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TOP ISSUES 2011

NATIONAL DEFENSE INDUSTRIAL ASSOCIATION

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The Voice of the Industrial Base

An open letter from the President and Chief Executive Officer of the National Defense Industrial Association (NDIA)

The origin of NDIA dates back to 1919 with the formation of the Army Ordnance Association, which was later renamed the American Defense Preparedness Association (ADPA). With the merger of ADPA and the National Security Industrial Association (NSIA) in 1997, the newly named NDIA became America's leading defense industrial association promoting national security. NDIA is a non-partisan, non-profit, international association located in Arlington, VA.

Our mission is to **advocate** for cutting-edge technology and superior weapons, equipment, training, and support for the war-fighter and first responder; **promote** a vigorous, responsive, government-industry national security team; and to **provide** an ethical forum for the exchange of information between industry and government on national security issues.

Currently, the association's membership base consists of individuals from the entire spectrum of the defense and national security industrial base and individual government employees. Included in the Association's membership are organizations that sell goods and services to the various Departments of the Executive Branch of government. Also included are organizations that advise and assist these companies or that desire to develop a relationship with them through the networking opportunities inherent in association membership.

NDIA's **2011 Top Issues** were developed by the senior industry leadership of the Association, prepared by the Government Policy Advisory Division, reviewed by the Education and Lobbying Committee, and approved by NDIA's Board of Directors on November 23, 2010. The **Top Issues** serve to guide the Association's advocacy and educational activities throughout the year. The issues highlighted within this text are broad in nature and are essential to maintaining a strong, viable defense industry capable of meeting U.S. national security requirements.

Each year, NDIA distributes this document to the Congress, key decision makers within the Executive Branch, Allied Governments, industry leaders, and the Association's membership. On behalf of the more than 1,722 corporate members and over 84,640 individual members of NDIA, it is our hope that the issues raised and recommendations offered herein will be seriously considered and addressed by the appropriate government officials.

Sincerely,

A handwritten signature in black ink, appearing to read "Lawrence P. Farrell, Jr.", written in a cursive style.

Lawrence P. Farrell, Jr.
Lieutenant General, USAF (Ret.)
President and CEO
NDIA

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ISSUE 1: Ensure an Ethical, And Agile Acquisition System Responsive to the DoD's Needs

- **REVISE DOD BUSINESS PROCESS REFORM**
- **RECOGNIZE AND ENCOURAGE INDUSTRY PROFIT DRIVEN METHODOLOGY TO REDUCE DOD COSTS**
- **PROPERLY DEFINE AND MANAGE INHERENTLY GOVERNMENTAL FUNCTIONS**
- **REVISE THE RULES ON ORGANIZATIONAL & PERSONAL CONFLICTS OF INTEREST**
- **IMPROVE EDUCATION, TRAINING AND RETENTION OF THE FEDERAL ACQUISITION WORKFORCE**
- **CONTINUE TO STRESS CONTRACTOR ETHICAL CONDUCT**
- **ENSURE THAT THE GOVERNMENT HAS FULL ACCESS TO COMMERCIAL PRODUCTS AND SERVICES**
- **IMPROVE THE USE OF EARNED VALUE MANAGEMENT SYSTEMS**
- **REPEAL THE THREE PERCENT WITHHOLDING ON ALL GOVERNMENT CONTRACTS**

Revise DoD Business Process Reform

The DOD is proposing a major Defense Federal Acquisition Regulations (DFARS) change that will establish unreasonable penalties for contractors who have a deficiency in any one of their of six (6) major business systems. These systems include: accounting, estimating, purchasing, government property management, material management and accounting, and earned value management. The proposed rule establishes that payment withholds be established for systems with deficiencies and mandates a 10% withhold on all receivables for each system with an identified deficiency. The withhold amount can grow up to 50% for delays in corrective actions, and if the unacceptable risk continues could grow to 100% of all payments until the identified deficiencies are corrected. NDIA continues to support the goal of detecting and preventing waste, fraud and abuse of taxpayer dollars. We further support the establishment of clear and uniform criteria for defining acceptable business systems and due process to resolve systems questions. However, we strongly oppose the proposed rule as an inflexible regulatory regime that is an unnecessary intrusion on the contractual relationship that unfairly and arbitrarily establishes a punitive approach to managing contractor business systems. Industry has concerns that the proposed rule increases oversight and enforcement cost with little benefit. Arbitrary payment withholding threatens companies, especially small business, with financial insolvency and creates a barrier to entering or remaining in the defense marketplace. It is also important to recognize that the government already has authority to address business system deficiencies through withholds and other appropriate actions under existing Federal Acquisition Regulations.

NDIA strongly believes that DoD should take action to narrow the overly broad definitions in the proposed rule, that any identified business systems failures must correlate to government risk, and that any payment withhold amounts relate to risk introduced by the system deficiency. The government must also establish a set time to perform follow-up audits to end the withhold process.

Recognize and Encourage Industry Profit-Driven Methodology to Reduce DoD Costs

On June 28, 2010 Dr. Ashton Carter, Assistant Secretary of Defense for Acquisition, Technology and Logistics, advised industry of a new program efficiency initiative with the goal of increasing warfighting capabilities by two or three percent without proportionately higher budgets. He issued a memorandum on improving efficiency by reducing unneeded or low priority overhead and outlined the following framework for restoring affordability in defense programs:



- Increase real competition for defense programs
- Increase the use of fixed price contracting
- Limit cost reimbursable contracting only when programs lack specification, and phase out time and materiel contracts
- Consider improved cash flow for price reductions
- A-line profits to performance risk
- Strengthen the skills of the acquisition workforce
- Improve the consistency and quality of audits
- Establish PEO for services contracting in each service
- Reduce industry overhead

NDIA clearly recognizes the budget constraints that drive this new DOD initiative and welcome the opportunity to engage in real and meaningful efforts to reduce industry cost and to exploit best practices to improve efficiency. This is also an excellent opportunity to review FAR and DFARS processes to eliminate or revise inefficient processes that are government unique and add cost with marginal value. Recent studies estimates that increased costs of approximately 18% may be added to defense products by application of unnecessary regulations.

NDIA is committed to working with the DoD to help find best practices that will encourage such savings and will encourage efficiency and submitted an extensive list of recommendations and suggestions to DoD, some of which included:

- Review the DoD competitive process eliminating non value added processes and paperwork. Fully embrace the guiding principles enunciated in FAR Part 1 as they apply to internal administrative processes.
- Standardize the source selection process, utilizing, to the greatest extent possible, the Air Force's Performance-Price-Tradeoff evaluation criteria, thereby reducing complex, time-consuming technical evaluations.
- Encourage increased partnering between the contractor and DCMA and DCAA and empower the ACO to render independent judgment in decision making vice full adoption of DCAA positions. Audit and legal reviews are advisory in nature and Contracting Officers should be encouraged to embrace the power and responsibility inherent in their position, and make decisions with as little oversight and review as possible.
- Establish effective performance based training to the DoD program entities to create greater specificity and specification in defense requirements.
- Maintain cost reimbursable and T&M contracting capabilities.
- Review non-statutory process mandates to reduce

government unique market processes. Contracting and program management decisions should be focused on statutory compliance and industry "best practices", where not otherwise precluded in the FAR or by law, should be embraced.

- Improve cash flow (i.e. twice a month payments) in exchange for reduced price. Review new punitive policies that reduce cash flow and increase the cost of government programs like the newly proposed business systems rule.
- Increase the use of commercial specification and commercial buying practices.
- Recognize that the industrial base is comprised large business, mid size business and small business. Often mid cap businesses struggle more to remain viable with little recognition to their challenges.
- Ensure that requirements define the "true needs," recognizing that "nice to haves" raise cost.

Properly Define and Manage Inherently Governmental Functions

NDIA has significant concerns with the federal government's implementation of insourcing. NDIA has joined with other industry trade associations in calling for an end to quota driven insourcing. NDIA fully recognizes the importance for the federal government to enhance their internal capabilities and to rebuild critical skills, especially in the acquisition workforce. The DoD has made it clear that their focus on insourcing of inherently governmental functions and closely related to inherently governmental functions is to ensure the department has control over operations and missions. Implementation of insourcing initiatives has resulted in each department being given a budgetary and savings target, thus creating numeric quotas. The use of quotas to manage insourcing goals conflicts with the foundation of the program, which is to enhance internal workforce critical capabilities. In recent insourcing efforts, industry has experienced the targeted recruitment of skilled employees and the insourcing of contracts without the rigor of mandated cost comparisons. In addition, small businesses are negatively impacted by the conversion of contractor jobs to government workforce as the numbers of conversions are significant when taken as a percentage of the small business workforce.

In January 2010, DoD released a Directive Type Memorandum that identifies a range of cost and assumptions to help evaluate private and public sector cost. While a positive step, the memorandum's assumptions continue to exclude a host of public sector cost. As an example, floor and rental space, educational assistance programs, sick leave and vacations and holidays are excluded. Today, no process exists within DoD to accurately

and fully account for public sector bottom line cost that can be the basis of public private sector cost comparison. NDIA supports establishing guidance which requires that a rigorous cost analysis be performed prior to any insourcing of individuals or contracted activities. In addition, NDIA strongly recommends that the military services and defense agencies consult with the Small Business Administration to determine the effect on small businesses of any proposed insourcing recommendations, and that measurable means be implemented to ensure small businesses are not adversely impacted by any proposed insourcing actions.

It is important that the government harmonize its approach to insourcing and return to the principals identified by Secretary Gates to re-build critical skills and remove the conflict associated with numeric quotas. NDIA continues to believe that adherence to the OMB memo of July 29, 2009 "Managing the Multi-sector Workforce" and the DoD memo of May 28, 2009 "In-Sourcing Contracted Services – Implementation Guidance" will provide a rational approach for resolving insourcing issues.

On March 31, 2010, the Office of Federal Procurement Policy published a proposed policy letter to clarify when work must be reserved for federal government employees. This guidance adopted the inherently governmental definitions from the Federal Activities Inventory Reform Act (FAIR). An inherently governmental function under this guidance is one so intimately related to the public interest that performance must be by federal government employees. NDIA supports this attempt to more clearly define inherently governmental functions.

Revise the Rules on Organizational & Personal Conflicts of Interest

On April 22, 2010, DoD proposed broad and sweeping reforms to organizational conflict of interest (OCI) rules in major defense acquisition programs. NDIA believes the proposed rules went beyond the legislative intent of section 207 of the Weapon Systems Acquisition Reform Act (WSARA) (Public Law 111-23). Under the proposed rules, defense systems developers, including all subsidiaries and affiliates, would be precluded from participating in the development or construction of a weapon system and also from participating in systems engineering and technical assistance requirements. The proposed rules add a new definition for OCIs to the DFARS by identifying three types of OCIs: unfair access to information, biases in ground rules, and impaired objectivity. The rule identifies methods for resolving an identified OCI such as: avoidance, limitations on future contracting, mitigation and waiver. NDIA has expressed concerns with the proposed rule

in a number of areas. The coverage was not limited to major defense acquisition programs as contained in the WSARA legislation and now applies to all DOD procurements, including most commercial items procurements. The proposed rule encourages adopting exclusion as the principal solution to identified OCI's. This approach to OCI resolution contradicts DoD stated policy of finding the least intrusive resolution. The primary responsibility for identifying a conflict of interest now rests on the contractors with little guidance to DoD to identify conflicts. The proposed rule also treats a contractor as a single entity even if only a small segment of the company does business with DOD. The rule has the potential of creating havoc on task and delivery order contracting with new procedures for post-award conflicts.

It is important to recognize the strength of specific OCI mitigation mechanisms that can, and do, overcome bias and impaired objectivity concerns through the establishment of affiliate firewalls similar to those that separate foreign ownership and control from US companies. These auditable processes can overcome concerns of unequal access to information, bias, and impaired objectivity through organizational, geographic and informational separation. This process would allow contractors' affiliates to operate on both the Systems Engineering and Technical Assistance (SETA) and development phases of weapons systems if contractors adequately separate their affiliates from the contractor by structural mechanisms such as organizational, physical and financial separation and are approved by the Secretary of Defense.

NDIA recognizes that the evolving role of contractors may give rise to the potential for personal conflict of interests (PCI). These conflicts typically occur when contractor employees perform Contract and Advisory Services contracts, program management, and acquisition support requirements. Currently regulators are pursuing proposed rulemaking and are exploring appropriate means of mitigating personal conflict of interest. NDIA encourages the government to work closely with industry in addressing personal conflicts of interest by contractor employees. PCI policies must fully define the term personal conflicts of interest and identify the types of performance that introduce PCI concerns. Further, mitigating policies must include a standard DFARS contract clause for ensuring that contractor employees are free of any personal conflicts of interest, and must identify the contracting methods, types, and services that raise heightened PCI concerns.

Improving Education, Training and Retention of the Federal Acquisition Workforce

DoD, in conjunction with the Defense Business Board, has established policies and plans for increasing the acquisition workforce. These objectives include growing the acquisition workforce by 20,000. (from 127,000 to 147,000) between 2010 and 2015. 10,000 of these new hires will come from contractor conversions (insourcing) and 10,000 from new hires. NDIA continues to be an advocate of bolstering and improving the federal acquisition workforce and believes that an overburdened and under-staffed acquisition workforce is frequently a factor in problems that arise during the life-cycle of major acquisition programs. Clearly, maintaining an effective acquisition workforce continues to be a real challenge for federal agencies. Insufficient and improperly skilled employees create contracting quality problems that impact the ability of agencies to meet their mission requirements. The challenge in integrating and training the new additions to the acquisition workforce can take three or more years. These realities are evident in many agencies as the skill and experience levels continue to drop. There has also been new government incentive hiring programs for acquisition professionals that value advanced degrees over experience for journeyman positions. Such incentive programs will continue to field workers in progressively more responsible senior positions with little practical skills and training and may not contribute significantly to the acquisition work force knowledge base. It is important to that the government focus more on experience of the acquisition candidate than higher education levels.

Resolving shortages of qualified personnel in all federal agencies, and in particular the acquisition workforce, calls for increased attention in the recruitment processes, including the full use of the government web site, www.usajobs.com. This government-wide site is a disincentive as the first experience for many as they consider government employment. NDIA urges the administration to continue to improve their recruitment tools to favorably attract qualified job seekers. The current human capital crisis must be met with immediate investment and effective policies.

Many organizations within the defense industrial base continue to offer a government-industry acquisition professional exchange program. These programs serve to broaden practical experience and to balance government training with an appreciation of industry policies and practices that can help both industry and government without invoking conflict of interest concerns. Robust and inclusive training is essential for acquisition professionals to gain critical skills and maturity.

NDIA supports efforts to institute human resources reform within government to meet the expanding acquisition workforce crisis, including allowing pay for performance, career progression and promotion with a foundation based upon learning and organizational contributions, not just time in grade.

Continue to Stress Contractor Ethical Conduct

The defense industry is frequently exposed to the media focus on contractor misconduct. Notwithstanding these reports, the fact remains that there is insufficient data to support claims of widespread waste, fraud or abuse in government contracting. This is the direct result of industry management and focus on training in business practices and ethical conduct. Throughout the U.S. industrial base, company policies and practices are institutionalized and foster transparency and accountability in the contracting process. These changes continue to encourage a supportive approach in working with government oversight agencies and are grounded in a fundamental focus on self-governance. The Federal Acquisition Regulations (FAR) Council published a rule requiring contractors receiving awards in excess of \$5 million and with performance periods of 120 days or more to have a written code of ethics and business conduct within 30 days after contract award. The government also issued new mandatory disclosure rules that require contractors to report when there is credible evidence of a violation in the law or significant overpayment. NDIA continues to support contractor ethics initiatives including effective policies, compliance training and internal controls to better manage compliance in all contracting requirements. New ethics policies and expanded compliance actions by industry result in an industrial base that provides high quality products and services, transacted in an ethical and transparent environment, at fair and supportable prices. (See NDIA's Ethics Code at the end of this publication.) NDIA encourages sustaining a broad-based effort between industry and the government to reinforce high ethical standards and responsibility in the entire acquisition process.

NDIA stresses through its seminars and educational events critically important procurement integrity information throughout the U.S. industrial base and recognizes that procurement integrity problems and ethical lapses negatively impact the public trust of government and industry alike. Adverse procurement integrity issues detract from public and private sector priorities to ensure that the federal procurement system is and remains fair, balanced and accountable. The federal marketplace is critical to our national security and industry and government must work together to enforce existing laws, maintain effective checks and balances, and eliminate

the potential for unethical conduct.

Ensure that the Government has Full Access to Commercial Products and Services

It is critical that the federal government has full access to new and emerging commercial technologies and that those technologies can be acquired using existing commercial item acquisition practices embedded in current law and regulation. These realities are grounded in the recognition that defense procurement cycles from development to completion for government unique products sometimes take many years to realize operational fielding. In contrast, commercial product and technology cycles move much faster, typically within a 12 to 18 month business cycle, usually as a result of ongoing, incremental development and market pressures on industry to compete and deliver superior products and services. Irregular warfare threats have created an environment where potential enemies have been able to rapidly adapt and apply commercial products and technology to maximum effect against US forces in the field. We must be able to maintain pace with those threats by supporting and improving the existing commercial item acquisition process infrastructure that allows DoD to take advantage of the best and most advanced commercial technology and to place that technology in the hands of our war-fighters quickly.

Accordingly, federal regulations governing the acquisition of commercial products and services must remain flexible to permit the acquisition of new and emerging commercial technologies. This includes giving government acquisition professionals the flexibility to exercise preferences for commercial items by utilizing all available contract types, crafting innovative risk management strategies, engaging with industry on profit policy and generally adopting/endorsing existing commercial item acquisition practices in areas such as the use of pricing data, performance of market research and the use of commercial products and services in the drafting of requirements. While these objectives seem clear, legislation and a growing number of regulatory restrictions threaten the potential for government to timely acquire commercial products and services from the private sector in a manner designed to maximize our technological warfighting edge.

NDIA continues to advocate for limits on proliferation of government unique acquisition requirements that ignore the commercial marketplace and that undermine our government's full and free access to the best commercial products and services. NDIA objectives call for a number of important legislative and regulatory changes described below that empower the federal acquirers to rely on commercial solutions using proven com-

mercial practices. Collectively these goals encourage more commercial companies to enter the federal marketplace.

- Protecting proprietary intellectual property (IP) and technical data: The government's efforts to expand commercial acquisition practices must recognize the importance of protecting contractor IP and proprietary business and technical data and information related to commercial items. The increasing failure of agencies to safeguard such information is eroding the commercial sector's interest in developing technology for government contracts with private funds that may be compromised by government acquisition practices.
- Establishing permanent simplified acquisition authority for commercial items: It is important that the federal government make permanent the application of simplified acquisition procedures originally established in the 1996 Clinger Cohen Act. This authority has been extended six separate times and should now be made permanent.
- Clearly define commercial services: Amend the current definition for commercial services found under 41 U.S.C. 403 (12) (E) and (F) and revise 41 U.S.C. 403 (12)(A) as follows: Commercial item means – (1) any item including any item of supply or services used by the general public or by non-governmental entities for purposes other than governmental purposes.
- Revising the competition requirements for time and materials contracts: The 2003 Services Acquisition Reform Act limited authority to acquire commercial services on a Time and Material (T&M) basis only when such awards were based upon competition. NDIA believes that authority should be amended to add “based upon competition or justified sole source determinations.”
- Restricting the growth government regulation over commercial item pricing documentation requirements that encourage an increased government demand for cost data as a default for price reasonableness determinations.
- Applying commercial item acquisition regulations consistently throughout DoD commands and agencies and reducing the number of local command guidance, handbooks, memoranda and acquisition practices that undermine or contradict existing commercial item regulation and foster non-standard approaches to commercial item acquisition.
- Encouraging increased government market research capabilities that emphasize the use of commercial items and services when drafting government contract requirements and comport with the regulatory preference for commercial items and services.

Improve the Use of Earned Value Management Systems

NDIA supports the objectives of DoD and other federal agencies to resolve Earned Value Management Systems (EVMS) implementation issues and to help program managers effectively manage their programs. Industry and the DoD, however, face unique challenges in meeting these objectives. Under the current approach to oversight, company processes and procedures are being overturned in favor of audit driven initiatives, which provide little flexibility for innovation or implementation of best practices.

Industry believes, first and foremost, that the DoD must recognize a company's inherent need for a consistent set of program management processes within its business units that can be tailored based on program risk and product maturity, and that the DoD should therefore exercise restraint in directing "one size fits all" industry processes. A consistent set of program management processes across operating units improves data quality, allows cost efficiencies through the standardization of processes and related training, and results in a stronger, more resilient industry to support our armed services. The potential for industry to upgrade information technology systems and to constantly improve and expand the availability of integrated program management information to internal and external users requires governmental support for processes that facilitate such improvements.

While industry wants flexibility, contractors must ensure that program management data are integrated in terms of schedule, cost, technical and risk parameters. For this reason, industry must follow its validated processes. However, this alone will not prevent the frequent program cost and schedule growth that is so often blamed on poor use of Earned Value Management (EVM). EVM is a significant program management process. However, EVMS alone cannot fix a contract with ill defined requirements, poorly defined or disputed scope, or insufficient funding. EVMS will measure progress and highlight performance issues, but it cannot prevent cost growth unless requirements are clearly understood, requirements "creep" is controlled, and program funding is stable. The apparent legislative and oversight agencies' perceived focus on EVMS as "the problem" (i.e., as the cause of cost and schedule overruns) is misinformed and misguided; this focus gives insufficient attention to the root causes of scope and cost growth.

Contributing factors to inefficient EVMS implementation and use, comprising three areas in which government and industry can collaborate to achieve needed improvements, include:

A. People – Both the government and industry are challenged by a limited pool of available resources with the

skill sets necessary for integrated program management, particularly scheduling and EVM. The development of a training program, with support by academia, to build a pool of these critical resources would be beneficial to both the government and industry.

B. Process –

1) Instability of requirements and funding of programs inhibits the effective implementation of EVMS. Industry recommends that more focus be placed on pre-award contract activities, including funding of pre-award Integrated Baseline Reviews, to ensure that programs have a reasonable probability of successful execution.

2) The DoD should perform a cost/benefit analysis of the current oversight process. Currently, the emphasis is on strict compliance rather than the efficient management and use of program performance data, by contractor and customer alike, for effective decision-making.

3) Numerous guidance documents or operating procedures used in the oversight process are becoming de-facto policy, and their content often impacts industry's cost effective/value-added program management capability, including EVMS. The DoD should be judicious in its creation of additional EVM guidance.

4) Reciprocity between DoD elements and/or oversight functions concerning a common interpretation and approach for EVM implementation and use is a necessity. The current business environment is fractured by competing visions as to "how to implement" EVM by the various entities within the DoD.

C. Tools – Contractors must work to improve the capability, usefulness, and efficiency of program management tool sets. Industry encourages the DoD to continue to enhance and modernize their internal systems to adequately summarize, analyze and use the schedule and cost data that industry provides for decision-making purposes.

Government and industry effort must be concentrated on understanding the probability of successful execution of their programs, improving system engineering to ensure the proper definition of requirements, and establishing adequate and stable funding for the contract. Once these objectives are achieved, contractors and government can focus on training, management use of earned value data, and the deployment of modern EVMS analytical tools to provide program management discipline. These efforts, which are encouraged by NDIA, coupled with well-planned, disciplined contracting and control of requirements, will allow the government and

industry to provide the products that our warfighters need to maintain our nation's security more efficiently and more cost-effectively.

Repeal the Three Percent Withhold on All Government Contracts

Section 511 of the Tax Increase Prevention and Reconciliation Act of 2005 (P.L. 109-222) as section 3402(t) of the Internal Revenue Code, mandates that federal, state, and local governments withhold 3% of nearly all of their contract payments, Medicare payments, farm payments, and certain grants. NDIA strongly believes that compliance with this law will impose significant, unnecessary financial burdens on both the public and private sectors.

NDIA is especially concerned with the very real impact on our nation's small businesses, particularly when much of the hoped-for economic recovery is placed squarely on their shoulders. Prime contractors may well pass much of the 3% expense down to their smaller subcontractors. Additionally, the small businesses that contract directly with the government will feel even more acutely the 3% withholding cut into their already narrow profit margins, especially as they will be forced to increase debt levels and lines of credit to ensure their ability to maintain operations. Businesses of all sizes do not need additional limits on capital while the economy begins to recover.

The 3% withholding is a flat percentage of revenues from government payments, bears no relationship to companies' taxable incomes, and will restrict cash flow needed for day-to-day operations and investments. In addition, the administrative and capital investment costs to businesses and governments will be substantial and the withholding mandate will be exceedingly complicated to implement.

The National Defense Authorization Act for Fiscal 2007 (Public Law 109-364) required DoD to estimate the cost to implement the 3% withholding. DoD reported to Congress on April 14, 2008 that it would cost DoD \$17 billion over five years to implement. At a time when the Administration, the DoD and the defense industry are all struggling to achieve efficiencies and reductions in overhead costs, the un-programmed cost to administer the withholding comes at a critical time when providing goods and services to the warfighter is, and should be, our number one priority.

There have been numerous legislative and regulatory measures put in place since the enactment of the 3% withholding law that have focused on increasing tax compliance and enhancing

transparency for companies receiving government payments. These measures put the burden of the law and regulation more on the tax avoiders, and provide a positive inducement to law-abiding firms and the public agencies with which they do business. All these initiatives taken together obviate any rationale or need for retaining the withholding mandate and will be far more cost-effective for the government. NDIA continues to believe these are a much better approach than the costly, broad brush mandate of the 3% withholding law.

The overwhelmingly large percentage of government contractors who abide by current laws and regulations should not and must not be made to shoulder the burden of the few who do not. The regulatory vigilance mandated by these additional measures will keep tax avoiders out of the public contracting market in the first place, rather than shifting the compliance burden to law-abiding firms and the federal, state and local governments.

While the withholding requirement is not scheduled to go into effect until January 1, 2012, it is already proving costly, and such costs will increase exponentially as the implementation deadline moves closer. Businesses and governmental entities are starting to expend resources now in preparation for implementation due to major system and process changes needed for withholding, reporting, and reconciling the millions of affected payments annually. These changes have to be made well in advance of 2012.

NDIA strongly urges Congress to enact a two-year implementation delay quickly to prevent governments and companies from incurring these un-needed and un-programmed additional costs. The unintended consequences of the 3% withholding will likely drive many of our nation's struggling business from the government marketplace and could drive them out of business all together.

In addition, NDIA urges Congress to require an independent entity to assess the costs of the 3% withholding regime for federal, state, and local governments and the companies that provide goods and services to them.



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ISSUE 2: The Defense Industrial Base – Now and in the Future

- **LEADERSHIP AND CULTURAL PERCEPTIONS**
- **RESEARCH AND DEVELOPMENT IN MANUFACTURING**
- **STRATEGIC MANUFACTURING CAPABILITIES FOR NATIONAL SECURITY**
- **MANUFACTURING WORKFORCE AND INFRASTRUCTURE**
- **FACILITATE A CAPABLE, RESPONSIVE U.S. MUNITIONS BASE**

America's military strength remains vital to preserving the nation's interests and sustaining international stability. While much of this strength is derived from the professionalism and skills of America's armed forces, the technologically superior military platforms developed and produced by the U.S. defense industrial base has been vital to ensuring a superior fighting force. In both peace and war, America's defense manufacturing industrial base has allowed the U.S. to meet the full spectrum of missions the military has been called upon to fulfill. Securing America's military dominance for the decades ahead will require an industrial base that can retain a highly skilled workforce with critical skill sets and sustained investment in platforms to respond to any potential threat.

U.S. national security depends heavily upon our domestic manufacturing capabilities and the DoD relies upon the U.S. defense industrial base for leap-ahead, innovative technologies with which to equip our warfighters. It is critical to understand that in the defense sector, if the government doesn't fund a particular system, industry will abandon the effort, including the underlying industrial capabilities. Work force and resources will move on to other funded programs. The segment that is not funded will eventually wither and industry will lose that capability, and once lost, these domestic capabilities take substantially more time and funding to regain. The U.S. industrial base is in crisis and needs attention, and based upon several key studies, the U.S. defense industrial base is facing a similar and parallel crisis. Moreover, the current government procurement policies will not produce the competitive, responsive, efficient and innovative industrial base that is required to face these challenges.

NDIA believes there are four main themes that need to be addressed to sustain a successful manufacturing policy: leadership and cultural perceptions; research and development in manufacturing; strategic manufacturing capabilities for national security; and workforce and infrastructure.

Leadership and the Cultural Perceptions

The health of the defense industrial base has to be elevated to a higher level in the scope of U.S. policy considerations, and this requires active and senior leadership, both within the Administration and the DoD. The U.S. agriculture sector represents 1% of our GDP, employs 1% of the workforce, and is represented by a cabinet Secretary. The manufacturing sector is ten times larger and is represented by an Assistant Secretary for Manufacturing and Services within the International Trade Administration of the Department of Commerce. Manufacturing and the industrial base are important enough for representation by at least a Deputy Secretary, which would also raise the level of coordination between government agencies.

In turn, defense manufacturing issues need more senior leadership within the DoD to unite policy, strategy, investment and implementation. Currently the DoD has a Director for Industrial Policy, with responsibility for stimulating competition and sustaining industrial capabilities within the defense industrial base. This office monitors the industrial base and uses authorities to promote competition or defense priorities over commercial production. However, DoD requires senior leadership for manufacturing which has the authority to define strategy and set policy, but also implement R&D alignment, infrastructure revitalization and workforce investment across all of DoD. There is also a problem in the U.S. with the per-

ception of manufacturing. In a recent survey by the Manufacturing Institute and Deloitte, 81% of respondents believe that America's manufacturing base is either important or very important to their standard of living and to economic prosperity, and 77% think the U.S. needs a more strategic approach to the development of its manufacturing base. However, only 30% of respondents would encourage their children to pursue a manufacturing career. The perception is that manufacturing is something akin to an iron foundry in the year 1900, but the reality is a manufacturing workforce is as likely to use a keyboard as a wrench, and operates in a clean, safe environment. The government needs to change this outdated perception in order to get the high-caliber workforce needed for high-tech manufacturing, particularly in the defense sector where the workforce is aging.

Research and Development in Manufacturing

Manufacturing research and development is literally the core of an innovation machine that this nation's economic engine is founded upon. Specifically, 70% of industrial R&D is performed by manufacturing-based companies, and the bulk of that R&D is applicable to manufacturing processes and procedures. This R&D results in the application of new technologies, new materials, and overall increased productivity within the manufacturing processes. All of these advances can make U.S. manufacturing more competitive within the global market, but only if the results of the R&D stay in the U.S. and add to the GDP for a significant period

The federal government has a role in the determination of R&D priorities, development of R&D clusters, investments for national security, and leveraging/incentivizing private industry investment. A crucial need at the macro level is the planning and management of a collaborative and highly connected research enterprise which spans large and small businesses, academia, and government research labs. Recent studies of best in class foreign R&D strategies have concluded that developing regional "clusters" of specialized R&D partners provide the most effective model for government, academic and industry innovation, and increase the probability of transition to domestic manufacturing capabilities. These clusters also offer the highest leveraging potential for government investment and have proven to drive associated capital investment in regional facilities and infrastructure. Government policy should support the formation and management of these clusters by offering a centralized process for creating and developing them and provide for collaboration between these clusters utilizing a "hub and spoke" model. Collaboration between the clusters offers innovation and product development opportunities that drive technology transition into complex systems, which offer

the greatest benefits.

With respect to manufacturing R&D for national security, the DoD has a single program that is legislatively chartered to develop and transition manufacturing processes and fabrication required for the production and support of defense systems known as the DoD Manufacturing Technology (ManTech) Program. For over 50 years, the ManTech Program has been department's investment mechanism for staying at the forefront of defense essential manufacturing capability. The ManTech program consists of four major areas:

- Effective management and delivery of processing and fabrication technology solutions
- Active support for a highly connected and collaborative defense manufacturing enterprise
- Active support for a strong institutional focus on manufacturability and manufacturing process maturity, and
- Active support for a healthy, sufficient and effective defense manufacturing infrastructure and workforce.

The effectiveness of this joint services program is well demonstrated in a recent report to Congress that identified over 100 projects funded by ManTech from FY03-FY05 which have been implemented and yielded a cost avoidance of \$6.3B. However, the investment in the ManTech program, currently averaging \$210M level in the President's FY11-FY16 budget, is not at the level required to effect substantial changes in the defense industrial base. A 2006 Defense Science Board study on the ManTech program concluded that the proper investment level for ManTech should be 1% of the DoD RDT&E budget, or about \$700M. This investment level would enable the DoD to pursue technical solutions for the most pressing defense manufacturing and industrial base problems facing the U.S. today and in the future.

Strategic Manufacturing Capabilities for National Security

One of the most critical balancing acts within the industrial policy domain is between open market competition and the creation or subsidizing of a domestic industrial capability. Industrial capabilities in manufacturing processes, raw materials, components, and technologies are disappearing from the U.S. every day in the form of off-shoring, business failures, supplier mergers, material shortages, global environmental restrictions and lack of demand. In some cases, disappearing domestic capabilities can be replaced with overseas suppliers, but this is not possible for defense-essential capabilities, where access to domestic sources is a national security requirement. The current DoD industrial policy is to rely on market forces (competition) to create, shape, and sustain the industrial, manufacturing, and technological capabilities necessary to



provide our fighting forces with systems that can engage and win full-spectrum warfare. However, when absolutely necessary, the DoD will intervene to create and/or sustain competition, innovation, and essential industrial capabilities. If intervention is warranted, the DoD can use mechanisms such as direct investment in supplier infrastructure, leveraging R&D investments, procurement assistance, purchase commitments, or collaboration with other federal agencies to drive growth in domestic vendor demand.

One vital program which provides direct support for defense-essential manufacturing capability is the Title III program, part of the Defense Production Act (DPA). The Title III program provides a set of broad economic authorities, found nowhere else in law, to incentivize the creation, expansion or preservation of domestic industrial manufacturing capabilities for technologies, components and materials needed to meet national security requirements which are determined through extensive evaluation as both defense essential and in need of support. The DPA authorizes the President to: (1) require performance under government-placed contracts or orders deemed necessary or appropriate to promote the national defense; (2) allocate materials, services and facilities in such manner, upon such conditions and to such extent as he shall deem necessary or appropriate to promote the national defense; and (3)

control the distribution of scarce and critical materials in the civilian market place that are critical to the national defense. The President's authority to place contracts under the DPA has been delegated to certain agencies and is used most frequently by DOD. The program is administered by the Department of Commerce's Office of Strategic Industries and Economic Security (SIES).

Another critical issue is the need for steady, long-term access to affordable raw materials. Sometimes, having domestic manufacturing capability is not enough, as in the case of secure access to raw materials. A U.S. industrial base can depend upon materials which are not readily available or affordable, causing additional cost, schedule or failure. The Government Accountability Office concluded that the DoD lacks a consistent, department-wide framework to monitor its supplier base. This vulnerability is particularly salient for strategic materials such as titanium, cobalt and rare earth materials, which have major applications in advanced weapons systems such as smart bombs, night-vision goggles and radar. Today, China produces 97.3 percent of the world's supply of rare earth minerals; Russia produces 1.6 percent, while the United States produces only 1.1 percent. Policy is needed on this topic establishing a federal-level working group to identify and act upon the multiple options, such as stockpiling, pursuing trade violation

cases, developing domestic/alternate sources, or entering into long-term purchase commitments.

Other key requirements exist for defense manufacturing, including the growing problems with counterfeit parts, environmental regulations, and visibility into the lower levels of the supply chain. Counterfeit parts are increasingly finding their way into the defense supply chain, particularly for legacy systems with longer life cycles. A key enabler for reducing counterfeit components is dealing with domestically based trusted suppliers, using a Qualified Vendor List. Trusted suppliers keep record of all transitions and thus can trace parts back to the Original Equipment Manufacturers (OEMs). However, in cases of obsolescence, there are no longer parts available from the OEM, and sources are used to procure these parts which do not have clear provenance. The DoD is defining both processes and technologies which can assist the procurement workforce in spotting and rejecting counterfeits.

Similarly, there are a growing number of environmental regulations establishing de-facto global restrictions on critical manufacturing materials. A recent NDIA White Paper, “Maintaining a Viable Defense Industrial Base,” lays out the dangers of global manufacturing standards, such as the elimination of lead-based solder and hexavalent chromium corrosion coatings. In the case of solder, the substitute lead-free solders are much less reliable than traditional tin-lead solders for aerospace and defense applications that involve harsh operating environments and long operating lives. Also, the U.S. is increasingly unable to obtain commercial-off-the-shelf (COTS) electronics that contain tin-lead solders and finishes. Further, pure tin finishes being increasingly used by COTS electronics suppliers as a low-cost approach to avoid the use of lead are prone to the random growth of “tin whiskers” that can lead to unpredictable short circuit failures. The solution demands focused investment in the development of alternative materials that offer performance equal to or better than the ones replaced, and a clear DoD policy determining how to identify and apply alternatives.

A crucial tool for assessing the U.S. defense industrial base is visibility into the lower levels of the supply chain, at the second and third tier. Traditionally, DoD takes the responsibility for monitoring the capabilities and competitive viability of prime contractors, OEMs, and key first tier suppliers. The capabilities and viability of lower tier suppliers is monitored by the primes and OEMs, which have access to and contracts with these suppliers. The recent economic challenges have highlighted the dangers in not understanding these lower tiers, which are predominately small businesses and most at risk

for failure from demand volatility or access to capital. This situation must change and DoD policy should specifically state that the DoD is responsible for monitoring and stress-testing the industrial base to the lowest levels. Technology advances should help these assessments, with newer modeling of supply chain networks able to stress-test the vendor networks and highlight risk.

Manufacturing Workforce and Infrastructure

The manufacturing workforce has been shrinking over the past 40 years, as productivity increases have allowed manufacturing output to remain steady using fewer labor hours. However, in the past two recessions (2001, 2008), the drop in employment has been precipitous, with over 4.5 millions manufacturing jobs lost in the past 10 years. The reason for this large decrease has been the interaction of three forces: offshore manufacturing, increased productivity and a decline in manufactured goods demand during the recessions. Offshoring is a response to lower foreign structure costs, and increased productivity is the natural competitive reaction to those costs. The only method of increasing employment in the manufacturing sector is to increase the demand, either domestically or through exports, and this requires new technology, either in terms of new products or, more often, advanced manufacturing. Advanced manufacturing technologies, particularly at the enterprise level, requires a workforce with special skills, such as familiarization with 3-D models, distributed supply chain interaction and digital work instructions. These skills will be required in the near future in order for the U.S. to compete in either the domestic or export markets, and there are no current government programs or leadership to drive this innovation into the workforce.

Moreover, the U.S. industrial infrastructure, and particularly that which supports defense manufacturing, has to be updated into a highly connected enterprise in order to enable the most advanced manufacturing practices. The use of service-oriented architectures and model based engineering requires substantial infrastructure investments, and policies are needed to incentivize these capital improvements within both the nation’s industrial base and the government organic base. An effective role for the DoD would be as a first adopter for many of these enterprise-level advanced manufacturing models. This would inevitably lead to a standards-based U.S. lead in these techniques and practices, which would transition to the domestic manufacturing base, create significant growth potential for new, cutting-edge U.S. manufacturing jobs, and help strategically position the defense industrial base in the increasingly hypercompetitive global economy.



Facilitate a Capable, Responsive U.S. Munitions Industrial Base

Funding for ammunition procurement is expected to decline significantly in the coming years. DOD and industry must ensure that a U.S. munitions industrial base funded at reduced levels is nonetheless able to remain capable, competent and responsive.

Historically, in response to budgetary pressures, funding provided for procurement of ammunition has declined at high rates. During the period FY 85-94, funding of ammunition procurement declined by 80% as budget cuts were made across the board. Little consideration was given to the effects of this decline on long-term viability of the industrial base, and no planning was done to maintain munitions production capability. The result was a crippling of the industry. More than 75% of the companies exited the business, never to return. Total collapse was barely averted through the intercession of the Office of the Secretary of Defense (OSD) with yearly increases in budget funding, by Congress with additional appropriations above the budget, and eventually by increased ammunition production demands created by the Global War on Terrorism.

Overall DOD funding has not declined due to continued funding of the Global War on Terrorism and “reset” costs. At the same time, however, the military services’ modernization programs will continue to extract a heavy burden on procurement funds over the coming budgets. Given the lessons of history, it is assumed that funding for ammunition procurement will decline in coming years. One of two alternate futures will result: 1) adverse impacts will accumulate to the point of threatening the continued existence of a viable and responsive U.S. munitions industrial base, as occurred in the past. Subsequent rescue will, once again, be expensive and will create signifi-

cant turbulence in the industry; or 2) purposeful actions taken now by DOD and industry can ensure that the industrial base remains in good health and able to meet the nation’s needs.

The Single Manager for Conventional Ammunition (SMCA) has undertaken several initiatives in cooperation with the SMCA’s industry partners to 1) identify required industrial base capabilities during the next 5 years, and 2) develop management tools that can assess the impact of budget decisions on those required base capabilities. The Industrial Base Sourcing Study (IBSS) has analyzed the current base production capabilities by product sector. The study identified base capabilities that are over or under the capacity required during the next five years. This information provides industry with a reasonable basis for making prudent capital investment or divestiture decisions. Management tools under development by the SMCA include the Industrial Base Assessment Tool (IBAT) and the Minimum Sustaining Rate (MSR) data bases. The IBAT allows the SMCA to identify the impact of a proposed budget on the industrial base for a specific key product area. The MSR data base allows the SMCA to identify the impact of a proposed budget on a specific key facility in the base. These initiatives must be aggressively pursued and completed. Further, a protocol ensuring that these management tools are used and the results acted upon by the services and DOD leadership is a necessary ingredient for reasoned budget decisions. Time is of the essence. DOD and industry must continue to actively partner to achieve an industrial base characterized by a skilled workforce; modern and efficient equipment and facilities capable of surge performance; and financial incentives sufficient to persuade businesses to remain in the base. The tools are in place. Purposeful actions are now required to maintain a munitions industrial base that is capable of responding to the future munitions needs of our nation’s armed forces.

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Issue 3: Increase Government Contract Usage of All Small Businesses

- **DISINCENTIVES FOR NOT MEETING SMALL BUSINESS SUBCONTRACTING GOAL**
- **PERMANENTLY REAUTHORIZE THE SMALL BUSINESS INNOVATIVE RESEARCH PROGRAM (SBIR)**
- **COMPREHENSIVE REVIEW OF SMALL BUSINESS SIZE STANDARDS FOR SERVICES INDUSTRY**
- **UNIFIED PARITY AMONG ALL SMALL BUSINESS CATEGORIES (8A, WOSB, VOSB, SDVOSB, HUBZONE, HBCU & MI, INDIAN INCENTIVE [INCLUDING ALASKANS AND HAWAIIANS], SDB) DURING FEDERAL CONTRACT COMPETITIONS**
- **IMPACT OF REGULATORY COSTS ON SMALL FIRMS**

Disincentives for Not Meeting Small Business Subcontracting Goals

Federal agencies have bundled many smaller contracts into one larger contract to ease the government contracting burden. As the federal acquisition workforce increases, the need for bundling should proportionally decrease. In the meantime, in an effort to retain qualified small businesses, the govern-

ment added contractual language to support small business subcontracting goals. Potential prime contractors submit Small Business Subcontracting Plans as part of their proposal to obtain the contract and after award; they are expected to meet those goals. However, the terms of the subcontracting goal have allowed the winners of these larger contracts to “overlook” the value of small businesses in the solution provided to the agency. In other words, larger primes are not held accountable in monetary terms for enforcing the small business subcontracting goals for which they signed up in their proposal. NDIA supports agency assessments of large contractors’ efforts to use small businesses as defined in the contractors’ Small Business Subcontracting Plan. The reporting mechanisms exist to measure progress against goals on a contract-by-contract basis, but the lack of accountability and oversight has enabled poor performance in this area. NDIA supports the use of a past performance system as a mechanism for reporting poor performance regarding utilization of small businesses. NDIA also recommends improving contract reporting tools such as Federal Procurement Data System – Next Generation (FPDS-NG) to include reporting of small business subcontracts through prime contracts to allow better analysis of small business participation as subcontractors in defense acquisition programs.

Permanently Reauthorize the Small Business Innovative Research Program (SBIR)

Small businesses provide some of this nation’s most innovative technological ideas. The Small Business Innovative Research Program (SBIR) provides critical early funding for research on new technologies which continue to give the U.S. an edge in technical advancement, especially in the defense and national security sectors. As NDIA testified before the House Committee on Small Business, NDIA believes it is imperative for Congress to permanently authorize the SBIR program. We strongly support efforts to provide additional funding to commercialize technology. DoD should also expand outreach efforts (to be performed by small businesses) to the small business community as a means of providing useful and timely information to assist qualified firms in understanding the opportunities and methodologies for becoming a member of the defense industrial base.

Comprehensive Review of Small Business Size Standards for Services Industry

NDIA encourages a comprehensive review of NAICS code small business size standards, specifically regarding service-related industry codes. Service NAICS codes should be among the first 1/3 reviewed by SBA in 2011-12, particularly in light of the increased focus on service-oriented small business in



the DoD Efficiency Initiatives. Annual increases for revenue-based size thresholds and promotion of employee count thresholds for services ensure a more viable transition of small businesses into full and open competition.

Clearly, NAICS size standards have not kept pace with inflation. For example, the Military and Aerospace Equipment and Military Weapons exception to NAICS Code 541330 is the most commonly used NAICS Code for Navy Engineering Support. In 1994, the SIC Code 8711 equivalent was \$20M and today it has reached only \$27M while the Employment Cost Index (ECI) for Wages and Salaries of Private Industry Workers has increased each year from 1.4% to 3.9%. (The inflation rate of wages and salaries is lower than the inflation rate of benefits/fringe every year, so ECI understates the total annual increase of services costs to the government). The \$20M threshold of 1994, if adjusted by each year's ECI, would currently be \$32.5M instead of \$27M.

NDIA supports the use of employee count thresholds for service-related NAICS Codes. Although larger employee count NAICS thresholds are prevalent for manufacturing/products, a manufacturing company's size is not as employee-dependent as the services industry. A services company provides

customers solutions and obtains revenue and profit through its employees. This revenue provides the investment capital needed to establish and sustain quality systems and infrastructure required to compete long-term in the federal marketplace. When a small service company is forced to partner with other companies to pursue large small business contracts, they do not always obtain the same level of investment resources to quickly grow from the small business program.

Unified Parity Among All Small Business Categories (8a, WOSB, VOSB, SDVOSB, HUBZone, HBCU & MI, Indian Incentive [including Alaskans and Hawaiians], SDB) During Federal Contract Competitions

Federal law requires that the government set aside 23 percent of its contracts to small businesses. The federal government also defines small business categories and associated goals that comprise the 23 percent. When agencies set aside contracts for a specific small business category to meet the federal guidelines, they reduce their opportunity to receive innovative and cost effective solutions from other categories. For example, if the contract is set-aside for Small Disadvantaged Businesses, a Woman-Owned business would be restricted from the competition even though that firm's solution may provide

the best value to the government. Although federal regulations establish the various individual set-aside requirements for each defined small business, NDIA supports parity among all small business categories during federal contract competitions. Opening the competitive field to all small business categories would reduce agency workload required to determine the appropriate small business category. Many resources are expended by both the contracting officials and small businesses when requesting, developing and reviewing sources sought and/or marketing research to determine the appropriate category. In some instances, because the agency small business category goal is not being met, contracting officials select a category that may or may not have sufficient qualified small businesses to compete for the work, thereby limiting innovation and cost effectiveness. NDIA supports the Women-Owned Small Business (WOSB) program and believes WOSBs should be on equal footing with other socioeconomic groups.

Impact of Regulatory Costs on Small Businesses

A major concern for NDIA is to expand small business participation in DoD, DHS, and other procurements by federal agencies. Small businesses play an important part in the overall U.S. economy, representing more than 99% of all employers including 51 percent of private-sector workers. Small businesses represent 44% of the total U.S. private sector payroll, employs 40% of high tech workers (such as scientists, engineers, and computer programmers) and makeup 97.3% of

all identified exporters (30.2% of known export value). Small businesses account for nearly all of the self-employed, which comprise seven percent of the work force. Small businesses play a role in federal contracting with about 33.3% of federal prime and subcontract dollars

According to a recent study prepared for the Small Business Administration, as of 2008 small businesses (defined as firms with 20 or fewer employees) face an annual regulatory cost of \$10,585 per employee, which is 36% higher than the regulatory cost facing large firms (defined as firms with 500 or more employees). Compliance with environmental regulations costs 364% more in small firms than in large firms and the cost of tax compliance is 206% higher in small firms. For small manufacturing firms, regulatory compliance cost per employee is more than double the compliance cost for medium-sized and large firms. NDIA fully recognizes the need for rules and structure when doing business with the federal government; however, the disproportionateness of the burden imposed on small business is a major decision factor for small businesses that are in or would like to be in the federal marketplace.

In the legislation and rule making process, NDIA strongly urges Congress and the Administration to take into account the cost of doing business with the federal government, especially for the nation's small businesses that are our single largest source of innovation and new technologies.

Annual Cost Per Employee of Federal Regulations by Firm Size				
Type of Regulation	Cost All Firms	Fewer than 20 Employees	20-499 Employees	500 or More Employees
All Federal Regulation	\$8,086	\$10,585	\$7,454	\$7,755
Economic	\$5,153	\$4,120	\$4,750	\$5,835
Environmental	\$1,523	\$4,101	\$1,294	\$883
Tax Compliance	\$800	\$1,584	\$760	\$517
Occupational Safety and Health Homeland Security	\$600	\$781	\$650	\$520
Source: The Impact of Regulatory Costs on Small Firms, by Nicole Crain and Mark Crain, 2010. U.S. Small Business Administration, Office of Advocacy				

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Issue 4: Sustaining Military Readiness While Providing For the Future

- **STRENGTHEN SCIENCE, TECHNOLOGY, ENGINEERING AND MATH (STEM) EDUCATIONAL OPPORTUNITIES FOR US CITIZENS**
- **NAICS CODES FOR MODELING & SIMULATION**
- **EVOLVE ENTERPRISE INFORMATION ENVIRONMENTS AND SECURITY**
- **INCREASE FUNDING FOR GROUND ROBOTICS RESEARCH, DEVELOPMENT AND ENGINEERING**

Strengthen Science, Technology, Engineering and Math (STEM) Educational Opportunities for U.S. Citizens

The U.S. defense and homeland security industries face challenges in filling some of the best and most critical technical jobs in our country. The U.S. is not producing enough graduates trained in science, technology, engineering, and mathematics (STEM) who qualify for security clearances. The graduates we do produce are not representative of the population of the U.S., reducing the diversity of the workforce that feeds innovation and creativity. The problem of a smaller, less diverse STEM workforce presents a serious risk for national security over the next decade, as Baby Boomers retire without an employable talent pipeline to replace them.

NDIA first began to advocate STEM education in 2007. Since then, the lack of clearable STEM graduates has become increasingly important, even gaining the attention of both major candidates during the 2008 presidential campaign. The leadership provided in this area by NDIA chapters, divisions and affiliate organizations has contributed significantly to advancing NDIA's reputation as a leading advocate for STEM.

NDIA has positioned itself to become part of the solution by establishing the STEM Workforce Division (SWD). Its goal is to increase the supply of quality, diverse, clearable STEM workers by leveraging the resources of our individual members, chapters, divisions and affiliates, working in conjunction with government, and partnering with educational organizations to raise awareness and accelerate the growth of existing, proven initiatives. This is critical to sustain our national security supremacy and improve the technical competitiveness of America's workforce. The SWD provides a forum for effective interaction between government, industry, academia, and the public for improving STEM graduation rates and strengthening a STEM workforce to support national security requirements. The division's executive board is comprised of exceptional and passionate representatives from each discipline. In 2009 the SWD completed a comprehensive report on its STEM activities which may be viewed at: www.ndia.org/stem. The report is organized chronologically and details the major actions taken by NDIA Chapters, Divisions, and staff. It is updated annually to include activities that have happened during the past year.

The SWD has worked closely with other associations in the creation of the Business and Industry STEM Education Coalition (BISEC). BISEC will engage at the national level to create awareness of the STEM challenge and engage in a national level dialog in creating innovative ways to increase and measure improvement in STEM education and worker readiness. NDIA's part will be to take that national dialog and turn it into local action. Quarterly meetings of the SWD are being held in conjunction with chapters to bring scalable and portable initiatives to each geographic location to help the local STEM-savvy leadership with ideas, metrics, tools and connections to make meaningful improvements that make sense for them.

NDIA also recognizes that the national defense workforce is not just made up of scientists and engineers. Our manufacturing workforce also requires a high degree of mathematic and scientific literacy in order to be effective on the shop floor and our manufacturing facilities. We must turn our attention, therefore, to broader scope efforts to increase the scientific, technical and mathematical literacy of ALL students that are

graduating from high school (and increase the number that do make it to graduation as well). A lack of manufacturing expertise will result in an inevitable decline in U.S. worker productivity heralding a time when the US is no longer an economic force in the world. NDIA, through its various divisions and chapters, is committed to ensuring we have the capability to continue the economic vitality that is critical to national security.

Ultimately, it is imperative that we increase the number of enthusiastic students who are qualified to enter vocational, undergraduate and graduate programs in STEM fields. With industry, government, and community involvement, NDIA believes this can be achieved and our national security workforce will be sustained and strengthened. To succeed, we as stakeholders in the national security of the U.S. must develop and support unique, exciting, and inspiring ways to encourage young Americans to pursue STEM careers.

NAICS Codes for Modeling & Simulation

An issue that has been frustrating the modeling & simulation industry for years is the lack of specific NAICS codes for modeling & simulation (M&S). Without specific codes, M&S work is not separately tracked and is bundled under other codes, making it impossible to quantify the size and scope of this industry.

In 2004, during the last NAICS revision, a coalition of industry groups (including the National Training and Simulation Association (NTSA), an affiliate of NDIA, submitted a proposal for new M&S NAICS codes to the Economic Classification Policy Committee (ECPC), an agency of the U.S. Census Bureau. The ECPC declined to make the proposed changes.

Last year, a similar coalition, led by NTSA, submitted a revised proposal to create new NAICS codes for M&S. The proposal was carefully crafted according to the guidelines published by the ECPC, and after consultations with the Chair of the ECPC. The 2009 proposal more clearly illustrated the unique nature of M&S, and provided considerable data on the size and scope of the industry, as well as compelling evidence of the growing recognition of the importance of M&S as recently proclaimed by H. Res 487 of the 110th Congress.

Unfortunately, the ECPC once again recommended against the creation of new codes for M&S, citing NAICS “production-based principles,” and asserting that “Simulation is not an industry. Simulation is a method or a specialized regimen that is produced and consumed in the provision of other services – training, testing, entertainment, etc.”

NTSA has submitted a formal response to the recent rejection, arguing that the ECPC’s logic is flawed, and that the principles of NAICS have been misapplied in this case. NTSA will continue to monitor this issue and work for the creation of unique NAICS codes for modeling & simulation. Copies of the proposal, the rationale for rejection, and a draft letter of opposition can be obtained by contacting Patrick Rowe, NTSA’s Director of Membership at prowe@ndia.org.

Evolve Enterprise Information Environments and Security

Continued innovation in information technology (IT) creates new opportunities for efficiency, security, resilience and assurance. This technology also brings openness and new vulnerabilities to exploitation and attack. The intersection of these trends is where robust dialog is needed between government and industry. Harnessing the power of information through technology to provide an advantage over adversaries while at the same time dramatically improving its ability to protect and defend our information assets will continue to be critical challenge for DoD far into the future.

The cyber domain, unlike other warfighting domains, is driven at the leading-edge of capability by consumers and the private sector, not by DoD (e.g. social media, iPhone, etc.). Cloud computing, agile development, open source software, and emerging platforms such as Google Earth and mobile devices are changing traditional perspectives on information environments.

Secure information sharing with mission/coalition partners, contractors and even non-governmental organizations like the Red Cross is a growing requirement for DoD. In some areas DoD looks to the commercial sector to leverage its technology adoption practices. However, DoD is unique in some very critical ways. Achieving a secure and resilient enterprise information environment requires a consistent framework of standards and architectures acceptable to both government and industry.

Increased emphasis is being placed on eliminating redundant information systems and migrating towards a federated, services-based Global Information Grid (GIG) that serves the entire DoD enterprise and its mission partners. DoD’s evolution towards net-centric operations that incorporate web-based capabilities in a services-based environment entails breaking through difficult barriers and unraveling complex challenges. Not the least of these is overcoming entrenched cultural obstacles that inhibit evolution to more shared environments.

Through its affiliates and divisions NDIA continues to recommend the inclusion of industry as a partner in these efforts to make necessary and significant changes to policies, programs and business practices. NDIA through its affiliate, Association for Enterprise Information (AFEI) recommends the following:

- Invest in expanding commercial capabilities in the cyber domain, with focus on alignment of DoD information environment requirements with capability investments in the private sector. Increased harmonization of global IT investment will reduce the number and size of gaps between government requirements and commercial capabilities that require significant investment to bridge.
- Accelerate the application of federation as an enabling mechanism for achieving interoperability across the defense enterprise. Federation is the only workable model where conditions prevent the application of common solutions across organizations.
- Continue the development of architecture as a tool for capability and investment portfolio management and as a guide for the alignment of capability provisioning across the enterprise. Bolster the training, certification and career path for architecture within the department to provide necessary skills, expertise and experience.
- Strengthen the engagement with industry on developing new and innovative approaches to ensure information, systems and networks are adequately protected from intrusion, disruption, ex-filtration and compromise. Accelerate adoption of federated approaches that are centered on interoperable, standards-based solutions for enterprise capabilities such as identity and privilege management.
- Develop new, innovative approaches to managing organizational and cultural change across the defense community, in partnership with industry, that are necessary to make the DoD net-centric vision and strategy a reality.

The Office of the DoD CIO engaged AFEI to represent industry views on the most significant information environment challenges. AFEI regularly hosts a dialog between industry and government on achieving resiliency, assurance, security and privacy, while simultaneously seeking efficiencies across all enterprise information.

Section 804 of the National Defense Authorization Act for Fiscal Year 2010 (Public Law 111-84) required DoD to develop

and implement a new IT acquisition process for information technology systems. Section 804 also required DoD to report to Congress on the progress of this new process. AFEI conducted a task force study composed of government and industry to make recommendations to DoD regarding its Section 804 response to Congress. AFEI provided DoD its recommendations in June, 2010 and a copy is available at www.afei.org.

The Section 804 requirement for a new IT acquisition process and the re-alignment of IT organizations in the DoD signals major shifts in the traditional view of information systems and processes. AFEI continues to collaborate with DoD on the adoption of enterprise service-oriented architectures and evolving business models.

Increase Funding for Ground Robotics Research, Development and Engineering

Robotics technology has the potential to achieve for warfighters in the next 30 years what information technology has achieved for them in the past thirty. Robots that are agile and autonomous are well-suited for jobs that are dull, dirty, and dangerous. For example, the US Air Force's aircraft with the single most combat hours is a RQ-4A Global Hawk robotic surveillance aircraft. This aircraft can operate for over 24 hours at an altitude of over 65,000 feet—something a human pilot cannot do. Naval applications include undersea mapping and mine detection, communication, surveillance and ship inspection capabilities. Ground based applications include unmanned ground combat vehicles (UGCV), surgical and medical-assistant robots, and robots that autonomously service and repair satellites. The US military is using robots extensively in Iraq to help clear improvised explosive devices (IEDs). Urban combat, sniper location, explosive detection, nuclear, biological, chemical sensing, and service as weapons platforms are additional applications which are either already in use or which provide significant promise for both DoD and the Department of Homeland Security (DHS).

The awakening of the military to the possibilities offered by robotics has resulted in an explosion of potential applications, many of which are currently under development or undergoing experimentation. An efficacious development process will ensure that limited funding is always applied in a manner that will achieve a balance of both near and long term results.

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Issue 5: Support Efficient and Transparent International Access for the U.S. Defense Industrial Base

- **SUPPORT THE ADMINISTRATION'S EXPORT CONTROL REFORM INITIATIVE**
- **IMPROVE DEFENSE TECHNOLOGY TRANSFERS AMONG U.S. PARTNERS AND ALLIES**
- **APPROVAL OF THE U.K. AND AUSTRALIAN DEFENSE TRADE COOPERATION TREATIES**
- **INCREASE CONGRESSIONAL NOTIFICATION THRESHOLD**

Support the Administration's Export Control Reform Initiative

NDIA strongly supports the Administration's initiative to review and reform the outdated U.S. export controls system by moving to a single tiered positive control list, development of single export licensing policies across the tiered list, creation of a single export enforcement coordination center, and implementing a single IT system for all agencies. These changes will help bring greater transparency and coherence to export regulations, enhance the competitiveness of the U.S. defense industry, increase defense exports, improve technology transfer with our allies and coalition partners, and strengthen U.S. national security. The reform of the U.S. export controls must

result in an effective technology control regime for the 21st century which protects critical technologies and safeguards our national security.

While many important and overdue reforms can be accomplished administratively without new legislation, NDIA urges continued close coordination and dialog among all agencies, defense industry and the Congress to ensure that the proposed changes and reforms--particularly the option of a single licensing agency--can be implemented in a way that will protect selected key U.S. technologies while at the same time allowing U.S. industry to be more competitive in the international defense market. In order to avoid any unintended consequences from these changes, there must be an open dialog and a structured approach that incorporates Congressional, regulatory, and business inputs as new approaches to export control are developed.

NDIA will continue to work with the Coalition for Security and Competitiveness (CSC) and a broad cross section of industry associations to bring about a more modern U.S. export control system that is efficient, predictable, and transparent and which contributes to America's broader national security strategy. More information about the CSC can be found at <http://securityandcompetitiveness.org>.

The administration's initiative will help to ensure that export reforms are aligned with our present day security needs and the realities of the global technological environment. Reforms must enable better technology transfer and exchanges with countries that have similar or superior technologies that are needed by U.S. forces. Globalization has changed the international defense industry and the nature of international threats to U.S. national security. The ability to team and partner with companies in friendly and allied nations requires new attitudes and approaches to international cooperation and partnering in the defense sector. Critical to the success of coalition operations is expediting the licensing and transfer of defense articles to our coalition partners, including streamlined DoD contracting procedures.

Export reform will enhance the ability of U.S. companies to export defense articles and services that are available from foreign competitors and help to level the playing field for international defense exports. U.S. firms should not be disadvantaged by unnecessary controls or restrictions not required in order to preserve U.S. national security or protect our key defense technologies. Nor should U.S. firms be denied the ability to export defense articles or technologies that are readily available from foreign competitors offering similar or even superior



equipment and capabilities. The new single control list will help to improve competitiveness of U.S. defense exports while also enhancing the possibility of incorporating foreign technologies and innovations into U.S. products via cooperative R&D and technology transfers that allow true partnering with defense industries in friendly and allied nations.

Improve Defense Technology Transfers Among U.S. Partners and Allies

NDIA recognizes and supports the evolving requirements of coalition operations to attain our national security objectives. Supporting those operations requires well trained and equipped coalition partners employing materiel and tactics that are fully interoperable and supportable in a timely manner during combined exercises and combat operations. Additionally, U.S. forces should have the benefit of being able to leverage advanced technologies developed by friends and allies which may not have originated in the U.S. but which offer near term opportunities as force multipliers. Both of these efforts require the ability to share in the advantages offered by the timely transfer of defense articles and technology among partner and allied nations. Ensuring efficient sharing of defense technologies is critical to winning today's conflicts and ensuring readiness for tomorrow's challenges. Technology sharing, in a controlled and orderly fashion, must be supported and administered in an efficient, predictable and transparent manner. In addition, it is imperative that the DoD contracting process be expedited to operate at the speed of war. The administration's Export Control Reform Initiative, supported by NDIA, should significantly enable improvement in defense technology transfers among our partners and allies.

Approval of the U.K. and Australian Defense Trade Cooperation Treaties

NDIA supports the recent ratification by the U.S. Senate of new treaties to enhance defense cooperation and exports to the United Kingdom and Australia. NDIA believes these new treaties protect our national security and address fundamental problems in our current system of sharing technology with our close allies. NDIA understands these newly ratified treaties will require a separate set of licensing and record-keeping procedures. Therefore, unless there is to be a complete revision of the International Trade and International Traffic in Arms Regulations (ITAR), it is important that implementation of these treaties be accomplished in a manner that enhances and does not degrade or further complicate the existing export administration process.

Increase Congressional Notification Threshold

The FY 2003 Foreign Relations Authorization Act increased modestly the thresholds for Congressional notification of Foreign Military Sales (FMS) and licensed transfers to NATO countries, Japan, Australia, and New Zealand. In a March 2005 legislative request, the administration recommended substantial increases to the arms sales and export notifications thresholds, from \$50M to \$100M and \$14M to \$50M for defense articles, and from \$200M to \$350M for defense services to these countries. NDIA supports these increases which will accelerate the process by reducing the number of Congressional notifications of smaller sales and which will further greater transparency in the Congressional notification process.

National Defense Industry Association Statement of Defense Industry Ethics

Preamble

NDIA Member Companies should adhere to the highest ethical standards and seek to place the defense industry at the forefront of business ethics in America. At a minimum, NDIA members must adhere to applicable laws and regulations governing the conduct of their business. Moreover, entrusted to our care are the lives of Armed Forces Personnel who bear the ultimate risk for their Country to provide security to their fellow citizens. Thus, our common ethical mandate is a higher imperative than our individual business interests. This statement of ethics is intended to capture that mandate by setting forth common ethical principles and emphasizing particular practices that NDIA members may use to put those principles into action.

Mission

NDIA shall serve in a leadership role in setting high ethical standards for the industry and communicating industry efforts in this area to the public and government officials. NDIA will work with its membership to facilitate the practices set forth below.

Common Ethical Principles and Practices for NDIA Membership

NDIA members should aspire to the following ethical principles and make every effort to implement the following practices:

- Advance national security by promoting trust among the Defense Industry, our government customers, the U.S. public and our men and women in uniform.
- Strengthen the integrity of a federal procurement system that encourages competition, rewards technical innovation and ensures that American fighters have the decisive advantage on the battlefield and wherever else our nation's enemies may be found.
- Operate our businesses from a foundation of ethical readiness where economic pursuits do not overtake our responsibility to our soldiers, sailors, marines, and airmen, while acknowledging that America's technological and military preeminence are sustained by promoting the financial health of the defense sector.
- Contribute to the common good of our industry and promote industry ethics whenever and wherever possible by sharing best practices in ethics and business conduct among NDIA members and including ethics training in NDIA sponsored events.
- Implement effective ethics programs for company activities at home or abroad. When contemplating any international sale to a governmental or quasi-governmental buyer, it is imperative that effective measures be undertaken to ensure full compliance, not only with the letter, but also the spirit of the Foreign Corrupt Practices Act, as amended, and the FCPA's bar against improper payments to foreign officials.

- Establish effective mechanisms of control over employees and agents operating overseas to promote ethical conduct based upon principles, not geographic location.
- Protect U.S. national security when performing contracts with foreign parties by committing to compliance with U.S. export control licensing regimes, and with all anti-boycott and embargo requirements.
- Establish corporate integrity as a business asset, rather than a requirement to satisfy regulators, by making ethics integral to all aspects of corporate life and culture to create an environment where employees aspire to do the right thing.
- Recognize that self-governance is key to management's commitment to abide by ethical standards. Accordingly, charge Corporate Boards with responsibility for creating an environment where ethical conduct is the order of the day, including developing and implementing a corporate-level process or procedure to review company best practices, policies, and procedures governing ethics.
- Demonstrate the Company's and its leadership's commitment to ethics by making the Chief Executive the top ethics officer.
- Implement a formal company ethics program that includes a written code of conduct to communicate institutional values and expectations and guide employees and management in their decisions and conduct.
- Organize training programs as an integral component of company ethics programs to commit employees to the Company's written code of conduct, encourage them to discern the difference between right and wrong, and to act on that knowledge despite pressures to compromise standards.
- Establish and communicate procedures for employees to identify and report suspected violations of the code of ethics without fear of retribution, establish mechanisms to promptly and effectively communicate violations to the government, and promote full cooperation with government investigations.
- Ensure that employee reports of ethics violations receive immediate and objective attention from Company leadership by establishing a reporting system that promptly, within twenty-four (24) hours, informs the Chief Executive or his designee of any allegation that raises ethical implications.
- Establish written remedial measures for prompt and appropriate corrective action, including disciplinary measures, where instances of unethical conduct are discovered.

Vision

America's leading Defense Industry association promoting National Security

Mission

ADVOCATE: Cutting-edge technology and superior weapons, equipment, training, and support for the war-fighter and first responder

PROMOTE: A vigorous, responsive, government – industry national security team

PROVIDE: An ethical forum for exchange of information between industry and government on national security issues

Motto

Strength through industry and technology

Ms. Mary Ann Gilleece
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