



**PROBLEMS OF MILITARY PROCUREMENT
BY THE
DEPARTMENT OF DEFENSE**

Honorable Kenneth E. BeLieu

NOTICE

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Reviewed by Col E. J. Ingmire, USA on 7 February 1964.

**INDUSTRIAL COLLEGE OF THE ARMED FORCES
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28 January 1964

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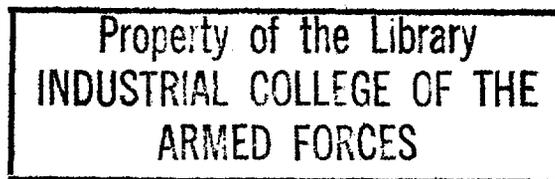
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Reviewed by: Col E. J. Ingmire, USA Date: 7 February 1964
Reporter--Grace R. O'Toole



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ADMIRAL ROSE: Gentlemen: As a major segment in our study of National Logistics Management, we give our attention to what is often called the biggest business in the world. I, of course, refer to the Defense procurement, which dwarfs in value the combined business of the very largest private enterprises. We all saw General Motors statement yesterday-\$15 billion worth of sales. We have \$51 billion worth of procurement. That is spending our money.

After distinguished combat service, not only in the Army during World War II and in the Korean action later on but also later on Capitol Hill, as a Congressional committee staff director, our speaker today has tackled the most hazardous combat duty of all, namely, top management responsibility for the Navy's \$8 billion annual procurement.

It is my pleasure to introduce the Honorable Kenneth E. Belieu, who will speak on Problems of Military Procurement by the Department of Defense.

Mr. Secretary.

SECRETARY BELIEU: Gentlemen: I think the definition of combat on the Hill and combat in this job is more appropriate than actually in combat. I sometimes think that the job of administering any amount of procurement when it gets over a billion dollars is the crossroad of all human interest.

I thought I would talk to you this morning about the basic fundamentals that we are trying to do in Defense procurement now as a matter

of emphasis. If I were to make one observation, based on my nearly three years of association in Defense management at the Department of Navy level, it would be that during this time our management approach has certainly not been static. This is particularly true in the procurement field. We have seen new approaches, new uses of old techniques, and new emphasis given to identifying the problem areas and to solving the procurement problems, many of which are not new.

I couldn't help but look at a list on my desk done by Earl Chesney in 1952. Some of you know him. He had some 20 items showing a racer going over hurdles: Buy American, Buy Canadian, Conserve Critical Material, Check Financial Responsibility, Encourage Subcontracting, Make Sure of Adequate Bid Time, Look to Distressed Areas, What About Offshore Procurement, Small Business, and Disperse Contracts. These are not new, but these are the things we are looking at again today in a different way.

These new approaches are in response to a number of influences. To give us a common perspective, I think our best approach is to look at Defense broadly and from several areas. I assume you know that in Fiscal Year '63 the Defense Department, in its procurement activities, consummated some 10½ million actions for about \$30 billion. This represents about 32 percent of the Federal Defense expenditure--not Defense, rather, but the whole Federal expenditures. Significantly, they accounted for approximately 5 percent of the gross national product.

The immensity of this task alone is enough to create substantial management problems. Add to this the fact that a large part of our dollars is going into research and development and highly sophisticated hardware,

and you have a management challenge that demands our most creative talents. I think we should also note that our changing Defense and Space programs have undoubtedly a significant impact on the economy as a whole. Many thousands of prime contractors, both large and small, as well as their subs, are not only subordinate but dependent upon us in varying degrees, and, since research and development is important to the national economy as well as to the defense effort, the impact of our programs on the national economy may be even more profound than the dollar volume I mentioned before. This, added to the fact that many hundreds of thousands of workers are employed by companies supplying our needs, shows the impact of the program on our Nation's economy. Program changes, cutbacks, and new contracts affect the very livelihood of these people.

Local community and State leaders are always concerned with the impact of defense industry on the economic and social health of their areas. At the national level there is understandable concern to insure that these huge expenditures for defense are made in a manner consistent with economic aims and objectives of the Government. Thus, ranging from the individual taxpayer to the leaders and thinkers at the national governmental level, there is continuing concern with Defense procurement because of its economic impact.

Now, we all know that the needs of national security are accepted as paramount by all. However, elements of our society--government, industry, labor--have corollary interests and objectives which are compatible with and, in fact, essential to this paramount objective. These

interests include several social and economic ends, including aid to small business and the support of distressed areas.

Looking at our procurement program from still another point of view, we see that contracting is the medium through which most of our hardware provided to our operating forces comes into being. It is through the contract that we are also preserving and continuing our traditional reliance on private industry and the free-enterprise system. The contract, therefore, becomes the key that determines the relationship between government and industry. This being the case, pressures are brought to bear on the contracting process from many quarters. Our operating forces demand reliable weapons and expect that we make every attempt to speed the delivery of hardware and that we keep pace with the advanced state of the art.

Business wants more business. Congress and the public, while demanding that we practice frugality and assure equal opportunity to all, also require that we consider the social and economic needs of the Nation. Our responsibility is to integrate these demands.

I thought we ought to look a little bit at the history of the Armed Services Procurement Act of 1947. Our present procurement law was born out of our experiences in equipping the Armed Forces not only during World War II but prior thereto. Most of us have had some experience, going back to almost World War I. If you look at the history you find that there was no definite planning prior to World War I. We had too many independent acting agencies, bureaus, and services, and competition between them, to

the end result that, after 18 months in World War I, Lloyd George said, in substance: It is a paradox of history that the greatest machine-producing nation on earth failed to turn out the machines of war after 18 months of toil and sweat. Pershing said the same thing.

In World War II it was different. We started out the same, however, but it was accomplished by several actions. In World War I and subsequent thereto, Assistant Secretaries were established in the War Department and in the Navy for these purposes. Attention was given to past mistakes in advance planning, and people were given the responsibility for taking certain actions. This experience clearly showed the need for a law that would permit us to award contracts by negotiation when the national interests or sound business judgment dictated, and yet to still preserve and require the time-tested procedures of formal advertising, where this method of procurement was feasible and practical.

Our present law fulfills this bill. It has enabled us to operate well in times of peace. That is not to say there have not been criticisms and recommendations for change. In the last three years Congress has given evidence of still greater concern. While we may think this is new, because maybe you and I are in jobs that require more attention to procurement practices, it is interesting to go back in time and find that, prior to World War II, it was practically impossible to let a contract other than under the formal advertised, competitive procedure. I don't know whether I pronounce his name right or not, but a Major General Benjamin Foullait, who was then Chief of the Army Air Corps,

elements of restricted, competitive procurement are, first, set-asides for small business and labor-surplus areas, and, second, small dollar purchases made by local installations, usually from local suppliers, after taking two or more quotes. In the latter case, the Department of Defense made over 6½ million purchases in Fiscal Year '63.

Now, were we in this area to engage in nationwide, formal advertising, we estimate that our operating expenses would be increased by at least \$100 million. I think we should note, too, that basic procurement patterns have changed considerably in the last decade. In today's dynamic environment it is becoming difficult to plan for stable and steady procurement of conventional, volume-production weapons. Since Korea the purchase of electronic, missile, and other new weapons has risen from 12 percent to over 50 percent of our annual placements. The weapons programs of the type which have emerged in the last decade have typically involved very large awards not readily susceptible to formal advertising, nor for that matter to direct price competition.

To a large extent the resultant contracts have been made on some form of cost-reimbursement basis. As a result of this we have witnessed a sharp increase in the use of cost-plus-fixed-fee contracts. I gave you the figure for 1941 a while ago. In 1951, for example, 13 percent of DOD requirements were on cost-plus-fixed-fee contracts. In 1961 the percentage was three times that. This amounted to almost \$9 billion of our procurement dollars, or nearly 40 percent of the total obligations.

In April 1962 a committee chaired by David Bell, then Director of the Bureau of the Budget, submitted its report to the President on government contracting for research and development. The Bell report had this to say about the cost-reimbursement type of contract:

"This type of contract has well-known disadvantages. There is little or no incentive for private managers to reduce costs or otherwise increase efficiency. In combination with strong pressures from governmental managers to accomplish work on a rapid time schedule, it probably provides incentives for raising rather than reducing costs. If a corporation is judged in terms of whether it accomplishes a result by a given deadline rather than whether it accomplished that result with minimum cost, it will naturally pay less attention to costs and more attention to the speed of accomplishment. On the other hand, without a given deadline, a CPFF contract may serve to prolong the research and development and induce the contractor to delay competition."

The Bell report then recommended a number of ways the contracting system can and should be improved. These were:

Provide more incentives for reducing costs and improving performance;

Give more attention to the feasibility studies in the development of specifications prior to inviting private proposals for major systems development, thus reducing brochuremanship, with its heavy waste on scarce talent;

Improve our ability to evaluate the the quality of research and development work.

Today a great deal of effort is going into carrying out these recommendations. In one area a complete revision of the Armed Services Procurement Regulations was issued last year. This revision establishes the firm fixed-price contract as the most preferred type, because here the contractor accepts full responsibility and the greatest amount of risk. Likewise, the greatest incentive to reduce costs exists under this type of contract, for the contractor receives the full benefit of every dollar by which he reduces cost.

The use of cost-plus-fixed-fee contracts is now limited to basic research, or study contracts, or a few developmental contracts where the unknowns are so great that feasibility cannot be clearly established. In all other cases which apply to most future contracts for development, the Department of Defense has established the objective of employing incentive contracts. These incentive contracts generally fall into two categories: cost incentives and performance incentives. Most everyone is familiar with cost incentives. It consists of a target cost, a target profit or fee, appropriate ceilings, and a share of the savings, or for added costs above this target.

The sharing formula is generally expressed either as a percentage ratio or on an incremental basis. For example, the contractor might receive 10 percent of the dollars by which he underruns the target cost.

Performance incentives are a bit more difficult to define and measure clearly. They are also difficult to measure objectively both as to dollar value and actual attainment. The number of possible

performance incentive goals will depend in each case on the equipment being procured and on the areas in which improvements are desirable. Some of the more simplified examples are such things as the speed, range, weight, rate of climb, or other performance of an aircraft. Performance incentives can also be applied to deliveries, reliability, accuracy, or meeting the specified milestones.

One other factor worth noting with respect to performance incentives is that they will rarely be used without accompanying cost incentives. It stands to reason that we want to achieve the best overall performance at the lowest overall cost, and we cannot expect to achieve the cost part of that goal if we use performance incentives without cost incentives.

Of course there exist varying degrees of resistance to incentive contracting. Among others, there is the theory that time proves that the potentially greater short-range profits provided by incentive contracts are not effective tools for reducing costs. Again the theory is advanced that a contractor's ultimate costs will be approximately the same regardless of contract type, the major difference occurring in the establishment of the original estimated cost. This theory holds that contractors will avoid cost overruns on incentive contracts by inflating target costs rather than reducing costs, and that the Government will be powerless to prevent this.

Regardless of the validity of these theories, which cannot be proved or disproved at this time, there are other valid reasons for using incentive contracts. One of the most important is the effect of

negotiations on incentives and what this effect will have on program or program management. In the past it has been a fairly simple matter to start expensive research and development projects under cost-plus-fixed-fee contracts without first defining the objectives or establishing reasonable estimates of cost. Precise project definitions can be and frequently are postponed for long periods by such practice. Measurement of contractor efficiency is virtually impossible under such circumstances.

It is true, of course, that it is not easy to estimate the cost of research and especially of development, but the really difficult areas in to estimate and control/basic research and exploratory development are at the early part of the R&D spectrum, and are rather small in terms of dollars. Industry, as well as government, devotes over 50 percent of its effort to engineering develop^{ment} and operational systems development. This type of work can and should be estimated and controlled more precisely.

The process of objectively defining an undertaking before commencing work is one which makes good sense, regardless of the type of task. However, in the case of the development of modern weapon systems, it becomes particularly important. Therefore, the Department of Defense is now employing project definition which will center most of its application activity in major weapons development. Project definition involves the solicitation of a number of early study contracts whose purpose is to simply define the project prior to authorizing full development. A decision for full-scale development effort can be made after going through

this definition phase. It can be made with greater assurance that cost estimates are sound, that system performance will meet the promise, and that the military requirement will be fulfilled at the time needed.

It is the purpose of project definition to force both our own people and industry to plan out how a program is to be developed and to isolate the major problems and resolve those first. The key is advance study and planning.

I might just mention here a couple of the pros and cons pertaining to project definition. One of the most common is the time factor. The argument goes something like this: "If all things were perfect we would of course do this, but we don't have the time; we can't do it now." Well, the answer is that we are only kidding ourselves if we think that by launching a full-scale development effort it will save us time. We must at some time do this work anyway. We must do the work involved in planning and preliminary engineering. Everyone will agree to this, so then it is simply a question of whether the work is interwoven among all the development and production activities which have to take place, or whether it is pulled forward into a special period prior to commencement of developments.

In addition to project definition another important product of incentive contracting is the fact that it will will contribute information regarding contractor performance which should be of substantial assistance in evaluating the contractor under a performance evaluation system. We are now in the process of implementing this system.

The contractor performance evaluation system is designed to provide future military source selection boards with a realistic analysis of past performances of competing companies. There have been a good many subjective feelings on this score for a long while, but no centralized record.

CPE is designed to provide something better--an objective judgment on how wisely the contractor promised and how well he actually lived up to his promise. This evaluation program will be placed in effect initially only on development contracts that exceed \$5 million a year or whose total cost is around \$20 million.

Contractor performance evaluation will make an important contribution in shaping proper incentives for Defense contracting. It will provide for longer term rewards for good performance on past contracts. While contract incentive arrangements will provide for shorter term rewards for good performance on contracts.

One other tool has been devised to assist in our efforts to increase the use of incentives. This is the development of weighted guidelines, a method of determining the objective target profit. This method was developed as a practicable and necessary means of protecting the traditional and restrictive profit philosophy of many negotiators. The weighted profit guidelines, which are applicable to only noncompetitive, negotiated contracts, are designed to give our negotiators a better means of analyzing cost proposals. The guidelines will show what profit rates should be used and what a given contract effort is proposed to produce.

In detail, the policy lists factors which the negotiator should consider in arriving at his decision as to what would be a reasonable profit and assigns a numerical range of weights for each factor. It contains instructions as to the selection of specific weights within the range, and thus provides rather precise, quantitative guidance to assure that the policy is applied in a uniform manner.

Among the factors to be applied are the extent to which the contractor is willing to undertake high-risk contracts, his record of past performance, the degree of special achievement required, the amount of his own facilities and capital and other resources that he will apply to the contract, and the difficulty of the contracting task.

One can see from all of this the extent to which the different attacks on the CPEFF problem have been tied to each other. The emphasis on incentive has required the employment of project definition. To achieve both short and long range incentives has required the development of the CPE and weighted guidelines.

However, we are not only pressing toward greater efficiency in our procurement program. By moving into project definition in the use of incentives, we are also striving to bring down the cost of our weapons through increased competition. Our objective is to obtain weapons with a high level of performance and reliability for use by our operating forces. We also recognize that a large portion of what we contract for does not have a potential for increased competition. A large percentage of the dollars we spend goes into research and development, and aircraft and

missiles which are not susceptible to price competition. We are therefore aiming our attack at the residual which is primarily represented by spare parts and end items.

Sole-source or noncompetitive procurement is not as inevitable as it sometimes appears. Many procurements become sole source by default. In the formative, precontracting phase of procurement, they are allowed to harden into a noncompetitive posture so that, when the time for contracting is reached, there is no choice but sole source. The sole-source problem must be viewed in the broadest possible context. It is not enough to say that the law binds the contracting officer to competition unless there are sufficient facts to preclude competition. The central issue is whether the reasons of expediency supporting the sole-source decision should have been permitted to develop in the first place. These reasons are usually one of a combination of three things--there are no drawings; the equipment is highly specialized; or the need is urgent.

Concerning this predicament the Deputy Secretary of Defense said recently:

"We must constantly challenge cases where performance and delivery deadlines do not permit adequate advance preparation and force the use of noncompetitive procurements."

The solution to the sole-source problem lies in reducing the occasions where poor planning or deficiencies in one of the of the earlier steps in the procurement process stymie competition. Advanced procurement planning is our answer to this problem. Advance planning starts at the time the

requirement is conceived and it takes that requirement through 3 to 5 year periods, so that those things necessary to obtain competition are planned for in advance. This means that such matters as its procurement history, economic factors, and lead-time estimates are cranked into decisions. It provides for definitive delivery dates and for technical dates, and separates potential competitive items from those which are clearly noncompetitive. With this knowledge decisions can be made to provide for effective competition.

These things that I have mentioned are among the major projects that have been undertaken by improved Defense procurement. Achieving success in these programs is going to be difficult. The present efforts, while geared to the past, are bolder and more intense. They force us to shake off old habits. They force us to adopt new ways of doing the job.

For these procurements to be successful, it will be necessary for all persons involved in the procurement process--requirements, technical, and contracting people--to work closely together as a close-knit team. An understanding by all members of the team of objectives to be achieved is essential. The need will require extensive training, and training teams have been developed. These courses are now being given throughout the country to all members of the procurement team. In addition, senior procurement-policy people in DOD have been spending much time with our people throughout the country, not only reiterating the philosophy but outlining the detailed procedures that are involved and effective. We

must ever be mindful that to project our strength abroad we have to preserve this strength at home.

Back in 1942--we are talking about small business now--they also said, there arose considerable sentiment to authorize and require purchasing agencies to pay premiums to small plants and to firms located in depressed areas. It so happens today, of course, that one of the cornerstones of our economic and political strength is the small business. More than 4 million small business concerns make up at least 95 percent of our entire business population. This represents 9 out of every 10 businesses. They act as safeguards against the concentration of power in any one area or one group.

But this is not the only reason we should concern ourselves with the welfare of small business. It is part of our strength for peace and also for war. Because of the tremendous volume of Defense purchasing, it is absolutely essential that small business be brought into our purchasing programs to the greatest possible degree. Failing this, we may find the industrial structure of the country altered simply through the size of Defense procurement.

In Fiscal Year '63 we spent \$4.3 billion in small business, or 16.5 percent of our procurement dollar. This was a decrease of 1.2 percent from the preceding year. While the percentage went down, the actual dollar figure went up. The best means we have for achieving an increase in the small business share of our procurement is through the efforts being made to increase competition. In so doing, we not only benefit

pricewise and qualitywise but also the record shows that when small business has an opportunity to compete for contracts its share of awards increases.

Another area of concern in procurement management is the effect that shifts in Defense spending from one section of the country to another have in creating distressed labor areas. Our studies in this area reveal that a heavy increase in Defense contract awards does not guarantee full employment, nor do heavy losses necessarily forecast rates of unemployment above the national average.

While the ability to obtain Defense contracts is of significant economic value to a community, our contracts constitute only one source and one element of prosperity, and this fact that we are only one of a number of forces at work must be kept forever in proper perspective.

In August of this year Senator Humphrey submitted an amendment to the Defense Appropriation Act, the purpose of which was "to allow more efficient use of government procurement in helping distressed areas." This amendment would permit the use of total set-asides for procurement for awards to areas of substantial labor surplus, rather than partial set-asides, which is the present situation.

The Department of Defense opposed this amendment for two reasons:

1. We think that total labor-surplus set-asides are undesirable since they would jeopardize making awards to the best qualified firms, they would probably cost more, and they would subject our contracting people to intense pressures from affected communities.

2. It is doubtful that total set-asides would in fact alleviate the unemployment problems of communities, when viewed on a national basis. Instead it probably would reshuffle the burden of employment from one area to another. A distressed area that receives a Defense contract and moves on to the labor-surplus category would be then denied the right to participate in follow-on contracts, and work would shift elsewhere.

We think a more realistic approach is the one we are now following.

First, we are assisting firms in labor-surplus areas to obtain Defense work by keeping them informed of opportunities, by encouraging primes to subcontract to them, and by making optimum use of partial set-asides.

Second, the economic utilization staff in the Department of Defense works with employees, companies, and communities which are adversely affected by changes in Defense programs.

These problems and improvements in Defense procurement are some of the more important ones we have today, but by no means do they cover the entire range of activity.

I planned to discuss something with you about the Navy organization, but I didn't know how long my voice would hold, nor did I think I could see my speech today because of a cold I had over the weekend. I prefer, if you have questions on Navy organization and management pertaining to procurement, that you take that up later.

I would like to emphasize in conclusion of these formal remarks that our efforts here have one purpose, and that is to keep America

strong. Regardless of the procedures and the format of our procurement system, we have only one objective in mind, and that is to field the best trained and best equipped fighting force we possibly can to meet a threat, or else there would be no reason. These procedures are simply designed to allow us to do this in the most efficient manner.

I think you remember hearing President Johnson recently when he talked to the Pentagon about a month back. He said, "I look to you not only to protect your country but to protect your country's purse; to safeguard not only her military strength but her financial stability."

This I guess represents a good enough creed for any procurement officer.

Thank you for the opportunity of presenting these remarks to you. I apologize for the fact that my voice is not up to fettle. I hope I'll do all right with the questions when they come around.

CAPTAIN CASTELAZO: Gentlemen, the Secretary is ready for your questions.

QUESTION: There was a statement in the paper on Saturday by Mr. Obolenski about prolonging big contracts like Dinosaur and Skybolt and hesitating to chop the projects off in terms of the economic impact. Would you care to comment on that?

SECRETARY BELIEU: Fortunately, I didn't have much to do with Dinosaur, excepting when I was on the Hill. I would gather that this comes to the moment of decision, as to whether you are going to go ahead

with it or not. If you are going to stop it, in my opinion, once you have made up your mind, unless there are scarce talents that you have to keep, the best decision that the contracting officer can make is, "We'll do it right now."

I have had cases, and one case particularly, as some of you know, on the big dish, where it took us about a year to make up our minds, and we spent \$2 or \$3 million a month during that period. So, if you are going to spend that kind of money for nothing, you'd better stop it now. The argument comes as to whether it is for nothing or not.

I was just talking in terms of the distressed-area aspect. Somewhere along the line in government there has to be a compassion for this, but in a military organization the first and primary decision has to be made on what you are getting for your dollar, with the exceptions of the technicians that you might need.

I don't know whether I answered you well enough or not. It's not an easy question to answer.

QUESTION: Mr. Belieu, with the emphasis today on incentive contracting and the need to make better measurement insofar as incentive factors of price, quality, delivery, performance, and the like are concerned, and also with the contract performance-evaluation procedures, are we taking any steps to refine the techniques of measuring these particular factors insofar as the end results are concerned?

SECRETARY BELIEU: Yes, we are. Of course you put your finger on two very controversial subjects--contractor evaluation and incentives.

You can get an argument on these on any part of the street if you want. We have issued instructions-- we'll take incentives to start with--to get a rule or format or matrix, if you please, for the contracting officer to negotiate and operate from, giving him a spread of percentage figures on these types of things--price, performance, and so on.

The idea of the incentive is not new. It was used in World War II. Certainly the first aircraft contract with the Wright brothers was an incentive contract. If I remember correctly, that was on range, or it might have been speed. I have forgotten. If you put all your emphasis on price in incentive contracts, you may substitute price for performance. It has to be an educational process. Each incentive contract has to be signed or approved by the Secretary concerned, the materiel Secretary. Then it has to be watched through its life.

On contractor evaluation, this was also done during World War II. It's sort of like efficiency reports on people. They are worth while up to a point. Most of us, when we look at the efficiency report of an officer, will also look for the signature of the guy who rated him. I think the great danger in contractor performance evaluation is that the team of a large manufacturing entity does not always stay as constant as perhaps the performance of a given individual. On the other hand, if you take no action, how do you measure? What do you put in your memory bank?

QUESTION: Mr. Be Lieu, will you discuss the results of the contract administration study that was made on Project 60?

SECRETARY BELIEU: Yes. As you know, it is undergoing a pilot run now up in Philadelphia. The only gripes I've recently had have been from comptrollers who want to hold a meeting next week because they are fearful that Project 60 gets into their audit area. Maybe it does. It's too early to tell what is going to happen on this. The idea was to establish a Defense Contract Management Agency to do all the functions that we do in inspecting and administering the contract in the field, and to put these together and avoid duplication.

The Air Force argued strongly against it. The Navy took a relatively positive approach toward it. We all said, "Let's only go into the pilot-run phase at the current time and see what comes out of it."

I can't give you much beyond saying that it is going through the trial-and-error procedure up at Philly right now. We'll undoubtedly have some big arguments on it before it finally shapes down.

QUESTION: Mr. BeLieu, there is great emphasis being placed on improved contract techniques right now, and we still see the same amount of pressure being put on for small business set-asides and distressed-area set-asides. This puts the contracting officer in a very precarious position. There are these diametrically opposed policies that he is supposed to be following.

SECRETARY BELIEU: Yes, I think it does, sometimes. Your law does not allow you to spend extra money for a contract even in a distressed area or for small business. There are two aspects. Take the small business first, however. We were discussing this during the break. I have

argued that the 16.5 percent I mentioned before is a fallacious figure. If you are talking small business and 95 percent of your base consists of small business, the real, key point is: Where does this money eventually go? How much money really goes to small business at the end of your contracting procedure? The figure of 16.5 represents those contracts which we make directly from our own major procuring activity, but does not consider the subcontractor level.

I have talked with many leaders in industry. I remember talking to the head of Raytheon not long back. He said that 50 percent, or a little bit less, maybe, of his contract dollars went to subcontractors in the small business area. This would indicate that really, we are getting a greater return or a greater result as far as the small business is concerned.

I tried to talk this over with the Small Business Committee on the Hill, but it went over like a lead zeppelin. They weren't interested in the subcontracting bit so much as they were in the direct percentage we apportioned out and that came out as a natural factor of our procurement.

The distressed areas is a difficult one. We who work in the military services sometimes hoist ourselves on two horns of a dilemma. We think nothing of utilizing Exception 16 for mobilization purposes, to put a contract somewhere where we want it for military purposes. Sometimes I wonder if we shouldn't exercise some sort of judgment in this field because of the dispersion aspects of it. We have in this country now concentrated a great percentage of our industrial might along the coastal

regions. If you draw a line from a 100-fathom depth 100 miles in, you pick off 80 percent or thereabouts of our population and our industrial capacity.

There is another aspect which is not necessarily yours and mine, but it seems to me that we have to be somewhat attuned to it. The President, being the Commander in Chief, must look at the welfare of the whole country. People say we shouldn't pay attention to this. Some do. On the other hand, in our own household, when one youngster doesn't do well one year in English we say, "I'll put my attention on you, but the next year it goes on Johnny on arithmetic." So we have to pay some attention to distressed areas, I believe, but not to the detriment of the equipment we receive or the timeliness of it. But we can't ignore it.

QUESTION: Mr. Belieu, until recently the Office of Naval Materiel reported directly to you and handled important contracting and procurement functions for you. Recently, as the result of reorganization, the Office of Naval Materiel has been given a new status and new responsibilities. Would you discuss any procedures and relationships existing as a result of this reorganization with respect to procurement?

SECRETARY BELIEU: Maybe you will answer that. You have been briefing me ever since I came on board. Now, under the Navy management plan, you might as well call it reorganization, I guess. The Chief of Navy Materiel did report directly to me, and I had authority in certain areas under Paragraph 5 delegated to me by the Secretary of the Navy. Under the new plan he reports directly to the Secretary, but, as it is operating

now I find little difference. The responsibilities of the Chief of Naval Materiel were augmented and strengthened because we had four somewhat monolithic bureaus working somewhat by themselves--not completely.

Every time you have this system you find that the coordination is beautiful at the staff level, but when you get topside on policy you sometimes don't have this. So we felt that we needed a cap in the bureaus. This cap, because it contained more things than the Navy materiel function that rightly accrued to the man in my position--such as R&D, comptroller functions, and so forth--had to then become responsible to the Secretary of the Navy.

On the other hand, the only authority I have is that which is delegated to me by the Secretary of the Navy. There is no statute that tells me my authority. He gives it to me in any kind of order he wants to name. So I still go to the Chief of Naval Materiel and he comes to me on those things in my purview. In fact, I go to him on other things as well.

Then under him he has deputies who report--this is our hope--directly to each of the Assistant Secretaries involved. He took over the second of December, if I remember correctly, or about that time, and there are still some growing pains, but I think it will work out.

QUESTION: Mr. Belieu, from the standpoint of design specifications or design standards, do you ever think it is possible to lick the language barrier between the user, the engineer, and the contract specialist?

SECRETARY BELIEU: It's hard enough to lick the language barrier

between the Army and the Navy. I can speak from experience. I spent 18 years in the Army. I suppose we will if we can go a certain length of time without changing signals again. I don't know that we ever will, exactly, no. You can't answer this one definitely. As long as I have been in town, and that has been since 1942, with the exception of the war years, we've had a reorganization of the Defense Department every time we've had a new Secretary.

QUESTION: Mr. Belieu, as you indicated this morning, there has been a considerable change in progress of procurement in the last several years. What in your view are the major problems and challenges that we can look forward to in the future?

SECRETARY BELIEU: First, the things we discussed today--competitive procurement, et cetera--are the bread-and-butter guidelines. But I think the biggest challenge is the one we have always had with us since World War II and probably before, and that is melding our procurement to well-known and well defined requirements, requirements predicated upon a concept of operation and doctrine and strategy. This is the key thing. The procuring man, the G-4 of the outfit, the Opo-4 of the Navy, the A-4, or whoever it is who has this function, never tells the commanding general or the commanding admiral that he can't perform. He shouldn't. He should just tell him up to what level he can. But he has to be in the operation from the gleam in the eye, from the plan or start of a new system, because today a weapon system is almost a decision in strategy. This, I think, is the key problem that we have in the procurement of the future.

QUESTION: One of the major procedural changes in contracting, I think, was the Presidential Memorandum of last October which in effect alarmed all the agencies as regards patent rights. He said, I think, "The Government shall normally acquire title to all patents." Now, this is diametrically opposed to the traditional DOD practice and the old title policy. Is it too early to say what the effect of this has been? I am sure industry must be unhappy about it.

SECRETARY BELIEU: Industry is not too happy. I understand this is an off-the-record meeting. I ran into this first, to my knowledge, when I was on the Hill in the Space Committee. The space outfit had a different patent-taking provision than Defense, and also with Senator Russell Long. I think there has to be a protection of patent rights to private industry. It's easy enough to say that those things which we pay for in government belong to us, and I guess we must have this. On the other hand, if I hire you to do a new job for me, and you come up with new ideas that were aborning in your outfit before we started, there has to be some proprietary right, I think.

I don't know the answer to it. It's a conflict in beliefs. It's a conflict in philosophy. Patents are private property. If properly defined and properly developed, there must be an honor to them, I think.

I haven't answered your question. We won't answer it in the kind of climate we have now.

QUESTION: I noticed in a recent publication that in the organization of the Navy, the Project Manager reports directly to the Chief of

Naval Materiel. How do Project Managers tie in with the bureaus, such as the Bureau of Weapons, or ASW?

SECRETARY BELIEU: We have two types of project managers. The type on which you want to put high emphasis, such as Polaris and the 3-T Program, were taken away from the bureau and in effect superimposed on the bureau, because their line of functioning crossed the line of functioning of several bureaus. By that then they can be brought up to or just below the level of the Chief of Naval Materiel, who can then give command guidance and support in resources, personnel, and money, if needed, by transferring from one account to the other, and therefore keep on top of the project that crosses several bureaus. Then you have a project manager within a bureau, and he is confined basically to the bureau. He just stays there.

QUESTION: Mr. Secretary, what can we do to make sure that buying from the lowest bidder won't lead to decreasing the cost of maintenance and the stocking of parts?

SECRETARY BELIEU: It will in some cases. You have to know your specifications, and you have to know what you want to buy, and you have to give a performance specification with this. There is no question about that. In complicated systems every once in a while we run into it. We had a buy for the Air Force not too long back when we thought we could go it competitively, but they came back and said, "No, not for us, because every new item we add to the supply business costs 100 bucks."

The only way you can do this is to make sure that your specifications

are correct. Even then you are going to pay a price for them.

You ought to be interested in knowing that in 1938 a guy by the name of Louis Johnson gave a speech in Chicago. I used to think that the Astronaut was the fellow who said, "My God, look. Everything in here was built by the lowest bidder." But this is not true. Louis Johnson was the originator of that. He said, "It's absurd, in talking about formally advertising the buying of Army trucks, that the Army must be forced to buy its trucks from the lowest bidder."

So we've gone around and around on this, and yet on trucks it was possible to get some sort of compatibility of standardization.

QUESTION: Mr. Belieu, I understand that, if a contractor makes a handsome profit on an incentive contract, he is subject to losing his profit through renegotiation. Is this true? If so, is anything being done to remove this hazard to the incentive contract?

SECRETARY BELIEU: It was true. If the Renegotiation Board doesn't get the word, it doesn't believe in it. We have held meetings with the renegotiation people to educate them on this incentive program that we have. I've had leaders of industry come in and say, "Well, this is fine. We'll take a flyer at it, but they will take our money away from us." It remains to be seen on that. We haven't had enough current experience, I believe. But it certainly could happen.

QUESTION: Mr. Belieu, we have recently had a speaker from industry indicate that despite the policy of the Secretary of Defense the negotiators still do not really support the incentive contract that he desires.

Will you comment on what we are doing about this?

SECRETARY BELIEU: Well, there is always somebody who doesn't get the word. This is true. I think that in an organization as big as the combined Defense procuring activity, it takes a while to get the word out. Speaking from my own experience, 2½ years ago, or thereabouts, when the emphasis came on incentive contracts again, always you had this talk at the top level and this bit of implementing, so it took a while to get the word down.

But we are letting more and more incentive contracts. I think the word is getting out.

QUESTION: Mr. Secretary, a couple years ago there was a DOD procurement management conference and the report on that indicated that our procurement operations were a training ground for industry negotiators, so that a lot of people migrated out of government into industry. That led me to wonder if perhaps the industrial contract negotiators are perhaps of higher quality than our government contract negotiators and we suffer a disadvantage. Is this true?

SECRETARY BELIEU: I don't think they are of higher quality. I think we have a problem of recognizing our government negotiators by proper rewards either in rank or recognition of the job they do. As a result of that we have a difficult time keeping good ones. There is no question that if we don't keep our good people they will go out to industry. It's like a poker game--they'll fade us every time. They'll whip us every time. For both military and civilian people in this field we need greater

continuity in office and greater recognition on the job to be done. I think also that we need to spend more time on people per se. We need to give our negotiators field trips, to give them an opportunity for broader education, and to move them out into industry over a period of, say, a couple months. Then they can come back and go to school. These things we can do and should be doing.

CAPTAIN CASTELAZO: Mr. Secretary, I thank you very much for coming over here and giving us the advantage of your knowledge.

SECRETARY BELIEU: Let me read one thing to you, if I may, because I want you to make certain that I have taken a stand on everything. If you haven't heard this, I want to read it to you.

They're talking about a candidate for office. He said, "I had not intended to discuss this most controversial subject at this particular time. However, I want you to know that I take a firm stand on every issue, regardless of how I feel about whiskey. And here is where I stand on this burning question: If you mean the devil's brew, the poison scourge, the bloody monster, the defier of the innocent, that liquid that dethrones reason, creates misery and poverty, and literally takes the bread out of the mouths of babes, if you mean that evil concoction that topples Christain men and women from the pinnacle of righteousness and gracious living into the bottomless pit of despair and degradation, shame, helplessness, and hopelessness, then I am against this brew of Satan with all my power.

However, if you mean that oil of conversation, that philosophic wine and ale that is consumed when good fellows get together, that puts a

song in the heart, laughter on the lips, and a warm glow of contentment and well-being into the eyes, if you mean Christmas cheer, if you mean the toddy that puts a spring in the old man's step on a frosty morning, if you mean the drink that enables a man to magnify his joy and happiness and forget his debts, if you mean that drink the sale of which pours into the Treasury untold millions of dollars which are used to provide tender care for little, crippled children, our aged, our blind, our sick and infirm, and to build highways, hospitals, and schools, then I am for it.

That is my stand, and I will not retract one word, nor will I compromise. You asked for my stand. There it is."

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