AMERICAN FEDERATION OF GOVERNMENT EMPLOYEES, AFL-CIO

Eric Bunn Sr.
National Secretary-Treasurer

Dr. Everett B. Kelley
National President

Jeremy A. Lannan
NVP for Women & Fair Practices

March 1, 2022

Honorable Kathleen H. Hicks
Deputy Secretary of Defense
1010 Defense Pentagon
Washington, D.C. 20301-1010

Dear Secretary Hicks:

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.

I write concerning the recent Department of Defense (DoD) Report "State of Competition within the Defense Industrial Base" (February 2022) issued by the Office of the Under Secretary of Defense for Acquisition and Sustainment. AFGE appreciates DOD's recognition that the state of the defense industrial base (DIB) has been severely weakened by disastrous policies encouraging defense industry consolidation since the 1990s.

President Biden's July 9, 2021, Executive Order 14036, "Promoting Competition in the American Economy" serves as an excellent starting point for a re-examination of the dangerous policies pursued by DoD for the last quarter century which have resulted in a vast consolidation of contractors and a resulting lack of competition for equipment and goods needed by our armed forces. The dependency on a very few prime contractors has placed the military in a tenuous position with respect to maintaining competitive pressure both in terms of innovation and pricing placed on the government's principal military contractors.

As the DOD report accurately observes:

> Since the 1990s, the defense sector has consolidated substantially, transitioning from 51 to 5 aerospace and defense prime contractors. As a result, DoD is increasingly reliant on a small number of contractors for critical defense capabilities. Consolidations that reduce required capability and capacity and the depth of competition would have serious consequences for national security. Over approximately the last three decades, the number of suppliers in major weapons system categories has declined substantially: tactical missile suppliers have declined from 13 to 3, fixed-wing aircraft suppliers declined from 8 to 3, and satellite suppliers have halved from 8 to 4. Today, 90% of missiles come from 3 sources. As a result, promoting competition and ensuring it is fair and open for future programs is a critical Department priority. (Footnotes omitted.)

As much as the report is accurate in its observations, the solutions proposed are a "day late and a dollar (trillions of dollars actually) short." In at least one instance, the accuracy of the background information provided in the report is misleading in the extreme.

Intellectual property (IP) limitations in defense procurement are a critical vulnerability. Contractors have taken advantage of various legislative changes they have lobbied for over the past twenty-five years which have bolstered their financial positions at the expense of the Department's ability to fully utilize IP to its advantage even when research and development costs have often been borne by taxpayers. While the Competition Report acknowledges these shortcomings, it simultaneously genuflects to the defense industry by continuing to champion these failed business policies.

AFGE represents thousands of employees who work at DoD depots and arsenals (the "Organic Industrial Base") who are directly affected by the limitations the Department has acceded to and often championed, particularly the so-called "commercial item" definition. This inventive and completely misleading term often classifies necessary defense equipment as "commercial," as if it can be purchased through the nearest chain store or on a web site. In fact, the term was developed by contractors primarily to shield themselves from the rigors of competition specifically with regard to pricing and IP. The "commercial" moniker automatically cedes IP to contractors and prevents hard-nosed negotiation of price, both of which are intolerable in sole source situations, where the "commercial" label does the most damage. AFGE's members often encounter outright resistance from contractors when they attempt to repair or overhaul so-called "commercial" equipment, with contractors refusing to provide technical data for what is clearly defense material. In some instances, our members have been threatened with lawsuits by contractors for even attempting to reverse engineer equipment or component parts.

The Competition Report is both inaccurate and misleading in its description of "commercial items" appearing on page 12. First, the report states that FASA [the Federal Acquisition Streamlining Act of 1994] included a preference for Commercial off the Shelf (COTS) items instead of the time-consuming and expensive process of creating government-unique items. That statement is patently inaccurate. COTS are not even mentioned in FASA. What FASA really did was create a new preference for purchasing faux "commercial items," which are often defense unique equipment re-labeled as commercial under a definition that conceivably makes everything the Department purchases fit under the "commercial" label.

Subsequent to the enactment of FASA, there are now really two forms of "commercial items": 1) Commercial items and commercial services; and 2) Commercial off the shelf items (COTS), the latter of which the Competition Report inaccurately references. To set the record straight, COTS are what in one form or another have always been called commercial items, and that definition, although its wording has changed over the years, has existed since at least 1962. COTS are the types of items any person can go into a store and buy or go online and purchase.

In contrast, the genius of FASA was to create a form of *non-COTS* "commercial items and services" that are known as "of a type" commercial. These "of a type" items are not available in the commercial marketplace, and are often openly defense or government unique. But, DoD using the FASA definitions and related regulations, qualifies these goods for so-called "commercial item" treatment. This "commercial" treatment includes failing to obtain certified cost or pricing data regardless of contract price in sole source situations, and ceding all IP to contractors. AFGE's continuing concern with the "commercial item" definition (as opposed to real commercial items per the COTS definition) is that it is a Trojan horse for doing business with contractors with none of the traditional safeguards that apply to government contracting.

The excerpt from the Competition Report also misleads in that after inaccurately describing the FASA preference for COTS, it seems to infer that DOD is now buying COTS (actually the Department has always purchased COTs without needing special procurement procedures or clauses). The Report then switches its coded language to state that "... Since then [referring to FASA], DOD has dramatically increased the use of commercial item procurements." That statement is true, but it is not COTS that have dramatically increased. It is *non-COTS* faux "commercial item" procurements such as for the C-130J military transport aircraft that have increased, as well as contracts for all manner of specialized military equipment purchases that are now classified as "commercial items." By merely changing the definition of what qualifies as "commercial," the Department has magically increased the number of "commercial item," (i.e., contractor-biased) contracts it awards.

The fallacy of this logic was recently borne out in a hearing of the House Committee on Government Reform where both the pricing and IP limitations the Department has endured through one relatively small contractor, TransDigm, were highlighted (see attached 2/2/2022 AFGE letter to the Committee). As TransDigm representatives repeatedly stressed during the hearing, the parts they were selling the government on a sole source basis qualified as "commercial items" despite having no real commercial market. Using a different moniker to describe the purchase of military equipment does not change the underlying nature of the items being bought. It just changes the terminology used to describe them with the loss of accompanying safeguards. TransDigm is only the tip of the iceberg the Department faces every day, as all major contractors employ the same techniques and tactics when selling to DoD.[1]

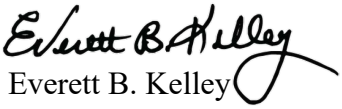
Finally, the Competition Report misleads when it states that 88% of all DoD procurements are now for "commercial items." That appears to be based on transaction numbers rather than dollars obligated. The vast majority of DoD contracts have always been for very small dollar items, such as office equipment and consumable supplies, what are considered to be commercial-off-the-shelf rather than the much broader term "commercial." Using transaction numbers rather than dollars obligated leads the reader to imagine that there are many suppliers of military

[1] *See* American Economic Liberties Project, "Caveat Emptor: Reversing the Anti-Competitive and Over-Pricing Policies that Plague Government Contracting," June 2020. Available at: https://www.economicliberties.us/wp-content/uploads/2020/06/Working-Paper-Series-on-Corporate-Power_4.pdf

systems when the entirety of the Report is the conclusion that there are only five remaining major defense contractors and a virtual collapse of competition for many weapons systems.

The "happy talk," misleading descriptions and lack of context in the "commercial items" section of the Competition Report cannot mask the ugly truth. The Department has placed itself in an untenable position from which it is unlikely to recover soon. AFGE members who are a part of the DOD organic industrial base see this all too clearly every day in their dealings with contractors, whether over IP or contract pricing. Rather than acting as a surrogate for industry, it is imperative that the Department flex its muscle as the monopsony buyer it really is. Only then will the Department be able to leverage its considerable weight to demand better prices and IP terms from its major suppliers who are so dependent on DoD's ultimately unsustainable largesse.

Sincerely,



Everett B. Kelley
President

Attachment

AMERICAN FEDERATION OF GOVERNMENT EMPLOYEES, AFL-CIO

Eric Bunn Sr.
National Secretary-Treasurer

Dr. Everett B. Kelley
National President

Jeremy A. Lannan
NVP for Women & Fair Practices

February 2, 2022

Honorable Carolyn Maloney
Chairwoman
House Committee on Oversight and Reform
2157 Rayburn House Office Building
Washington, D.C. 20515

Honorable. James Comer
Ranking Member
House Committee on Oversight and
2157 Rayburn House Office Building
Washington, D.C. 20515

Dear Chairwoman Maloney and Ranking Member Comer:

On behalf of the American Federation of Government Employees, AFL-CIO, which represents over 700,000 federal and D.C. government employees who serve the American people in over 70 different agencies across the nation and around the world 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 also appreciate the Committee's interest in and jurisdiction over civilian agency procurement issues.

The January 19, 2022 Hearing on "Price Gouging in Military Contracts: New Inspector General Report Exposes Excess Profit Obtained by TransDigm Group," was a reprise of a prior hearing on this same problem. Unfortunately, the underlying issue that TransDigm's behavior was not unlawful, and in fact encouraged by the existing contract pricing statutory and regulatory framework, was not addressed in any kind of meaningful detail. Starting with the Federal Acquisition Streamlining Act (FASA) and culminating in continuous additional statutory amendments, including implementation of Section 809 Panel recommendations for "streamlining acquisition regulations," the Oversight and Reform Committee acquiesced in radical expansions of what is considered to be a "commercial item or service" to embrace sole source procurements for spare parts for military weapon systems, even though those spare parts were not goods or services sold in substantial quantities to the general public. In addition, the Committee is well aware that various statutory changes over the years have directly weakened application of the Truth in Negotiations Act (TINA) (now "called the Truthful Cost or Pricing Data statute) to the point where its application is often easily evaded.

The legal consequences of this expanded definition of "commercial items and services," as well as the growth of TINA exemptions and increased dollar thresholds is that contracts end up being exempted from TINA, and contractors are effectively given a "free pass" from providing contracting officers with current, complete and accurate information to negotiate contract prices even in sole source situations.[1] In

[1] Indeed, most recently in the Fiscal Year 2022 National Defense Authorization Act, the Armed Services Committees continue to promote expanding upon these faux-"commercial" procurements, requesting DoD identify and address through further legislative proposals any further "impediments" to further expansions of "commercial" acquisitions of "innovative technologies." The policy rationale for these radical changes has been that private sector research and development spending has outpaced military research and development spending, and that companies developing innovative technologies will not want to do business with DoD but instead sell their technologies to military competitors. We think these assumptions are misleading as both the Department of Defense and State Department must approve technology transfers to foreign governments. Additionally, much of what is characterized

the case of TransDigm, once the Inspector General reports were released and TransDigm was characterized as charging "excess profits," TransDigm voluntarily provided uncertified cost and pricing data to the government's contracting officers. The problem remains that uncertified "cost and pricing data" provides little insight and no remedy to contracting officers during the course of negotiations, unlike "certified cost and pricing" data that application of TINA requires.

Accordingly, legislative "solutions" to this problem that would merely ratify voluntary practices already authorized in the Federal Acquisition Regulation to provide uncertified cost or pricing data to contracting officers provide far less useful remedies to the government than would the application of TINA, a course of action that would simply require returning to the pre-FASA definition of what constitutes a "commercial item," the lowering of TINA dollar applicability thresholds, and the elimination of one-proposal TINA exemptions. We recommend that the "Fair Pricing With Cost Transparency Act of 2022," include additional language that would return to the robust definitions and remedies previously provided by TINA, and would be happy to provide the suggested language to the Committee.

At a minimum, AFGE urges the Committee to endorse language regarding the so-called "commercial items" definition by adopting language proposed by Congressmen Tim Ryan and Tom Cole, on a bipartisan basis, in the House version of the FY 2020 National Defense Authorization Act. This language would require actual sales in "significant quantities" [to the general public] before an item or service could be deemed to be "commercial." While this change would not address all the TINA exemptions identified by the Inspector General in the TransDigm report, it would when combined with recalibrating the TINA dollar applicability threshold to a more modest $500,000 (from the recent near trebling of the threshold to $2 million) serve to illustrate that Congress is serious about reigning in overpricing of government contracts.

We appreciate your consideration of our views. Any question on the details of this letter may be directed to Dr. John Anderson, at 703-943-9438, john.anderson@afge.org or our policy counsel, Richard C. Loeb, at 202-639-6466, richard.loeb@afge.org.

Sincerely,

Everett B. Kelley
National President

Copy Furnished:

Senate Homeland Security and Government Affairs Committee
Senate Armed Services Committee
House Armed Services Committee
Senate Committee on Appropriation – Defense Subcommittee
House Committee on Appropriations – Defense Subcommittee

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as private sector research and development has a significant federal government component to it, so the data comparing private sector and governmental research and development spending trends needs to be analyzed in detail to make proper comparisons, and when the data is normalized, the federal component of research and development spending is far more robust.