

Twenty-five Years of Acquisition Reform: Where Do We Go From Here?

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Chairman McKeon, Ranking Member Smith, distinguished members of the Committee, thank you for the honor and privilege of appearing before you today to discuss the very important topic of improving the defense acquisition enterprise.

I am before the Committee today as an individual, not representing any particular institution. However, I have been a student of and lived with the defense acquisition system for over 25 years. As a policy analyst and a participant in the acquisition reform efforts of the last two decades, I have been affiliated with the Center for Strategic and International Studies as both the Director of the Defense Industrial Initiatives Group from 2002-2007 and currently as a Senior Associate (Non-Resident). I am also a guest lecturer at the Defense Acquisition University and the Industrial College of the Armed Forces, and have participated in dozens of acquisition reform studies and commissions. As a business person, I spent over a decade on Wall Street as an equity analyst and investment banker during a period that spanned the last downturn in defense spending, have run my own strategy consultancy firm and most recently a firm that invests in/supports small businesses in the aerospace/defense/government services sector. I therefore approach the problem from both an academic and very pragmatic business viewpoint.

The topic of acquisition reform is an excellent one for the Committee to be addressing, particularly as we head into a period of slowing defense spending. As defense budget dollars become more precious, there will still be a need for additional capabilities and the

development of new technologies. Therefore, having an efficient acquisition system will be strategically critical to the Department of Defense over the next decade. Bringing a considered and thoughtful approach to the problem will be important; and difficult given that this is a topic fraught with hyperbole, mythology, and the confusion of symptoms for root causes.

I would like to raise five key observations as you consider the last 25 years of acquisition reform and look forward to what should be done.

- 1) First, there has been a very useful evolution in the nature of the acquisition reform debate over the last seven years. It is eye-opening and instructive to read the Congressional record of the acquisition reform commissions that followed the Revolutionary War, Civil War and other conflicts. The acts of outright fraud and corruption are abundant and one can see why the focus of reform for most of our history has been broadly focused on the issue of fraud, waste and abuse. In the 1980s, 1990s and 2000s, the debate then evolved to looking at bringing efficiencies to the processes and functioning of the acquisition system.

During the last decade the discussion has shifted from trying to reform just the acquisition/procurement process. There has been the recognition that the acquisition process is part of a broader system that includes the requirements, budgeting and acquisition processes, referred to as the "big A" acquisition system (the Defense Acquisition Performance Assessment project of 2005 and CSIS's Beyond Goldwater-Nichols project are two studies that discussed this issue). This has led to a focus on improving the requirements process, as well as the interaction between the components of the "big A" acquisition system. GAO analysis and Defense Acquisition University studies indicate that 85% of the lifecycle cost of a weapon system is determined by the time the requirements are set. A perfectly performing acquisition system that efficiently delivers unneeded items or poorly conceived items or inherently expensively designed items, will still produce bad outcomes and be viewed as a failure. Continued focus on the requirements system, the professionalism involved, discipline used and how it interfaces with the acquisition system should be a very fruitful area for future reform efforts.

- 2) Second, the Department of Defense's acquisition system is a large and complex enterprise, whose governing laws, regulations, rules and procedures have evolved and slowly accreted since the founding of the Republic. I believe an analysis of the system would reveal that most of these laws and regulations were based on real problems/issues that required a solution or response, but that over time the problems

evolved, solutions to other problems create conflicts with older rules and there has been a tendency to add rules but not take them away. This is why periodic reviews of the system aimed at reviewing the laws and regulations, such as the Section 800 Panel of 1993 or the rewrites of the DoD Instruction 5000 are so useful. As an aside, putting a sunset clause on all new laws or rules to force a periodic reexamination would be an interesting best practice to consider. It would be my observation that many of the problems of the acquisition system are the result of unintended consequences of a very byzantine and, at times, outright contradictory set of laws and regulations, rather than problems of outright malice or malfeasance - despite what some breathless headlines would have you believe.

- 3) Third, one size does not fit all when it comes to the acquisition process. The Department of Defense buys an extremely wide range of technologies, products and services; it touches virtually every segment of the economy. The appropriate processes for the purchasing of commodities will differ from those required to acquire emerging innovative technologies such as cyber capabilities, let alone the procurement of more mature and asset intensive systems such as heavy space launch vehicles, heavy armored vehicles or naval vessels. There has also been recognition that the purchasing of services by the Department of Defense has become significant and has different characteristics than the development of weapon systems/procurement of hardware.

Similarly, the rapid acquisition systems required for war time environments or rapidly changing technologies may not be appropriate for the development of very long cycle, complex weapon systems. In fact, acquisition reform efforts aimed at the traditional, long cycle acquisition processes, if improperly applied to the rapid acquisition systems could fundamentally break them. And vice versa. One of the characteristics of the modern era is that the Pentagon is faced with operating in both modes, the rapid wartime system and the long cycle development system, simultaneously. It begs the question as to whether well defined, different "tracks" in the acquisition system are required – each with their own rules and processes. The creation of DARPA, with its own set of acquisition rules and culture, was the recognition in a prior era that a different "track" was required to develop cutting edge technologies for example.

Overly broad laws and regulations that are applied across the entire span of activity of defense acquisition are likely to cause as many problems as they solve. Defense acquisition is varied, nuanced and, I would submit, rarely amenable to simple rules; it is

an endeavor that requires judgment and that judgment cannot be legislated or imposed by regulation.

- 4) Fourth, cost overruns, missed deadlines and failed programs are symptoms, not root causes. Unless the root causes are addressed, no amount additional oversight, extra regulation, rearranging of organization boxes, creation of new offices or changes to processes will help. In fact they will likely (and have), make things worse. I believe this is why after decades of acquisition reform, the statistics show the same persistent cost overrun percentages and lengthening development timelines.

There are four root cause factors to consider:

- a) The U.S. military has relied on having technological and industrial superiority as part of its core strategic advantage on the battlefield for almost a century. The acquisition system is asked to push the limits of technology and do very difficult things – go faster than the speed of sound, make an invisible airplane, build a missile that can precisely hit a target half way around the world. Pushing the limits of technology is expensive, is fraught with risk and setbacks, and can rarely be predicted with precision. Some of the cost overruns and delays are simply inherent to what we ask the acquisition system to undertake. As long as technological superiority is a key goal it will be impossible to reduce the overruns to zero. It does not mean we should tolerate poor performance and not try to improve the efficiency of the system; it simply says eliminating all cost overruns is incompatible with our strategic goals and potentially counterproductive.
- b) There are fundamental and structural disconnects in the time frames used by the different actors in the acquisition system. Decade long projects are funded annually, are being executed by project managers who change every few years, with oversight applied by members of Congress who have to think in two and six year cycles, and built by companies who need to meet quarterly financial performance metrics. Because the time frames of the actors are driven by other considerations, these disconnects are likely structural. This structural churn creates friction (and cost) to the system. That being said, reducing the gaps is a worthwhile goal for future reform efforts – ideas suggested by prior acquisition reform studies include extending the tenure of program managers to better match the milestones of long projects. I would also suggest looking at matching the funding cycles for programs to match the type of technology/service being acquired. So, long cycle projects get multi-year appropriations/budgets, while others have annual appropriations. This

simple, but culturally difficult issue, could result in billions of dollars of savings by providing greater visibility and stability to programs.

- c) The economic/profit incentives culturally embedded in the system creates adverse results. Culturally we have evolved to a point where the system would rather pay \$1 billion and 5% profit for a defense good, than \$500 million and 20% profit. Even though in that example the taxpayer would save over \$400 million, the focus would be on why 20% of profit was paid. I exaggerate for effect, however, there are deep roots to this cultural issue – notions of profiteering that go back the First World War, and differences in perceptions of risk and value add. As long as this phenomenon of favoring “cost plus” persists, there will a disincentive to reduce costs and use the normal economic/profit motivator used by the commercial world to drive for efficiency in order to maximize profit.

- d) Finally, there is a structural incentive for the entire system to be optimistic. Put more bluntly, the system is incentivized to lie to itself. A contractor is incentivized to be optimistic about the costs of a new weapon system because it wants to win the competition; the Pentagon is incentivized to believe the low (potentially unrealistic) bid because it wants to launch the program; and the Congress is incentivized to believe the proposed (and potentially unrealistic) program budget because it wants to see a program launches and jobs created. Compounded over multiple programs and the system ends up with the “ten pounds of programs in an eight pound bag” problem. I would submit that a portion of the cost overruns is simply the revelation of the self-lie that was embedded in the program at launch.

Furthermore, there are rarely consequences for being wrong. In fact, mis-budgeted programs/accounts or overrun programs are often given more money to solve the problem, while the poor program manager who actually delivers under budget and early has money taken away from them. There has been some thought given to this issue in recent acquisition reform efforts – budgeting to the 80% probability line (vs 50%) for example. I also believe creating incentives for good performance are ideas to consider – if your program performs the budgets are preserved/untouched for example, or better share lines/profit for industry for coming under budget or early.

Although these are difficult issues to address and many are structural, I would submit looking at these core topics and seeing where the unintended consequences could be offset or narrowed would be fruitful areas for potential study.

- 5) Fifth and finally, in many of the acquisition reform studies (until recently) the topic of incentives rarely comes up. I believe this is another reason why the problems persist despite the decades of acquisition reform attempts – the development new processes, organizations and regulations. Unless the proper incentives are put into place in order to cause behavior to change, we should not expect different results. It is a simple premise but one that is often overlooked, people respond to the incentives put before them. If there was one area for significant more thought and effort by a future acquisition reform effort, I would submit the topic of incentives in the system is key.

Mr. Chairman, Mr. Smith, members of the Committee, thank you for the opportunity to share some thoughts. I look forward to your questions and the dialogue.