchase price.

(5) S. 1264 should increase the use of sealed bidding for two reasons: first, it does not give a blanket exception from sealed bidding to classes of products; second, the use of functional specifications makes it easier to consider different types of the same product under sealed bidding procedures.

(6) In my opinion, sealed bidding remains the best method to buy those products which can be competed on the basis of price.

(7) S. 1264 makes the use of sealed bidding the first consideration in any purchase situation.

Sealed bidding is not the cure to all the problems in procurement however, in many cases, sealed bidding simply won't generate competition or won't bring about the most effective purchase. A prudent consumer considers more than the sticker price when he buys a car: he looks at gas mileage, frequency of repair records, safety features and the like. In the same way, the government needs to look at design features and total ownership costs as well as the sticker price when it buys a major system or contracts for advanced research and development. It would be imprudent to expect the government to buy F-15 fighters through sealed bidding; much more than the sticker price needs to be considered. Competitive negotiations on the other hand allow the government to compete other factors in a purchase, such as quality of design and total ownership costs.

Current law says very little about negotiatons. It gives little guidance as to how negotiations should be conducted, and barely distinguishes competitive negotiations from non-competitive negotiations. As a result, under today's system once you decide not to use sealed bidding, it's almost as easy to make a sole source contract as it is to use competitive negotiatons.

S. 1264 on the other hand makes a clear distinction between competitive and non-competitive negotiations. It states that competitive negotiations, when used in the appropriate circumstances, is a valid way to obtain competition. On the other hand, S. 1264 makes non-competitive negosiations, or sole source contracting, extremely difficult to use.

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For competitive negotiations S. 1264 sets out some much needed ground rules to insure that each competitior will be treated fairly. It requires the government to indicate the relative importance it plans to attach to each evaluation factor at the outset of each competition. It also sets up a definite start and finish to the negotiation process, and prohibits practices such as auctioneering, which have lead to buy-ins and cost overruns in the past. Generally, S. 1264 calls for a limitation on detailed negotiations early in the negotiation process. The limitation does not prevent the government from talking price issues with each competitor, nor does it force the government to commit itself to a single contractor prematurely. This limitation is intended to eliminate the current practice of drawing up definitive contracts with each competitor before selection, a costly and time consuming process. It also is designed to encourage each competitor to come forward with his best offer right away, rather than starting a protracted gaming process. Finally, it is intended to prevent the government from combining aspects of each competitor's proposal with every other proposal. That practice, in the past, has led to the purchase of unproven products which only exist on paper and which combine characteristics taken from every competitor's proposal.

For non-competitive, or sole source negotiations, S. 1264 takes an entirely different approach. I believe that there is too much unjustified sole source procurement today, and S. 1264 is designed to make it much more difficult to award contracts without the benefit of competition.

Before making a sole source award, agencies would be required to meet two requirements. First, the agency must make a detailed justification for going sole source. The determination does not ask: what exemption are you using this time but rather, "what efforts did you make to find other firms? Why are these delivery schedules so short? What are you doing to increase competition the next time around?" That detailed determination then must be approved at a high level in the agency, a tightening of current procedures.

In addition to the determination requirement, S. 1264 forces the agency to subject its intention to award a sole source contract to an actual market test. It requires that notice of any non-competitive award be publicized.

If any company comes forward in response to the notice and has the capability to meet the job requirements, then the agency must award the contract competitively. This approach recognizes that internal determinations, no matter how detailed, represent the agency's opinion as to how much competition exists. S. 1264 calls for the marketplace to determine if competition exists, not the agency.

After a contract is awarded, the government must have the ability to assure itself that a contract price is reasonable, and that the quality of the product meets the standards called for in the contract. Effective contract auditing and cost controls are an absolute necessity if we are serious about spending the taxpayer's dollar prudently. Because there are two procurement statutes and a multitude of differing audit systems, however, government audit requirements have become confusing, inconsistent and overlapping. The absence of standard audit procedures causes agencies to duplicate and diffuse government surveillance efforts, and imposes a heavy regulatory and paperwork burden on businesses.

S. 1264 establishes uniform, consolidated audit procedures which will reduce paperwork for businesses, while strengthening and focusing government audit efforts. The Truth in Negotiations Act is retained and extended by statute to all executive agencies. The Truth in Negotiations Act allows the government to adjust contract prices downward if a contractor submitted inaccurate cost data or pricing data.

Section 306 of S. 1264 provides the contracting agency and the General Accounting Office with the authority to examine a contractor's books and records. This section is based on the access to records authority currently contained in the Armed Services Procurement Act, with two changes. First, it requires agencies to coordinate their inspection and audit responsibilities, thereby eliminating duplicative audits contracted by different agencies. This will save paperwork for the contractor and allow the government to use its auditors more effectively. Second, it gives the agencies the authority to conduct "should-cost" audits to determine if a contract work is being performed efficiently and economically.

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The most effective way to insure efficient contract performance is to make sure that contracts are awarded competitively, and that the contractor, not the government, bears the risk in performing the contract. The erosion of competition in today's system, however, has lead to the creation of a system of elaborate supplemental controls to assure prices equivalent to those obtained through competition. Those controls are necessary for large contractors, and for contractors who do little competitive business. Smaller businesses, businesses operating in a competitive atmosphere and businesses willing to bear all the risk for their contracts must have strict internal cost controls if they are to stay in business.

Consequently, S. 1264, while giving the government broad access to a contractor's records, allows companies whose business is predominantly competitive and who have limited cost-type contracts with the government to apply for a 2 year waiver from certain management efficiency requirements. This waiver is designed to focus those requirements. This waiver is designed to focus those requirements where they are needed most -- on large contractors and on contractors who do not touch controls over individual contracts on the contrary, these controls are broadened and strengthened by S. 1264. All costs must be legal and necessary for performance.

Any company which does more than $10 million in non-competitive government contracts could not apply for this waiver. Any company which has more than 25% of its revenues in non-competitive contracts could not apply for this waiver. The waiver lasts for two years and may be cancelled by the agency at any time. The waiver exempts eligible contractors from reviews of the reasonableness of elements of a contractor's indirect or overhead costs. The premise behind the review is that companies who operate in a competitive environment will be forced to control their management costs and will do so far more effectively than extensive surveillance would. This waiver provision is similar to the CWAS concept the Defense Department uses but is far stricter in its eligibility requirements and applies only to smaller contractors.

Section 509 provides a waiver from the requirements of the Cost Accounting Standards Board under the same eligibility rules. This waiver is similar but not identical to one which the CAS Board itself put into effect earlier this year.

This question is: should the government have one standard for all of these waivers or should the Cost Accounting Standards Board be allowed to use a different standard from everybody else? To me, it only makes sense that you have one standard for a waiver. To do otherwise goes against one of the basic goals of this bill: to eliminate unnecessary inconsistencies in the procurement system.

I can appreciate the Cost Accounting Standard Board's desire to be able to make its own exemptions without regard to all the other agencies in the government. But I think the needs of the entire government must override the concerns of one agency.

In closing, I would like to raise an issue which I hope the Committee will give careful consideration to: the question of U.S. purchases from foreign governments and international organizations. The Department of Defense suggested that S. 1264 be amended to enable the government to make such pruchases without regard to the procurement laws. The Governmental Affairs Committee was sympathetic to the concerns raised, but felt that the Armed Services Committee should consider the impact of any such proposal.

Furthermore, I was puzzled that the Defense Department did not set forth specific examples of problems which have arisen from the lack of such authority today. In any case, I think that if such an authority is granted, it should be carefully limited, and Congress should play an active role in its operation.

What I have tried to do today is set out the basic purposes of S. 1264, and dicsuss some of the major changes it makes in the current procurement system. There may well be some other matters which need to be worked out, and I stand ready to work closely with this Committee in working out any such questions.

In closing I would like to thank this committee for the interest it has shown in procurement reform, and for its commitment to move this legislation forward expeditiously.

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