July 13-19, 1998
Defense News

Reforms Need Reforming: Commercial Acquisition Fails To Cure Overpricing

"Inside View" op-ed by Marcus Corbin

In the 1980s, the toilet seats, coffee pots and other examples of gross overcharging by defense contractors led to reforms designed to improve government oversight. In reaction to these reforms, the defense industry counterattacked, successfully pushing the White House and Congress to change the rules again.

By widely expanding the definition of commercial purchases, which are exempt from many of the normal contracting protections, the new rules allow contractors simply to bypass a lot of the tougher regulations from the 1980s. But as a result of the new rules, we have seen new cases of gross overcharging, such as the $76 screw recently discovered by the Defense Department's inspector general.

In contrast, there has been precious little solid evidence of the billions of dollars of claimed savings that were touted in the Defense Department Acquisition Reform Week ceremonies in May.

In a sophisticated response to the overcharging scandal, the Department has acknowledged the errors, but alleges they are anomalies. This sleight of hand may deflect attention from the deeper problems exposed by the overcharging cases, and limit examination of whether the changes went too far.

Buying more products as commercial items is a great idea when the products really are commercial and there is a competitive free market from which to buy them. Stretching the concept to include C-130J military transport aircraft, to cite one case, is a terrible idea.

If no reliable market is available, the reforms make the government vulnerable to bilking. Jacques Gansler, undersecretary of defense for acquisition and technology, claims the procurement changes have indeed produced large savings for the government overall. Yet this remains to be demonstrated with hard figures.

To the contrary, Eleanor Hill, defense inspector general, testified March 18 to the Senate Armed Services acquisition and technology subcommittee that her office has "not been shown or found data from which overall conclusions can be reliably developed" on the savings or success of the latest procurement reforms.

Hill stated that there is a "lack of good management information on the overall experience to date in buying commercial items" and said one Defense Department study claiming even modest savings was completely unsupportable.

The Federal Acquisition Streamlining Act of 1994 and the even more radical Federal Acquisition Reform Act of 1996 brought on the overpricing cases investigated by the inspector general, under the mantle of procurement reform, although the reforms were pursued by contractors.

These laws, in harmony with the deregulation doctrine of the administration's National Performance Review and its Reinventing Government campaign, stretched the definition of commercial beyond any sensible limit. By March, the inspector general's office confirmed that its investigations had revealed cases of extreme overcharging for so-called commercial items.

Under the new practices, for example, contractors charged $76 for 57¢ screws, they inflated prices by more than 1,000 percent on a variety of parts, and billed the government $6.1 million for spare parts that were worth $1.6 million.

Following hearings, Congress has attempted to deal with the difficulties through legislation in the 1999 defense authorization bill. Unfortunately, the language does not address the central problem: The law allows items to be called commercial that do not have prices set by the normal free market. The problem is clear, and the fix should be straightforward - tighten up the excessively loose definition of commercial items.

The cases investigated by the inspector general reveal a paradox that says a lot about the source of the problem: The government was negotiating commercial prices. Why would the government have to negotiate a price when the price is supposedly set by commercial markets? The useful kernel behind the 1994 and 1996 legislative changes was to ease purchases of simple, true commercial items whose prices are fixed by the free market - off-the-shelf items like the ashtray Vice President Gore smashed on David Letterman's show.

If the government does have to negotiate, the new rules hamstring it by making contracting officials negotiate in the dark. Under commercial item rules, contractors are not required to show certified cost data. This explains how the Defense Department has overpaid even for simple items like screws.

Declaring one of the overpricing problems discovered by the inspector general solved, the Department boasted about how it re-negotiated a new contract with prices below the offending contractor's catalog prices. Apparently the Pentagon does not realize catalog prices reflect true market prices as faithfully as sticker prices on a new car.

Proof of the promised savings from procurement reforms has yet to materialize, but we do have concrete cases of gross extortion of the government purse under the guise of commercial pricing.

In the name of deregulation, contracting supervision has been changed from oversight into undersight. Rather than continue to distort the meaning of commercial and the free market, we should be more sure that we are indeed saving the government money with reforms, rather than exposing the government to new forms of overpricing.

© The Project On Government Oversight 2004
updated:Thursday, February 12, 2004