

UNCLASSIFIED

STATEMENT BY

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BEFORE THE HOUSE COMMITTEE ON OVERSIGHT AND ACCOUNTABILITY,
SUBCOMMITTEE ON NATIONAL SECURITY, THE BORDER, AND FOREIGN AFFAIRS, AND
SUBCOMMITTEE ON GOVERNMENT OPERATIONS AND THE FEDERAL WORKFORCE

ON

CHALLENGES FACING THE DEPARTMENT OF
DEFENSE RELATED TO FINANCIAL MANAGEMENT

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THE HOUSE COMMITTEE ON OVERSIGHT AND ACCOUNTABILITY

Chairman Grothman, Chairman Sessions, Ranking Member Garcia, Ranking Member Mfume, and distinguished Members of your respective subcommittees, thank you for the opportunity to testify today at this joint hearing to address challenges facing the Department of Defense related to procurement policies and practices that support sound financial management.

I am John Tenaglia, the Principal Director, Defense Pricing and Contracting, in the Office of the Under Secretary of Defense for Acquisition and Sustainment. I began my civil service career with the Department in 2008 after retiring from active duty as an officer in the United States Air Force. As the Principal Director, Defense Pricing and Contracting, I am privileged to serve as the functional leader of DoD's contracting and pricing community. My staff and I provide the policies, guidance, regulatory framework, and e-business capabilities that enable DoD Components, through their pricing and contracting professionals, to effectively and affordably acquire goods and services to meet the requirements of our nation's Warfighters. We partner with key stakeholders, including the DoD Comptroller, Defense Contract Audit Agency (DCAA), and Defense Contract Management Agency (DCMA).

On January 19, 2022, I testified before the House Oversight and Reform Committee to address pricing of contracts for military spare parts. Since then, and with the strong support of the Congress, the Department has advanced legislation and additional policies that reinforce our contracting officers' ability to negotiate and administer contracts with the defense industry. DoD's contracting officers are charged with the fiduciary responsibility of balancing the taxpayers' interest (that we pay a fair and reasonable price) with the mission imperative to timely deliver combat capability at scale. In carrying out these responsibilities, DoD's contracting professionals serve alongside our defense acquisition workforce colleagues including the functional communities of program management, financial management, engineering, and lifecycle management.

As a team, the defense acquisition workforce persevered through the pandemic to rapidly respond and execute public health-related requirements on behalf of our interagency partners. The Department executed over \$87B, on behalf of the interagency, in support of the COVID-19 Pandemic, where the DoD Acquisition Workforce demonstrated the ability to effectively use a variety of authorities, to include the Defense Production Act, Commercial Solutions Opening, Other Transactions, and Federal Acquisition Regulation (FAR)-based contracting solutions, to rapidly deliver medical countermeasures to the American people and strengthen the medical industrial base. Currently, our defense acquisition workforce is engaging with the defense industry to deliver combat capability in support of Ukraine while at the same time modernizing our own systems and sustaining fielded systems. Recently, our contracting officers have been challenged to navigate, with industry, through economic conditions that have required us to manage the risk of cost/price uncertainty. On May 25, 2022, I issued guidance to the DoD Contracting workforce on *Inflation and Economic Price Adjustments*. On September 9, 2022, I issued further guidance on *Managing the Effects of Inflation with Existing Contracts*. We continue to encourage use of Economic Price Adjustment clauses where appropriate to equitably balance the risk of inflation between the Government and the contractor. However, not all contractors are requesting such clauses and whether one is appropriate depends on the type of contract, contract length, and other contract-unique circumstances.

As I asserted in my testimony last year, the price we pay matters because the more we pay, the less combat capability we can acquire for a ready force. Ideally, our contract pricing is based on competitive market pressures that dictate boundaries of what is fair and reasonable. However, we don't always enjoy the benefit of competitive market forces. A significant percentage of DoD's annual contract obligations support follow-on procurement and sustainment of fielded systems. In that acquisition environment, the Department employs statutory authority of the Truthful Cost and Pricing Data Act, where contractors are required to provide relevant data that places the Government and

contractor on equal footing for negotiations, unless an exception applies. Where certified cost and pricing data is required, contracting officers evaluate that data and conduct negotiations based on their analysis. Contracting officers can leverage tools and request assistance, such as pre- and post-award audits from DCAA, and evaluation products from DCMA. Having access to data and analyzing it is one of the most effective ways for contracting officers to ensure they are paying fair and reasonable prices.

My staff and I are focused on ensuring DoD's contracting and pricing professionals are best equipped to effectively negotiate in instances where competition is not available, including our largest programs with the biggest defense contractors. In the last legislative cycle, my staff and I engaged with Congressional staff to improve our ability to negotiate fair prices for sole source contracts. The Department appreciates enactment of Section 803 in the FY2023 National Defense Authorization Act, "*Data Requirements for Commercial Products for Major Weapon Systems.*" This change to Title 10 United States Code Section 3455 requires product information to support new commercial assertions to ensure accurate commercial determinations. It also requires an offeror to provide data to support price reasonableness for major weapon systems.

On April 7, 2023, my staff and I published the DoD Contract Finance Study. The Study was the first comprehensive review of contract financing since 1985. We performed the Study in response to a Government Accountability Office (GAO) recommendation that the Department conduct a comprehensive assessment of the effect that its contract financing and profit policies have on the defense industry. The Study report includes 16 recommendations for action within the following seven tenets: 1) Recognize the role of profit and cash flow in a healthy defense industrial base; 2) Improve means to ensure timely payments to subcontractors; 3) Ensure progress payment rates reflect the business environment; 4) Assist small businesses on defense contracts with financing; 5) Address

perceived challenges with government accounting system; 6) Determine effectiveness of performance-based payments; and 7) Understand the role of interest. The report with its associated appendices is available on the Defense Pricing and Contracting public website.

Our report emphasized that a financially healthy defense industry is essential to ensure that the DoD can procure the goods and services the U.S. warfighter needs to effectively defend our nation. We concluded that, in aggregate, the defense industry is financially healthy, and its financial health has improved over time. We observed that contractors operating in the DoD environment have unique advantages, especially with respect to cash flow through DoD's contract financing policies, and this result is demonstrated by traditional major defense contractors out-performing commercial counterparts in many key financial metrics. Our study concluded that defense subcontractors and suppliers generally do not receive the favorable cash flow benefits to the same extent enjoyed by defense prime contractors; we noted as a crucial finding. GAO has estimated that 60 to 70% of defense work is being performed by subcontractors (GAO-11-61r). The Department is committed to advancing policy improvements in this area, which would not only aid in the financial health of defense subcontractors but could assist in attracting new entrants into the defense industrial base at the supply chain level. We observed that small businesses are particularly vulnerable when it comes to having cash on hand to cover operating expenses. In general, they do not have the same opportunities to obtain working capital as their larger counterparts. As we seek public, including industry feedback in the months ahead about prioritization of the Study recommendations, we look forward to working with the Congress in assessing whether statutory changes are necessary to support these objectives.

DoD's acquisition and contracting professionals work closely with our colleagues in the DoD financial management community. My staff, in particular, has collaborated with the OSD Comptroller staff to jointly develop standard procedures to address how the requirements, procurement, accounting,

and entitling communities should conduct business across nine critical data exchanges (we call “handshakes”) in the Procure to Pay (P2P) process. This past April my staff jointly hosted, with the OSD Comptroller staff, the *2023 DoD Procure-to-Pay (P2P) and Financial Audit Training Symposium*. We use that forum to provide our contracting, logistics, and finance communities and our industry partners with a better understanding of requirements for standard data and processes, use of enterprise systems, and related internal controls that support audit requirements and ensure efficient government management of P2P activities and taxpayer funds. We highlighted the latest P2P and audit initiatives, to include information on procurement data standards and tools, financial management reform, government furnished property, traceability and transparency of awards, and cybersecurity. All of the presentations from this year’s and prior years symposiums are available on our website.

Defense Pricing and Contracting is executing against our strategic plan to develop and deploy Defense wide procurement capabilities featuring use of established data standards, enterprise services, internal controls, and business intelligence. One such, of the 50+ capabilities available to both Government and industry in our Procurement Integrated Enterprise Environment (PIEE), is the Government Furnished Property (GFP) Module. In collaboration with our teammates in the Office of the Assistant Secretary of Defense for Sustainment and Defense Logistics Agency, we deployed the GFP Module on March 24, 2021, to consolidate GFP management into a single automated platform. It enables reuse of data throughout the GFP lifecycle; thereby, improving data accuracy and reducing manual input of data by contractors. The GFP module application is based upon newer technology that provides contractors with a much more efficient process to submit data for their reports. For instance, contractors are not required to enter the same data into multiple fields; the system will automatically populate data fields throughout the process. By creating a single tool for all reporting of Government property, data can be readily accessed across various processes, thereby reducing contractor input and

errors while enabling traceability across the Government property life cycle. This capability supports the Department's Financial Improvement and Audit Remediation priorities. Use of the GFP Module to capture GFP information throughout the GFP lifecycle from GFP Attachment through disposition is an important step forward in addressing the Department's material weakness in accounting for Government Property in the possession of contractors.

As of January 2021, Defense Federal Acquisition Regulation Supplement (DFARS) Procedures, Guidance, and Information subpart 245.103-72 requires contracting officers to create a GFP Attachment in the GFP Module, when GFP is anticipated in performance of a contract. Contractors are required by contract clause to use the GFP Module to report receipt and shipment of GFP and can repopulate some of the required property loss data from the GFP Attachment already in use for the property. The supporting documentation and summary data for the completed loss cases created in the GFP Module are saved, making the information accessible to auditors and property owners to perform audits and update property records. On April 27, 2023, my staff and I published a proposed DFARS rule to consolidate existing contract clauses for the management and reporting of Government property into a single contract clause, to replace references to legacy software applications used for reporting Government property within the DoD enterprise-wide eBusiness platform, and to convert existing form-based processes into electronic processes within that platform. The public comment period closed on June 26, 2023, and we are currently assessing those comments in formulation of a final rule.

Sound financial management of the precious resources allocated to the Department of Defense involves the aforementioned policies, practices, and tools (amongst many others). We rely on responsible defense contractors to manufacture and sustain our weapon systems and render critical support services. Our program managers and contracting officers, with support and advice from various oversight organizations such as DCMA, DCAA, DoD Office of the Inspector General, and

GAO, have sufficient statutory coverage and implementing policy to hold contractors accountable to fulfill contractual obligations at affordable prices. The Department of Defense is absolutely committed to delivering and sustaining preeminent capabilities for the Warfighter and our international partners. Thank you for the opportunity to testify, and I look forward to your questions.