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Quality of Competition for Defense Contracts under "Better Buying Power"

Jesse Ellman

From their peak in 2009 to 2013, defense contract obligations have declined by over 25 percent. With budget caps in place through FY2021, and thus overall defense budgets unlikely to significantly increase in the near term, policymakers within the Department of Defense (DoD) have focused on getting greater value and efficiency using existing funding levels. A chief means to this end is increasing competition in defense contracting. Continuing and building upon efforts by his predecessor, Under Secretary of Defense for Acquisition, Technology, and Logistics Frank Kendall's Better Buying Power (BBP) 2.0 initiative lists "promoting effective competition" as one of seven major goals.[1] In late August of this year, Secretary Kendall released "Guidelines for Creating and Maintaining a Competitive Environment for Supplies and Services in the Department of Defense," setting forth new policy steps, review processes, and procedures to increase the amount and effectiveness of competition in DoD contracting.[2] On September 19, the draft version of Better Buying Power 3.0 presented by Secretary Kendall at CSIS continued the emphasis on competition in DoD contracts.[3]

Recent commentary, from oversight entities such as the Government Accountability Office[4] as well as outside analysts, reports on the success of DoD's efforts to promote effective competition. Reports like these conclude that competition not only failed to increase under BBP, but that it has actually declined. However, CSIS analysis concludes that such comments do not accurately capture the true state of competition in DoD contracting. Using data from the publicly available Federal Procurement Data System (FPDS) and drawing on preliminary research to be presented at the 2015 Naval Postgraduate School Acquisition Research Symposium, this paper shows how rates of effective competition in DoD contracting have changed over the last six years.

This paper focuses on three key breakdowns of FPDS competition data for DoD contracting:

- Overall trends in "effective competition" within DoD contracting
- Trends in effective competition rates by major DoD component
- Products/services/R&D as drivers of effective competition trends

[1] "Memorandum for Defense Acquisition Workforce—Better Buying Power 2.0: Continuing the Pursuit for Greater Efficiency and Productivity in Defense Spending," November 13, 2012, http://www.acq.osd.mil/docs/USD%28ATL%29%20Signed%20Memo%20to%20Workforce%20BBP%202%200%20%2813%20Nov%2012%29%20with%20attachments.pdf.

[2] For Secretary Kendall's report, see http://fedne.ws/uploads/082514_dod_competition_guidelines.pdf.

[3] For Secretary Kendall's briefing and draft materials, see http://csis.org/event/better-buying-power-30-discussion-under-secretary-frank-kendall.

[4] See, for example, "Defense Contracting: Early Attention in the Acquisition Process Needed to Enhance Competition," Government Accountability Office, May 2014, http://www.gao.gov/assets/670/662985.pdf.

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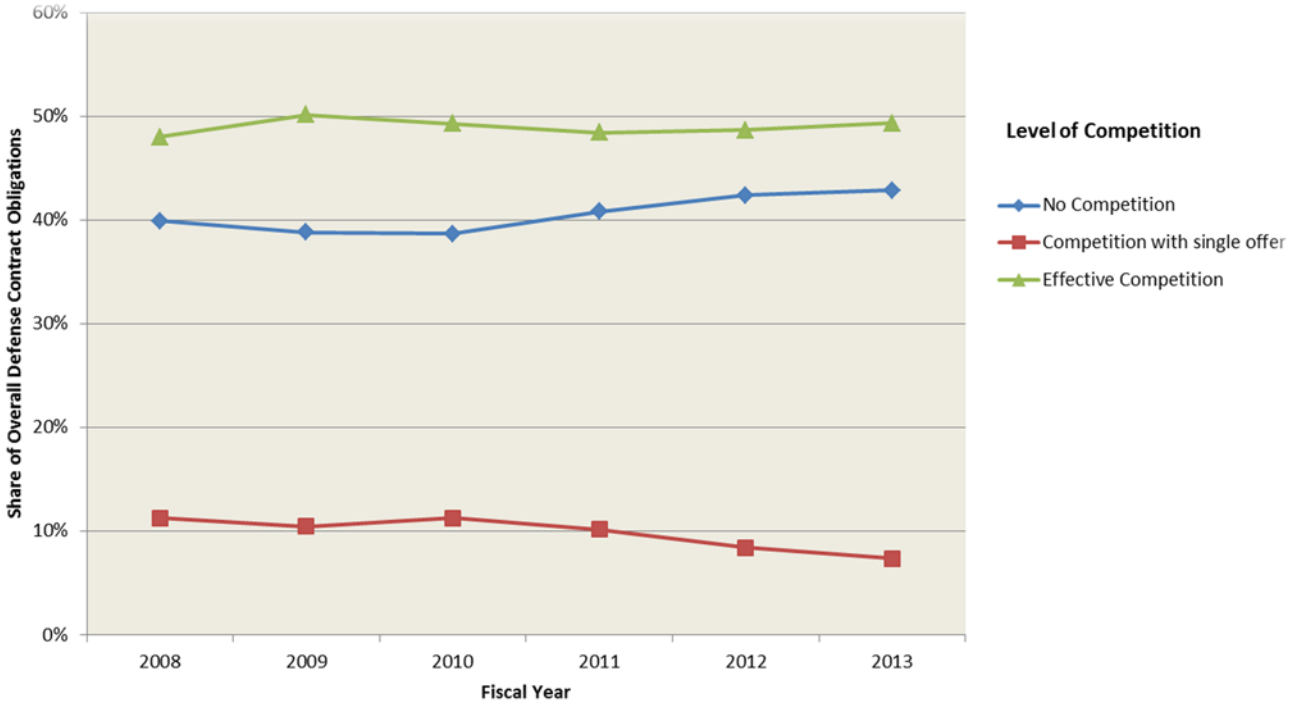
FAX (202) 775.3199

Overall Trends in "Effective Competition" within DoD Contracting

CSIS defines "effective competition" as a competitively solicited award that received two or more offers, which is similar to DoD's definition of effective competition.[5] This excludes contracts awarded after competitions receiving only one offer, which have accounted for as much as 11 percent of DoD contract obligations in recent years. CSIS excludes single-offer competition because the solicitations that receive only one bidder are less likely to see the expected benefits of competitive bidding. As a result, CSIS's rate of effective competition for overall DoD contracting is notably lower than the rate of competition for DoD cited in recent reports, including DoD's "Performance of the Defense Acquisition System—2014 Annual Report," released in June 2014.[6] That report cites a 57 percent overall competition rate (different from the effective competition rate) for DoD in 2013. As seen in Figure 1, by excluding single-offer competition, CSIS results show a 49 percent effective competition rate in 2013.

Figure 1: Level of Competition for Overall Defense Contract Obligations



Source: FPDS; CSIS analysis.

The figure shows that the rate of effective competition in DoD contracting has been remarkably consistent, fluctuating between 48 percent and 50 percent in each of the past six years. There was a slight shift within the category of effective competition, however; the share of contract obligations awarded after competition with three or more offers has increased slightly since the mid-2000s, whereas the share awarded after only two offers has declined. This could represent an actual increase in real competition.

[5] See "Department of Defense Competition Report for FY 2012," 4, http://www.acq.osd.mil/dpap/cpic/cp/docs/DoD_FY_2012_Competition_Report.pdf.

[6] For Secretary Kendall's 2014 annual report, see http://www.acq.osd.mil/docs/Performance-of-Defense-Acquisition-System-2014.pdf.

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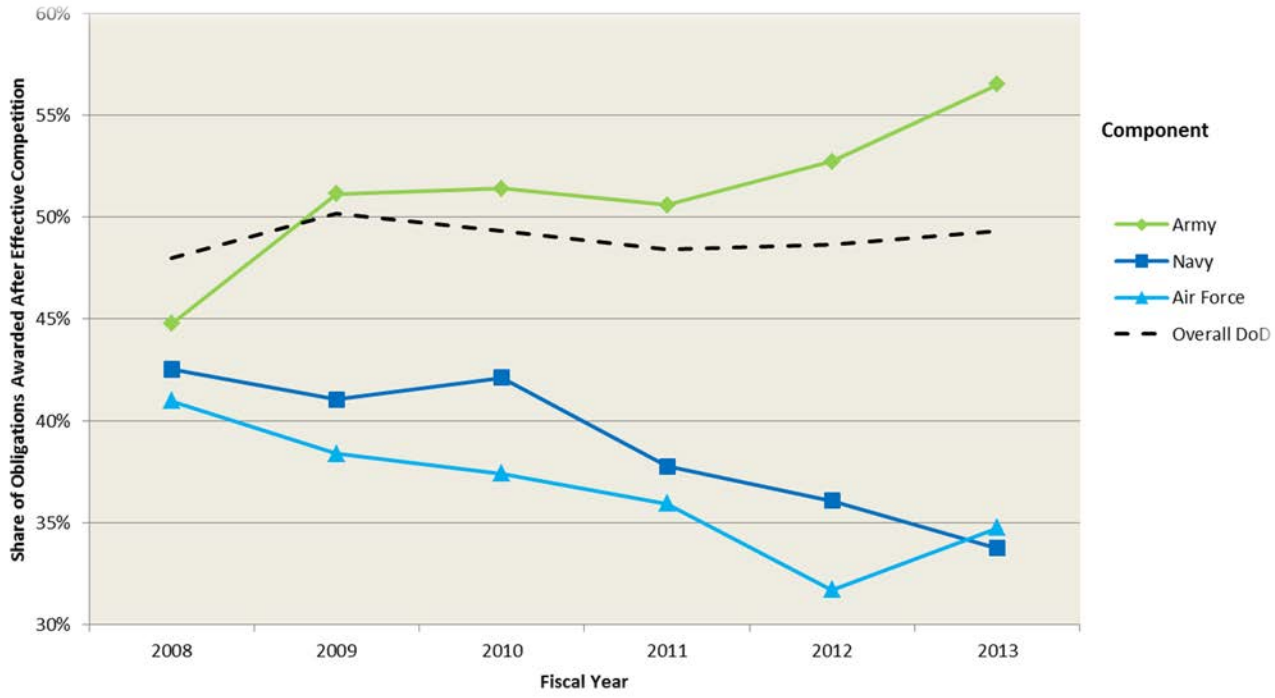
These results raise a significant question: if CSIS's data show that rates of effective competition have been steady in recent years, why do DoD's own data show a decline (from 62 percent in 2010 to 57 percent in 2013)? The explanation for this could be the decline in the share of contract obligations awarded after competition with a single offer, which fell from 11 percent in 2010 to 7 percent in 2013.[7] In parallel, the share of contract obligations awarded without competition increased proportionately. The data suggest that many single-offer competitive contracts could have been more appropriately solicited and awarded under an exception permitting noncompetitive contract awards. It thus seems likely that the category of single-offer competition masked some contract awards that would more properly have been solicited and awarded under sole-source justifications. Instead of competition declining, such contracts more appropriately recognize actual market conditions.

Trends in Effective Competition Rates by Major DoD Component

A major limitation of recent commentary on DoD competition trends is that looking only at overall DoD trends masks significant differences among the major DoD components. Implementation of centrally issued guidance is handled largely at the component and subcomponent level. Analysis of trends within those components is necessary to gain a more accurate picture of the impact of recent guidance to promote effective competition.

Figure 2: Share of Contract Obligations Awarded after Effective Competition, by Component



Source: FPDS; CSIS analysis.

As Figure 2 shows, there are significant differences in rates of effective competition between the Army, Navy, and Air Force. The Army has seen its rate of effective competition increase notably since 2008, from 45 percent in 2008 to 57 percent in 2013, surpassing the rate for overall DoD in every year since 2009. The Navy has seen

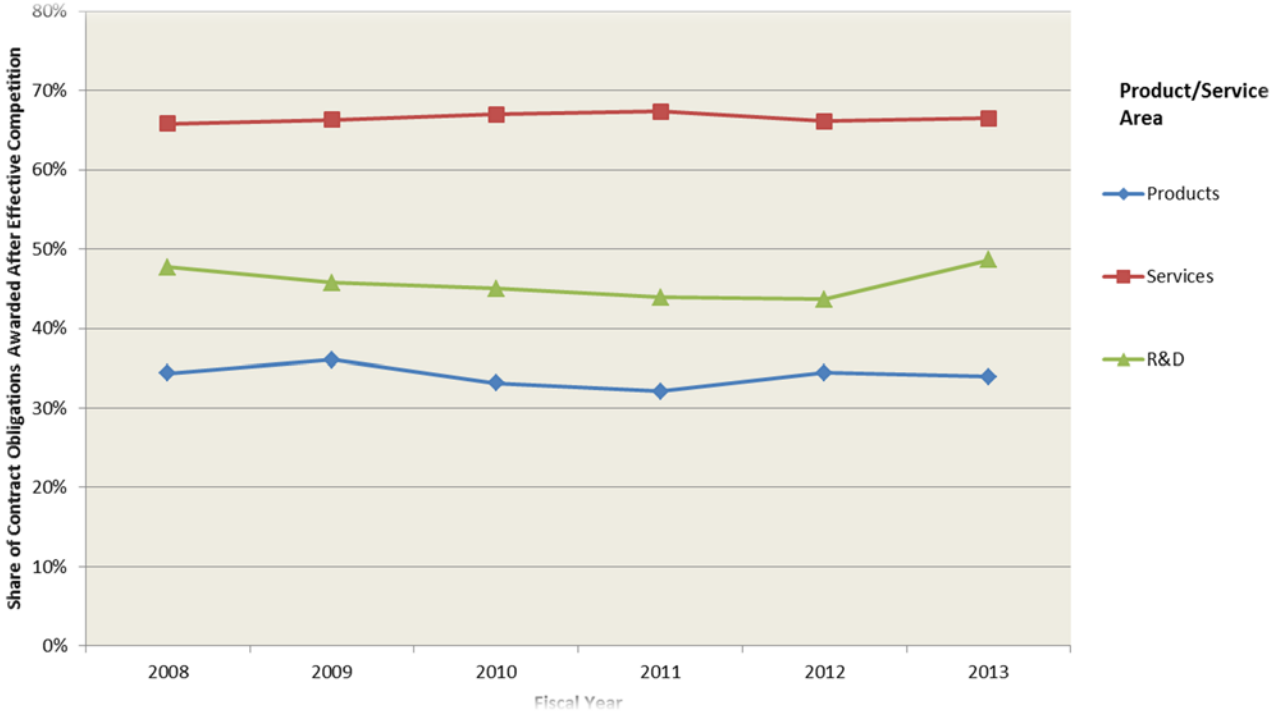
[7] The CSIS totals for effective competition plus single-offer competition are close, but not exact, matches to the DoD total competition rates. CSIS suspects that this is due to a minor difference in methodology regarding which contract obligations are included in the analysis, but the exact methodological difference remains unknown.

a steady decline in effective competition, from 43 percent in 2008 to 34 percent in 2013. Effective competition rates for the Air Force have declined similarly, from 41 percent in 2008 to 32 percent in 2012 (the lowest of any major component in the 2000–2013 period), but increased to 35 percent in 2013. There are many possible reasons for these differences among DoD components, and the next section of this paper looks as some of them.

Products/Services/R&D as Indicators of Effective Competition Trends

At first glance, the data in Figure 2 might be taken as an indication that the Army has been more successful at implementing the BBP guidance to increase competition, whereas the Navy and Air Force might appear to have been less successful. The true picture is significantly more complicated, however. One approach is to examine how rates of effective competition vary based on what CSIS calls the "area" of what is being purchased—that is, products, services, and research and development (R&D).

Figure 3: Share of Contract Obligations Awarded After Effective Competition, by Area



Source: FPDS; CSIS analysis.

As Figure 3 shows, those rates have been remarkably stable within each area for DoD as a whole. Between 2008 and 2013, approximately one-third of DoD contract obligations for products have been awarded after effective competition, whereas nearly two-thirds of DoD contract obligations for services have been awarded after effective competition.[8] For R&D, slightly less than half of contract obligations were awarded after effective competition in most years. The lower rate of competition for products reflects the fact that DoD does not buy complex defense platforms in sufficient numbers to sustain more than one supplier. Many weapon

[8] These rates of effective competition for products and services have been remarkably consistent since 1991, the first year in which CSIS has reliable data.

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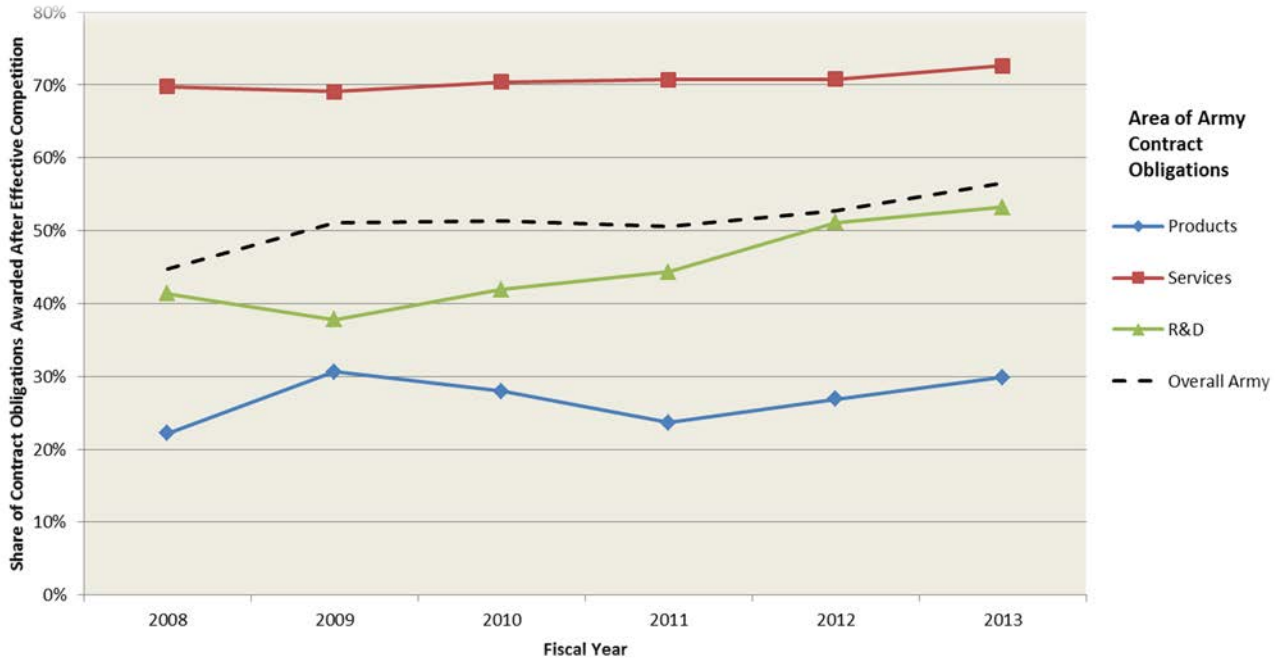
systems are competed in development, but subsequent production contracts are generally awarded on a sole source to the contractor that won the development competition.

The next section of this paper examines rates of effective competition for products/services/R&D for each of the three major DoD components.

Army

Figure 4: Effective Competition for Army Contract Obligations, by Products/Services/R&D



Source: FPDS; CSIS analysis.

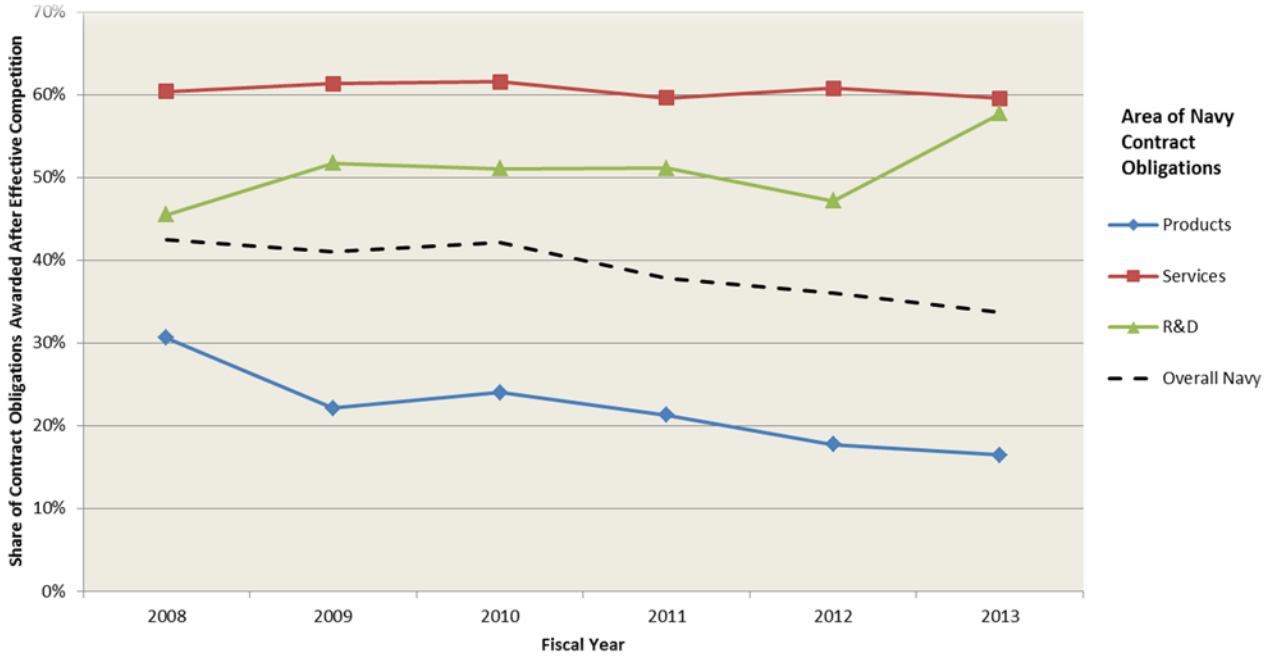
As Figure 4 shows, nearly 70 percent of Army contract obligations for services have been awarded after effective competition in every year since 2008. The rate of effective competition for Army R&D has risen from 38 percent in 2009 to 53 percent in 2013 (coinciding with the cancellation of large Army R&D efforts such as the Future Combat Systems), whereas the rate for products has fluctuated between 22 percent and 31 percent. The overall increase in effective competition within the Army can be attributed in large part to a significant shift in what the Army is contracting for: the share of Army contract obligations for products decreased from 49 percent in 2008 to 35 percent in 2013, whereas the share awarded for services increased from 45 percent in 2008 to 60 percent in 2013. (The share awarded for R&D declined from 7 percent in 2008 to 5 percent in 2013.) A large share of the Army's increase in effective competition can thus be directly attributed to the Army's high rates of effective competition for services contracts. The most recent CSIS report on government-wide contracting for services showed that, across the federal government in FY 2012, approximately 60 percent of contract obligations for equipment-related services (ERS) and professional, administrative, and management support (PAMS) services were awarded after effective competition.[9] In FY

[9] Gregory Sanders et al., *Structure and Dynamics of the U.S. Federal Services Industrial Base, 2000–2012* (Washington, DC: CSIS, September 2013), http://csis.org/files/publication/130827_Sanders_ FederalServicesContractingTrends2000-2012_Web.pdf.

2013, the Army awarded 76 percent of ERS contracts and 69 percent of PAMS contracts (two of the three largest categories within Army services contracting) after effective competition.

Navy

Figure 5: Effective Competition for Navy Contract Obligations, by Products/Services/R&D



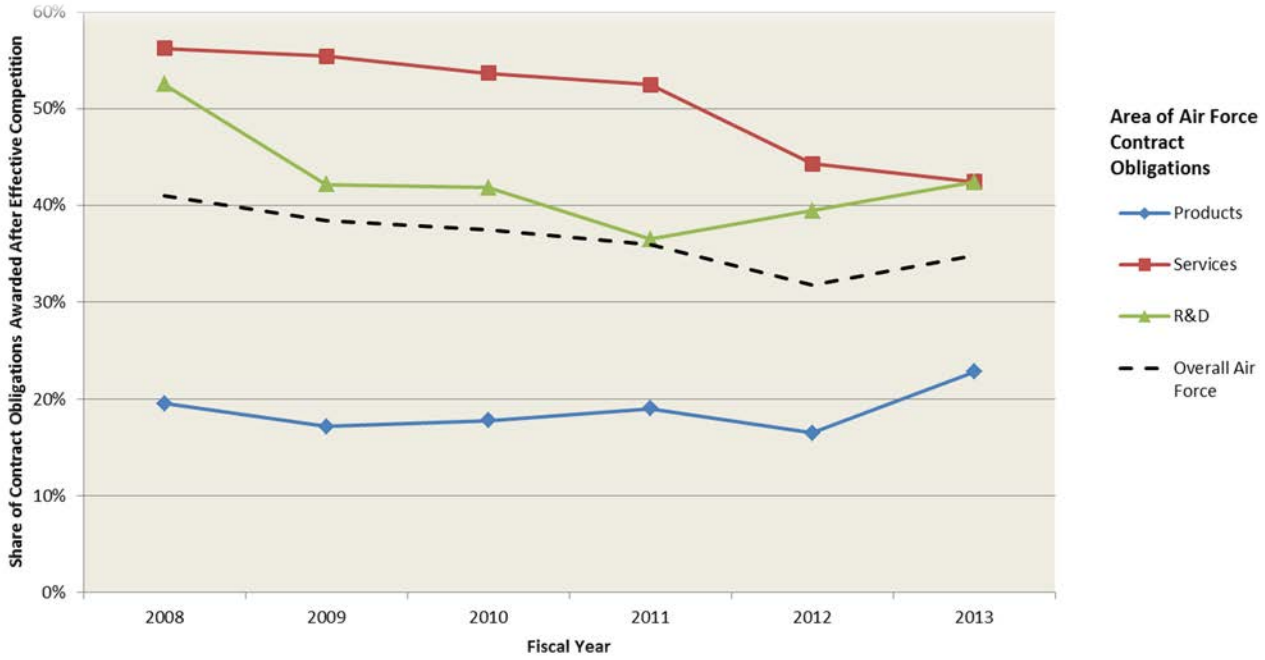
Source: FPDS; CSIS analysis.

As Figure 5 shows, approximately 60 percent of Navy contract obligations for services have been awarded after effective competition in every year since 2008. The rate of effective competition for Navy R&D had been relatively steady, but it increased sharply in 2013, from 47 percent in 2012 to 58 percent. The rate of effective competition for products has declined by nearly half, from 31 percent in 2008 to 16 percent in 2013.

Just as the increase in Army effective competition rates was driven by a shift in what was being contracted for, the decline in Navy effective competition rates overall was driven by similar factors. The share of Navy contract obligations awarded for products has increased significantly in recent years, from 48 percent in 2009 to 59 percent in 2013, whereas services (38 percent in 2009, 30 percent in 2013) and R&D (14 percent in 2009, 10 percent in 2013) have declined. The Navy's shift in recent years towards spending a higher percentage of their contract dollars on products, which are often necessarily awarded as sole-source contracts, appears to be the main driver of the decline in Navy effective competition rates.

Air Force

Figure 6: Effective Competition for Air Force Contract Obligations, by Products/Services/R&D



Source: FPDS; CSIS analysis.

As Figure 6 shows, the share of Air Force contract obligations for products that was awarded after effective competition was relatively stable at a level around 20 percent from 2008–2012, but it jumped to 23 percent in 2013. The share of R&D contract obligations awarded after effective competition declined from 53 percent in 2008 to 36 percent in 2011, but rose to 42 percent by 2013. And, in contrast to the Army and Navy, the share of services contract obligations awarded after effective competition declined from 56 percent in 2008 (already lower than the Army or Navy for any year from 2008–2013) to 42 percent in 2013.

This decline in the rate of effective competition for services contracts within the Air Force is broad-based: rates of effective competition for ERS (46 percent in 2008, 34 percent in 2013) and PAMS (49 percent in 2008, 37 percent in 2013) both declined sharply, with most of the decline coming between 2011 and 2012. Those two categories of services accounted for 75 percent of Air Force services contract obligations in 2013, but every category of services (except for medical services, which have never accounted for more than 1 percent of Air Force services) saw declines in rates of effective competition during the period observed. CSIS has not determined at this time why Air Force rates of effective competition for ERS and PAMS have declined so steeply in recent years. The study team will continue to investigate to determine the drivers behind this decline.

Also in contrast to the Army and Navy, there were only relatively minor shifts in the share of contract obligations awarded for products and services within the Air Force as rates of effective competition declined between 2008 and 2012. The data indicate instead that the decline in Air Force effective competition resulted from significant declines in competition for services contracts with the Air Force, across nearly all categories of services.

Final Thoughts

Although rates of effective competition have not increased overall for DoD during the period where the Better Buying Power initiatives have been in effect, neither have they declined to the extent suggested by recent commentary. A careful examination of the data shows that rates of effective competition with the major DoD components are heavily influenced by the changes in the share of contract obligations for products and services. For the Army and Navy, fluctuations in rates of competition seem to result from preexisting competition trends. For the Air Force, by contrast, the decline in effective competition appears to result from a broad-based reduction in effective competition for services. CSIS urges policymakers to examine whether any particular policies or practices within the Air Force can account for their declining rate of effective competition for services.

While defense products have the most room to improve in terms of effective competition rates, the realities of demand and supply for major defense platforms are likely to make significant improvements difficult in the near term. Where there is only enough demand to keep one vendor in business, generating competition is nearly impossible. There appears to be room to improve the level of effective competition for services and R&D, though there is likely some share of both where only one vendor is capable of performing.

CSIS will continue to analyze trends in defense competition, as well as other trends in contracting by both DoD and the broader federal government, in the months to come, with the latest edition of the Defense Contract Trends report series (with FY 2013 data) to be released on October 16, and a broader research effort on defense competition to be presented at the 2015 Naval Postgraduate School Acquisition Research Symposium.

Jesse Ellman is a research associate with the National Security Program on Industry and Resources at the Center for Strategic and International Studies. Inquiries may be directed to him at jellman@csis.org.

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