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CONGRESS AND CONTRACTORS

Trying to describe or predict what the Congress is doing or will do about profit for government contractors is about as chancey as trying to make sense out of the love life of one of my teen-age daughters. However, just like that love life, it certainly bears watching.

Profit policy is much more a creature of negotiation between the executive and the private sector. The Congress ordinarily does not get into the question of how pricing is done and profit is calculated or allowed, except in gross terms. These gross terms

are usually in some form of philosophical or generic profit limitation, such as through renegotiation or Vinson-Trammel type legislation.

There are those who say that the way Congress feels and acts about contractor profit fits a cyclical pattern, going from parsimony to generosity and back again.

They attribute this less to a rational thought process than a reaction to other forces. These other forces are variously described as Republican versus Democratic politics, inflation times versus recession times, war versus peace. Election versus non-election years or the ascendancy or decline of some powerful Congressional figure.

I think that these views may well have been correct in the past, and I am sure that there will be some response to these causes in the future.

However, I believe that we are in the beginning of a long, and hopefully permanent, pattern of more rational treatment of government contractor profit.

With the exception of a few in the Congress, a slow realization has been building that a fair profit is a vital and necessary element of doing business with the government, and that the government is no different in this regard than any other customer.

There will always be a few, who for political purposes of their own, or in zealous but ill-informed good faith, insist that it is somehow immoral for a contractor to get a fair profit when he deals with the government. They will always contend that perfectly upright firms, respected by their competitors and commercial customers, switch from Jekyll to Hyde when they get a chance at the government trough.

I believe the number of these people is few, and will get fewer. I don't think they should be ignored, or their numbers may grow. I believe it will always be necessary to confront the demagogues in this group and try to education the well-meaning but mis-informed, or they may proliferate.

There may be many reasons for this new consensus. I will describe only the three that stand out for me.

First is the historical profit picture. Both government and its contractors have been able to see exactly what the profits have been in government contracts over a long period of time. There was a time when our audit, information and analytical tools were not adequate to tell us what the real profit was on government contracts and how this compared to commercial business. Now we have that information and it has become clear that the number of government contractors who realize excessive profits from those contracts is small indeed. The history of the Renegotiation Board and how little it was ever able to show as excess

profit, and recover", should be ample proof of this.

The second reason I see is the new conservatism in the electorate, which is represented in the Congress. Business as such is no longer the enemy in the minds of the people. They are coming to believe that the government does not always know best, that "who governs best governs least", that "the business of the country is business". They are maturing to the realization that reasonable capitalistic profit and retained earnings are the way to business expansion, jobs and prosperity. Their confidence in the basic business structure is returning.

The third reason for Congressional confidence in the government contractor

profit picture is the competence of the government as a customer.

I know that in the past there were many instances where the government was just not an informed customer who was tough enough to get the best bargain possible. I believe there will always be occasions when this will happen, but I believe it is no longer the norm and that Congress is coming to recognize that fact.

There is a growing understanding that there is a growing expertise in government financial manager competence. This new breed is quite able to assess the likely profit on a government contract, through informed risk assessment and financial analysis.

There are several reasons for this developing ability. One is the increased emphasis that has been placed on proper training of government financial managers for their jobs. Going along with that is the fact that government salaries for those managers, at least at the working level, have become competitive with industry, and good people are making these jobs their career.

Another reason for the increased competence in this area is the tools that have been provided ^{to} the manager. The enormous strides in information management, analytical techniques and communication have greatly increased the ability of the manager to evaluate potential risks and profit, monitor financial progress and evaluate

final profit.

Even the Congress, which gets little enough credit, can take credit for the new confidence in government profit management. Over the past 20 years there has been a considerable body of legislation, and implementing regulation, which has given the government financial manager the clout to get the attention of the contractors. They can now be quite confident that they are getting the information and cooperation they need, if they really want to do a good job of profit assessment and management.

The safeguards that the government has, to make sure that profits are reasonable, are many and varied.

1. Diligence of GAO
2. Defense Contract Administration
Services oversight
3. Defense Contract Audit Agency
4. Cost Accounting Standards
5. Defense Acquisition Regulations
6. Federal Acquisition Regulations
7. Truth-in-Negotiations Act
8. Office of Federal Procurement
policy oversight
9. The leisure of peacetime
procurement
10. The possible offspring of
Vinson-Trammel

As a matter of fact there is such a wide array of laws, regulation, audits and oversight activities, that there are many who say it is impossible to even make an

adequate profit, let alone excessive profits.

Those who have this feeling, such as those who want to do something about the admittedly anachronistic Vinson-Trammel Act, are faced with a political dilemma. Only politicians with a demonstrated record of fiscal conservatism and responsibility will dare take action to repeal or even modernize the Vinson-Trammel Act. On the majority side in the Congress, many of those in positions to do something about Vinson-Trammel either are anti-defense and want the Act kept as is or strengthened, or they would like to modernize the Act but don't have the political authority to do so because of liberal spending records. There are only a few with the fiscal, moral and political authority to take on the problem of

modifying this legislative management tool.

There is another, and less attractive, side to this coin of government management. That is program and cost management. As the Congress is becoming convinced that the government is doing an acceptable job of managing profit, the Congress is becoming increasingly concerned that the government is not properly structuring and managing its programs to get timely delivery of quality products at an acceptable cost.

I am not talking about a case like the GSA procurements, where wholesale improprieties were discovered. That was not a case of incompetent program management. It was a case of incompetent bureaucratic management and an abuse of talent. The GSA

experience really is an example of Congressional confidence in government profit management, since there was very little criticism of the profit element, but rather that the bureaucracy did not properly manage its contract managers.

Rather, the concern I am talking about is that the government is not properly managing its programs structures, progress and costs. Let me give you an example from the Department of Defense.

If we look at just the fifty major weapon systems currently being monitored in quarterly Selected Acquisition Reports, we see a dismal picture.

As of May, 1979, the cost of these fifty major programs has increased \$95 billion over the original cost estimates.

You naturally think that most of this increase is due to inflation. Not so. Only \$24 billion of this growth is caused by inflation. \$71 billion can be attributed to management-controlled issues.

These management-controlled issues have many causes. Quantity changes, engineering changes, cost control problems, schedule changes, support changes, and many other things. The responsibility for these changes, and the resulting cost increases, can be placed in several quarters. Quantity changes can be the result of funding constraints or program changes mandated by

Congress. Most of the other changes are within the control of the Department of Defense and the contractor.

There are many excuses for these changes. Major weapons systems are difficult to estimate. Improvements are put into the system as it is being developed. The mission changes. The threat changes. Nonetheless, Congress is becoming very impatient and want major changes in procurement philosophy and execution.

This story is repeated in other agencies and the Congress is not going to hold still for it much longer. In this matter there will be agreement between those who are convinced contractor profits are too high and those who are not afraid of the profit

picture. They will join together and exhibit increasingly intense interest in better program management and cost control.

It should not surprise us to see the coalition building to attack the problem. The new conservatism I described earlier is a business-like conservatism which will not put up with the bad management currently going on in many government programs.

So, there is good news and bad news. The good news is that there is increasing feeling in the Congress that profit is not evil and that the government has been and will be able to do business without allowing excessive profits.

The bad news is really only bad news for the government and contractor program managers who are not doing their job properly. If they plan poorly, structure programs poorly and manage the program poorly, they are in for a very rough time in the near future.

Since the government procurement is by nature inflationary, in that it consumes resources of money, raw materials and labor, without satisfying consumer demand, it is certainly not going to escape scrutiny by anyone interested in fighting inflation. Contractors will be allowed a fair profit. But government and contractors must work very hard to keep down unnecessary program costs or the Congress will take Draconian

measures to get your attention. You can have your profit, but not if you don't control your costs.