



GENERAL COUNSEL

GENERAL COUNSEL OF THE DEPARTMENT OF DEFENSE
1600 DEFENSE PENTAGON
WASHINGTON, D. C. 20301-1600

APR 4 2000

The Honorable Al Gore
President of the Senate
Washington, DC 20510

Dear Mr. President:

Enclosed is proposed legislation that would extend authority to carry out certain prototype projects for three years, authorize the use of other transactions for follow-on production for up to a maximum of twenty programs, and authorize the use of other transactions for prototypes developed under the Commercial Operations and Support Savings Initiative. This legislation is part of the Legislative Program of the Department of Defense for the Second Session of the 106th Congress and we urge its enactment. Each proposal is accompanied by a sectional analysis that more fully describes its purpose.

The Department currently has authority through September 30, 2001 to award "other transactions" for prototype projects that are directly relevant to weapons or weapon systems proposed to be acquired or developed by the Department. "Other transactions" is the term commonly used to refer to the section 2371 of title 10 authority to enter into transactions other than contracts, grants or cooperative agreements.

This authority has been used successfully to attract innovative commercial companies that typically do not compete for defense business and to test creative contracting strategies with traditional defense firms. The flexibility afforded by this authority permits the government to forge new relationships with companies, to leverage corporate investments, to negotiate appropriate intellectual property rights, and to utilize cost savings from commercial practices or processes instead of maintaining systems in accordance with more expensive specified government requirements.

If the Department is to be successful in establishing new ways of doing business and in attracting new commercial companies, then it is imperative that the "other transaction" authority be extended into production for that selected sample of programs that successfully complete the prototype phase. It is not reasonable for a company selected for these prototype efforts to change its business practices or enter into a future prototype agreement with the government, if there is no avenue to continue with the same practices in production and sell the product to the government.

The first provision is a three-year extension to the prototype authority for a limited number of programs. The second proposal provides for selected current prototype projects begun under "other transaction" authority to proceed into production under the same "other transaction" authority. The third permits prototype projects begun under the Commercial Operations and



Support Savings Initiative to execute the production stage of the competitively attained business deal as an "other transaction" (otherwise these firms will not be able to do business with us).

When used selectively, this acquisition authority is a vital tool that will help the Department achieve the civil and military integration that is critical to reducing the cost of defense weapon systems.

The Office of Management and Budget advises that from the standpoint of the Administration program, there is no objection to the presentation of these initiatives for your consideration and for the consideration of the Congress.

Sincerely,

A handwritten signature in black ink, appearing to read "Douglas A. Dworkin". The signature is fluid and cursive, with the first name being the most prominent.

Douglas A. Dworkin
Acting General Counsel

Enclosures:
As Stated



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APR 4 2000

The Honorable J. Dennis Hastert
Speaker of the House of Representatives
Washington, DC 20515

Dear Mr. Speaker:

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This authority has been used successfully to attract innovative commercial companies that typically do not compete for defense business and to test creative contracting strategies with traditional defense firms. The flexibility afforded by this authority permits the government to forge new relationships with companies, to leverage corporate investments, to negotiate appropriate intellectual property rights, and to utilize cost savings from commercial practices or processes instead of maintaining systems in accordance with more expensive specified government requirements.

If the Department is to be successful in establishing new ways of doing business and in attracting new commercial companies, then it is imperative that the "other transaction" authority be extended into production for that selected sample of programs that successfully complete the prototype phase. It is not reasonable for a company selected for these prototype efforts to change its business practices or enter into a future prototype agreement with the government, if there is no avenue to continue with the same practices in production and sell the product to the government.

The first provision is a three-year extension to the prototype authority for a limited number of programs. The second proposal provides for selected current prototype projects begun under "other transaction" authority to proceed into production under the same "other transaction" authority. The third permits prototype projects begun under the Commercial Operations and



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When used selectively, this acquisition authority is a vital tool that will help the Department achieve the civil and military integration that is critical to reducing the cost of defense weapon systems.

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Douglas A. Dworkin
Acting General Counsel

Enclosures:
As Stated

**SEC. ____ . FOLLOW-ON PRODUCTION PROGRAMS TO CERTAIN PROTOTYPE
PROJECTS.**

1 (a) FOLLOW-ON PRODUCTION PROGRAMS.—The Secretary of Defense, under the authority
2 of this section, may enter into fixed-price transactions (other than contracts, cooperative
3 agreements, and grants) for follow-on production, as designated by the Secretary of Defense, that
4 were initiated as prototype projects under section 845 of the National Defense Authorization Act
5 for Fiscal Year 1994 (Public Law 103-160; 10 U.S.C. 2371 note), as amended.

6 (b) EXERCISE OF AUTHORITY.—(1) The authority provided under subsection (a) may be
7 exercised:

8 (A) *Without regard to section 3324 of title 31, United States Code, regarding*
9 *advance payments.*

10 (B) Without any requirement for funding or other contributions to the cost of the
11 production program by other parties to the transaction.

12 (C) Only when a determination has been made that a standard contract is not
13 feasible or appropriate.

14 (D) Only after guidance has been issued in accordance with paragraph (2).

15 (E) For programs that are initiated as prototype projects under section 845 of the
16 national Defense Authorization Act for Fiscal Year 1994, as amended, by September 30,
17 2004.

18 (F) For up to a total of 20 follow-on production programs.

19 (2) The Secretary of Defense shall issue guidance for exercising the authority provided
20 under subsection (a). The guidance, at a minimum, shall provide that—

21 (A) To the maximum extent practicable, competitive procedures are used when

1 entering into transactions;

2 (B) Each pilot program has identified—

3 (i) performance objectives;

4 (ii) price control measures;

5 (iii) delivery schedules;

6 (iv) acceptance and Inspection criteria,

7 (v) technical data and other intellectual property rights of the

8 parties; and

9 (vi) termination and disputes criteria.

10 (C) achievement of performance objectives, price control measures, and delivery
11 schedules are reviewed annually.

12 (D) If acquisitions are to be made through the transaction beyond five years after
13 the transaction has been executed, the Secretary of Defense makes an assessment no later
14 than the end of the fifth year (and every three years thereafter as long as acquisitions are
15 made through the transaction), taking into account achievement of performance
16 objectives, price control measures, and delivery schedules and application of the guidance
17 issued under this subsection, to determine whether continuing to acquire through the
18 transaction is in the best interest of the government.

19 (c) CONGRESSIONAL REPORTING.—(1) Funds may not be obligated for follow-on
20 production unless they have been appropriated in a procurement account. Prior to obligation of
21 funds for the follow-on production of a major systems acquisition under the authority of
22 subsection (a), the program shall be identified and included in the justification supporting the
23 President's Budget Request, along with a description of the scope of the procurement, including

1 projections as to the number of units to be purchased, the unit purchase cost, annual purchase
2 amounts, and duration and total cost of the program.

3 (2) No funds may be obligated for follow-on production under the authority of subsection
4 (a) until the Secretary of Defense submits to the Committees on Armed Services and
5 Appropriations of the Senate and the House:

6 (A) a report that describes the guidelines and procedures that will apply to a
7 program under subsection (a); and

8 (B) for an acquisition conducted under the authority of subsection (a), a notice
9 including a description of the acquisition strategy, performance objectives, price control
10 measures, terms and conditions for termination, and projected termination liabilities.

Sectional Analysis

Transactions other than contracts, cooperative agreements, and grants commonly are referred to as other transactions. Other transactions are determined in the negative; that is, they are not procurement contracts, cooperative agreements, or grants. Currently there are two circumstances when other transactions may be used. The first involves cost-shared research projects where there is a dual interest by both industry and the Government. The second situation relates to prototypes that are directly relevant to weapons or weapons systems with or without cost sharing. This allows the Government to prototype technology or items that are directly relevant to weapons or weapons systems.

This section authorizes use of other transactions for follow-on production of up to a maximum of twenty programs designated by the Secretary of Defense that are follow-ons to prototype projects conducted pursuant to section 845 of the National Defense Authorization Act for Fiscal Year 1994, as amended. Other transactions are not procurement contracts and, as such, generally are not subject to the laws and regulations governing such contracts, however this pilot authority is limited to fixed-price transactions. Use of this authority is conditioned upon a determination that a standard contract is not feasible or appropriate. As with prototype projects conducted under section 845, this provision allows for advance payments, eliminates the requirements for cost matching, and requires competition to the maximum extent practicable. The exclusion from the requirement for cost-matching is consistent with section 845 and is not intended to imply there is a requirement for any level of cost-sharing. This pilot authority requires that the Secretary establish performance objectives, price control measures, acceptance and inspection criteria, and termination and disputes criteria for each of the pilot programs.

The authorities of the Secretary of Defense may be delegated. The Secretary must submit to the Committees on Armed Services of the Senate and the House of Representatives: (1) written notification of follow-on production programs to obligation of any funds for follow-on production; and (2) a report, prior to the obligation of any funds, describing the procedures to be used for follow-on production programs.

This provision will optimize the transition from prototype to production for successful prototype projects conducted under section 845, as amended. The flexibility of the other transaction authority provides the Department the opportunity to streamline the acquisition process, facilitate development of contractor strategic relationships, take advantage of innovative or commercial business practices, and attract companies that do not traditionally do business with the government. In an environment where commercial industry is leading in many technological areas and Defense budgets are declining, it is imperative that the Department have the flexibility to use innovative instruments that provide the opportunity to broaden the technology and industrial base or foster new relationships and practices that support national security. An extension of the authority to follow-on production is necessary to ensure a smooth transition for prototype projects that demonstrate readiness for production. This provision will give the Secretary of Defense the flexibility to optimize the transition of prototype projects to production while imposing oversight and safeguards on these production programs.

**SEC. ___. THREE YEAR EXTENSION OF AUTHORITY TO CARRY OUT
CERTAIN PROTOTYPE PROJECTS.**

Section 845(c) of the National Defense Authorization Act for Fiscal Year 1994, as amended (Public Law 103-160; 10 U.S.C. 2371 note), is amended by striking "September 30, 2001" and inserting "September 30, 2004".

Sectional Analysis

This section extends for three years Section 845 Other Transaction Authority for prototype projects. DARPA was provided an initial three year authority to award prototype other transactions by section 845 of the National Defense Authorization Act for Fiscal Year 1994 (Public Law 103-160; 10 U.S.C. 2371 note). This authority was extended through September 30, 1999, and broadened to include the military departments and other officials designated by the Secretary of Defense by section 804 of the National Defense Authorization Act for Fiscal Year 1997 (Public Law 104-201). The authority was extended again through September 30, 2001 by section 241 of the Strom Thurmond National Defense Authorization Act for Fiscal Year 1999 (Public Law 105-261).

The basic 10 U.S.C. 2371 other transaction authority for research was initially provided to DARPA for two years, but was permanently codified and extended to the military departments at the end of the two years.

Other transactions are not procurement contracts and, as such, generally are not subject to the laws and regulations governing such contracts. The Under Secretary of Defense for Acquisition, Technology, and Logistics (USD(AT&L)) and the Director, Defense Procurement have issued policy on the use of prototype other transactions.

The USD(AT&L) submitted a report on "Other Transaction" Awards for Prototype Projects to the Congressional defense committees in February 1999. Other transaction authority has been used successfully by the military departments and defense agencies to attract companies that typically do not do business with the Department and to experiment with potentially more efficient ways of doing business with traditional defense contractors.

Other transaction authority is an important acquisition tool that facilitates integration of the civilian and military industrial bases and incorporation of commercial technology into military weapon systems. The flexibility of the other transaction authority provides the Department the opportunity to streamline the procurement process, facilitate development of contractor strategic relationships, take advantage of innovative or commercial business practices, and attract companies that do not traditionally do business with the government. In an environment where commercial industry is leading defense in many technological areas and defense budgets are declining, it is imperative

that the Department continue to have the flexibility provided by this important acquisition tool to use innovative contractual instruments that provide the opportunity to broaden the technology and industrial base or foster new relationships and practices that support our national security.

SEC. ____ . FOLLOW-ON PRODUCTION PROGRAM FOR PROTOTYPES

**DEVELOPED UNDER THE COMMERCIAL OPERATIONS AND
SUPPORT SAVINGS INITIATIVE.**

1 Section 203(g) of the National Defense Authorization Act for Fiscal Year 1998 (10
2 U.S.C. 2511 note) is amended by adding at the end the following paragraphs:

3 “(5) The Secretary of Defense and the Secretaries of the Military Departments may enter
4 into transactions (other than contracts, cooperative agreements and grants) for follow-on
5 production of products developed under the Initiative that were initiated as prototype projects
6 under section 845 of the National Defense Authorization Act for Fiscal Year 1994 (Public Law
7 103-160; 10 U.S.C. 2371 note), as amended.

8 “(6) The authority provided under paragraph (5) is separate and in addition to any other
9 authority and may be exercised under the following conditions:

10 (A) Provided that the total acquisition of production quantities of a product
11 developed pursuant to the Initiative does not exceed \$25 million unless the Secretary of
12 Defense (or designee at a level not lower than an Under Secretary of Defense) determines
13 that acquisition in amounts in excess of this amount through the transaction is in the best
14 interest of the government.

15 “(B) Without regard to section 3324 of title 31, United States Code, regarding
16 advance payments.

17 “(C) Without any requirement for funding or other contributions to the cost of the
18 production program by other parties to the transaction.

19 “(D) With a determination that a standard contract, grant, or cooperative
20 agreement is not feasible or appropriate.

1 “(E) Only after guidance has been issued in accordance with paragraph (7).

2 “(F) For programs that are initiated as prototype projects under section 845 of the
3 National Defense Authorization Act for Fiscal Year 1994, as amended, by September 30,
4 2004.

5 “(7) The Secretary of Defense shall issue guidance for exercising the authority provided
6 under paragraph (5). The guidance, at a minimum, shall provide that—

7 “(A) To the maximum extent practicable, competitive procedures are used when
8 entering into transactions;

9 “(B) Each pilot program has identified—

10 “(i) performance objectives;

11 “(ii) price control measures;

12 “(iii) delivery schedules;

13 “(iv) acceptance and Inspection criteria,

14 “(v) technical data and other intellectual property rights of the parties;

15 and

16 “(vi) termination and disputes criteria.

17 “(C) Achievement of performance objectives, price control measures, and delivery
18 schedules are reviewed annually.

19 “(8) If acquisitions are to be made through the transaction beyond five years after the
20 transaction has been executed, the Secretary of Defense makes an assessment no later than the
21 end of the fifth year (and every three years thereafter as long as acquisitions are made through the
22 transaction), taking into account achievement of performance objectives, price control measures,
23 and delivery schedules and application of the guidance issued under this subsection, to determine

1 whether continuing to acquire through the transaction is in the best interests of the Government.

2 “(9) CONGRESSIONAL REPORTING.— (A) Amounts in excess of 525 million may not be
3 obligated for follow-on production under a transaction entered into pursuant to the authority of
4 paragraph (5) unless the Secretary (or designee at a level not lower than an Under Secretary of
5 Defense) has notified the Committees on Armed Services of the Senate and the House of the
6 projected total Cost and duration of the program and termination liability.

7 “(B) Not later than 120 days after the end of each fiscal year, the Secretary of Defense
8 shall submit to the Committees on Armed Services of the Senate and the House of
9 Representatives a report on the use by the Department during such fiscal year of procurement
10 transactions authorized under this Initiative. The report shall include an overall listing of each
11 procurement and an analysis and assessment as to how well the Department met the objectives in
12 paragraph (7)(B) for the procurement under these authorities.”.

Sectional Analysis

This section authorizes another use of transactions other than contracts, cooperative agreements, and grants (Other transactions). Other transactions are determined in the negative; that is, they are not procurement contracts, cooperative agreements, or grants. Currently there are two circumstances when other transactions may be used. The first involves cost-shared research projects where there is a dual interest by both industry and the Government. The second situation relates to prototypes that are directly relevant to weapons or weapons systems with or without cost sharing. The proposed legislation will allow Other Transaction Authority for production of prototypes developed under the Commercial Operations and Support Savings Initiative (COSSI).

COSSI was established by section 203 (g) (1) of the National Defense Authorization Act for Fiscal Year 1998 (Public Law 105-85) to reduce the operations and support (O&S) costs of legacy systems. COSSI involves two stages. The first stage is the fabrication of a prototype. The second stage is the procurement of follow-on production quantities of the prototype fabricated in Stage I. Currently, Other Transaction Authority is used for Stage I and a FAR contract is used for Stage II.

This proposal would authorize Other Transaction Authority, instead of a FAR contract, to

be used for Stage II follow-on production. This is important because the cost of fabricating the prototype in Stage I is shared between the government and contractor. Other Transaction Authority for follow-on production will provide for a seamless transition between prototype development and procurement and provide the contractor with assurance that the investment made in Stage I will be recouped in Stage II. In addition, the proposed legislation will facilitate more rapid insertion of technology into military systems by eliminating the need for a new FAR contract for Stage II production.

COSSI project proposals are competitively selected. Proposals must stipulate Stage I costs and target prices for follow on production. Projects that provide the best value to the government are selected. One of the criteria considered in determining best value is expected operation and support (O&S) cost savings. Factored into the O&S cost analysis is the total costs to DoD of implementing Stage I and purchasing follow on production in Stage II. This figure is compared to the baseline cost of the status quo. The target price for production quantities is a key factor in the computation of O&S cost. As a result, the Stage II target price is identified and evaluated as a part of the Stage I source selection. If the agreement participant does not meet the production target price, which was a big factor in the proposal being selected, a Program Office can decide not to proceed with procurement of follow on production or to use competitive procurement procedures. Indeed, even if the agreement participant meets the target price, a Program Office is still under no obligation to proceed with a procurement of production quantities. The legislative proposal merely empowers the Department to execute both stages of the COSSI project pursuant to OTA if deemed to be in the best interest of DoD.

One of the goals of COSSI is to attract non-traditional defense companies. Using Other Transaction Agreements for Stage I makes this goal easier to accomplish; however, requiring a FAR contract for Stage II could discourage companies from doing business with the Department of Defense. Allowing both prototype development and follow-on production to be covered by a single Other Transaction Agreement will encourage more commercial suppliers to participate in the program and give DoD greater access to commercial technologies.

The flexibility of the other transaction authority provides the Department the opportunity to streamline the acquisition process, facilitate development of partnerships, take advantage of technologies developed by commercial firms, and attract companies that do not traditionally do business with the government. In an environment where commercial industry is leading in many technological areas and Defense budgets are declining, it is imperative that the Department has the flexibility to use innovative instruments that provide the opportunity to broaden the technology and industrial base.

This provision allows for advance payments, and eliminates any requirement for cost matching or for establishing that a procurement contract is not feasible or appropriate. The exclusion from a requirement for cost-matching applies during Stage II follow-on production only. Some cost sharing is required for prototype development in Stage I. The \$25 million limitation on the value of any single follow-on production effort provides a reasonable restriction on how the authority can be used. Finally, these agreements will be required to be entered into subject to certain criteria as established by the Secretary of Defense to provide further safeguards to ensure their appropriate use.