

Competition is inherent in the acquisition process. We are committed to the use of competition to ensure fair and reasonable prices for our military hardware. However, we must also ensure that what we buy is responsive to our needs. To achieve a reasonable balance is our objective. There will always be some instances one could point to where a suboptimization on price competition was not achieved. Such instances should not be misinterpreted as either a lack of commitment or a failure to adhere to a policy.

ESTIMATING WEAPON SYSTEM COSTS

Unrealistically low cost estimates have long been recognized as the beginning of cost growth problems and as a major source of program instability, "buy-ins," incorrect cost-effectiveness trade-offs, unmet force level goals, and a host of other problems. Some analysts believe low cost estimates to be the fundamental weakness in the entire system for acquiring defense hardware.

Question 1. Do you believe faulty cost estimating to be one of the fundamental weaknesses in the system for acquiring defense hardware? If not, what is, and how does low cost estimating rank as a problem?

Answer. Initiative No. 6, Budget to Most Likely Cost, is an important element of the Acquisition Improvement Program. As I indicated in my prepared statement, unrealistic cost estimating is a major cause of cost growth. In the past we have been overly optimistic about the projected outyear costs of programs. The cost growth that results from this optimism produced tincreasing instability, stretch-outs, and more cost increases. It is a vicious cycle and a difficult one to reverse.

Question 2. Please list the remedial measures in place and planned that address cost estimating and provide the Committee with a progress report on their implementation and results to date.

Answer. We have been performing intensive, independent reviews of cost estimates to minimize the use of low initial cost estimates. We now require program managers to use independent cost estimates and also require the Service Secretaries provide an explanation of any decision leading to a choice of a budget based on the lower estimate (independent or program manager's) and to provide plans for ensuring the budget is met.

OSD held a special review of independent cost estimates of 10 major systems in 1982 (F-15, AIM-54D, F-16, LHD-1, AV-8B, Bradley, Pershing II, Navstar, DIVAD, and AMRAAM). For 1983 this special review will be expanded to 25 programs.

Because cost estimating will no doubt be a recurring problem I have included it in the six major initiatives that I intend to personally emphasize.

EXPECTED COST SAVINGS FROM MULTIYEAR PROCUREMENTS

The multiyear contracting concept, No. 3 on the list of 32 DOD acquisition improvement initiatives, was promoted as a way to save in the range of 10 to 20 percent in unit procurement cost through improved economies of scale and efficiencies in production processes, economy-of-scale lot buying decreased financial borrowing costs, better utilization of industrial facilities, and a reduction in the administrative burden of placing and administering contracts.

In Mr. Carlucci's testimony before this Committee last year, he announced that the Defense Department planned to initiate four multiyear contracts in fiscal year 1982 (the F-16, C-2 and UH-60 aircraft and the Troposcatter Radio). In Dr. DeLauer's recent testimony before the Procurement Subcommittee of the House Armed Services Committee, he stated the Defense Department had recently submitted six new multiyear candidates to begin in 1983 and eight more in 1984. Dr. DeLauer announced at that hearing that the cumulative savings resulting from these 18 multiyear contracts will exceed \$4 billion.

There are, of course, a number of impediments to achieving these cost savings. To begin with substantially all, if not all, of the contracts are sole source (noncompetitive). If the negotiated price is higher than it should be, or DOD has selected the wrong clauses in the contract, the Department is locked in for three years.

Question. What specific implementing guidance has the Department of Defense issued to assure that:

(a) Current, accurate, and complete cost and pricing data is available to Government Officials at the time they negotiate these contracts.

(b) Profit rates are established at levels that are directly related to the relative degree of risk the contractor must take, and the clauses that tend to shift the risk factor significantly toward the Government are not inserted arbitrarily.