

Lockheed Martin Comments and Recommendations

Defense Acquisition Regulations System Public Meeting On Weapon Systems Acquisition Reform Act Organizational Conflicts of Interest Requirements

December 8, 2009

Lockheed Martin is pleased to participate in this industry-Government dialogue. We commend DOD for seeking industry perspectives on the impact of the 2009 Weapon Systems Acquisition Reform Act (WSARA) on DOD contracting, in particular, Section 207 of that Act that directs the Department to review and tighten rules and regulations regarding organizational conflicts of interest (OCI).

In the November 9 Federal Register Notice announcing today's session, DOD invited industry to focus on three areas of potential impacts on DOD contracting relating to OCI. In our comments today, we will focus primarily on the second of those areas, providing recommendations for specific policies, practices, and structural solutions for effective mitigation of OCI concerns that may arise regarding ownership of business units that perform systems engineering and other support services on major defense acquisition programs (MDAPs) in relation to the business units that compete to perform as supplier for the program; we will also suggest certain activities in the Government acquisition process for which OCI mitigation may not be appropriate. Finally, we will comment briefly on the third area, regarding the award of major subsystem contracts by the prime contractor to affiliated business units on MDAPs, and providing technical evaluations on MDAPs.

OCI Concerns regarding Business Unit Ownership Relationships

Concern with OCI in Government contracting has increased in recent years primarily due to consolidation of companies within the defense industry resulting in fewer companies with the technical expertise needed by the Government; significant reductions in the Government workforce with required "in-house" technical expertise; and the increasing complexity of weapon systems, command and control systems, information systems, and other Government management and services systems that must interface seamlessly with each other to accomplish missions. These complex systems demand the highest degree of technical expertise for integration into systems of systems for maximum operational effectiveness. Not only is this essential to the warfighter, but it is also essential to the efficient use of taxpayer resources in procuring goods and services across the Government.

Government contractors, especially those with experience in MDAPs, possess significant technical expertise and technological capabilities and facilities. The Government should have access to this expertise, if the work can be accomplished in an unbiased and impartial manner and these contractors are not given an unfair competitive advantage. Part 9.5 of the Federal Acquisition Regulation (FAR) provides general parameters for the resolution of OCI issues. Recently, however, isolated OCI violations and inadequate OCI mitigation measures have cast some doubt on the ability of Government and industry to effectively mitigate OCI concerns.

The FAR gives the responsibility for resolving OCI and determining a contractor's eligibility to compete for OCI-sensitive work to the contracting officer. Several DOD components and other Government agencies have developed organization-wide policies that reject OCI mitigation and require disqualification of a contractor from competing for potentially OCI-sensitive work. In addition, in some instances, even when an OCI mitigation plan is approved by the contracting officer, the contractor is rated negatively in the evaluation process on OCI grounds. In other instances, later development work is

denied on the basis of its relationship to previous OCI-sensitive work, even if an OCI mitigation plan for that work was approved by the contracting officer and the contractor complied with the terms of that plan.

The potential unintended consequences of an overly cautious approach to OCI must be considered in formulating a DOD-wide or Government-wide policy. The people, processes, tools, infrastructure, and culture of development contractors combine to create technical expertise through cross-training of personnel between systems engineering and major development efforts over the life of an employee's career. If such development contractors are precluded from competing for certain contracts due to a blanket policy of OCI avoidance, a significant element of systems engineering and technical expertise will become unavailable to the Government, because large development contractors will opt to maintain eligibility for development work rather than choose to work only on the systems engineering foundation.

In addition, requiring development contractors to divest a portion of their business to resolve OCI concerns will not be effective in ensuring that expertise remains available to the Government. It is not just a matter of transferring people to non-conflicted companies, because many seasoned employees may choose not to leave the employ of the development contractor if that contractor offers broader career opportunities or other advantages. Further, it is difficult to transfer effectively to a new entity the processes, tools, infrastructure and culture that create the needed expertise. Segregating systems engineering from development engineering will also, over time, eliminate the benefits of broad cross-training, resulting in a dilution of expertise available to the Government to solve complex system of systems issues. Companies with a narrower technical focus do not offer the Government the same breadth of experience in solving complex problems. In short, failure to formulate a Government-wide policy that recognizes the feasibility and advisability of effective mitigation of OCI concerns would create a significant limitation on competition for Government systems engineering work and, more importantly, would put at risk the future success of complex development programs that may lack a highly sophisticated systems engineering foundation due to the unavailability of that expertise to the Government.

To ensure a rigorous and effective OCI mitigation process, we make several recommendations for development of a clear DOD-wide policy that reflects the desirability and necessity of utilizing the vast amount of technical and systems engineering and integration expertise of its Government contractors, while ensuring effective mitigation of OCI. With this updated policy guidance and revised regulations, the Government will be able to continue to take advantage of the significant technical expertise that major defense contractors have to offer -- expertise that has been developed over many years of highly sophisticated, state-of-the-art technical work.

Our recommendations address mitigation in two broad areas of potential organizational conflict: "unequal access to information" which might otherwise give a contractor an unfair competitive advantage, and possible perceptions of "biased ground rules and impaired objectivity".

Unequal Access to Information

Mitigation of OCI, in many cases, can be viewed most basically as a restriction in the flow of information to those to whom the Government does not want to disclose this information. It is very similar to controlling the flow of classified and other sensitive information, such as export-controlled information. Government contractors, particularly those dealing with DOD and the intelligence community, have decades of successful experience with effectively compartmentalizing information within their organizations and strictly complying with information security laws and regulations.

The GAO and Federal Courts have ruled on many "unequal access to information" OCI issues and consistently found that if the Government carefully considers the OCI, documents its findings, and

requires contractors to take appropriate OCI mitigation steps, OCI mitigation plans with “firewalls” and other measures are effective in mitigating these types of OCIs.

Recommendations. The Government should implement policies that promote competition and permit continued access to the extensive expertise of integrated defense contractors while ensuring effective mitigation of OCI. Specifically, we recommend that the FAR and DFARS be revised as follows to address concerns regarding unequal access to information:

- Include a menu (see Chart 1 below) of acceptable OCI mitigation processes and procedures. Authorize contracting officers to select from that menu a combination of appropriate mitigation measures tailored to the specific circumstances of each acquisition.
- Require that competing contractors with acceptable OCI mitigation plans be evaluated on an equal basis with contractors having no OCI issues.
- Require that the contracting officer for a related developmental contract be bound by previous approval of an OCI mitigation plan and not be permitted to disqualify or evaluate negatively a contractor so long as the contractor complies with the OCI mitigation requirements in its support contract, and the OCI remains unchanged.
- Create a procedure to support voluntary contractor requests for a review and certification by the senior acquisition executive of a Department or Agency of its historical OCI mitigation compliance, and such certification would require the contractor to be considered “non-conflicted” for purposes of future competitive source selection evaluations; the “past performance” compliance certification would be required to be renewed on a periodic basis.

CHART 1 – Options for Mitigating “Unequal Access to Information” OCI Concerns

<i>Organizational Segregation</i>	Performing organization is segregated from affiliated organizations.
<i>Physical Segregation</i>	Buildings and/or rooms are identified specifically as OCI Restricted Work Areas and are secured with access control devices.
<i>Employee Access</i>	Employees’ access to OCI Restricted Work Areas is granted only upon completion of initial OCI training and execution of a Non-Disclosure Agreement (NDA).
<i>Computer Security</i>	Network account access approval is required by OCI manager prior to account set-up. Performing organization information storage servers are separate from affiliated organization servers.
<i>Information Protection</i>	OCI- sensitive information is clearly marked and controlled with limited (“need to know”) access, password protected softcopy storage folders, registered locking files for hardcopy storage, and access rosters and logs.
<i>Training</i>	Personnel are required to complete mandatory annual OCI training. Failure to re-train results in access termination.
<i>OCI NDA</i>	All employees and subcontractors must sign a standard NDA and acknowledge OCI compliance rules.
<i>Employee Transfer Restrictions</i>	Employees are not permitted to transfer to any position in affiliated organizations that could create a conflict. Every personnel transfer from an OCI sensitive program is reviewed prior to approval. Any exception requires Government approval.
<i>Subcontractor Flow-down</i>	All OCI mitigation requirements are flowed down to subcontractors, and prime contractor reserves the right to audit subcontractor compliance, as appropriate.
<i>Audit</i>	OCI audits are conducted annually, and an audit report is provided to the Government.
<i>Certification</i>	Performing and affiliated organizations sign an annual OCI compliance certification that is provided to the Government to certify full OCI mitigation compliance for the previous year.
<i>Corporate Policy</i>	Formal ethics and OCI mitigation policies are enforced at performing and affiliated organizations to ensure full compliance.

Biased Ground Rules and Impaired Objectivity

The GAO and Federal Courts have ruled consistently that firewalls alone are insufficient to mitigate “biased ground rules and impaired objectivity” OCI issues. Therefore, we recommend additional measures that will be effective in mitigating bias and impaired objectivity OCI. As with OCI concerns regarding unequal access to information, the Government should implement policies that promote competition and permit continued access to the extensive expertise of Government contractors while ensuring strict and effective mitigation of OCI concerns regarding bias and impaired objectivity.

Recommendations. We recommend that the menu of acceptable OCI mitigation processes and procedures in Chart 1 be augmented by the items listed in Chart 2 below to specifically address concerns regarding bias and impaired objectivity. An OCI mitigation plan utilizing any or all of these additional options would result in the contractor being considered “non-conflicted” for purposes of source selection evaluation, and the contractor’s compliance with the OCI mitigation plan would preclude a contracting officer on a related development program from disqualifying the contractor on OCI grounds.

CHART 2 – Options for Mitigating “Biased Ground Rules and Impaired Objectivity” OCI Issues

<i>Multi-contractor IPTs</i>	Established independent product teams (IPTs) which serve to avoid or neutralize bias OCI issues.
<i>Assignment of Work to Non-Conflicted Subcontractor</i>	Additional levels of mitigation are applied to particularly OCI sensitive tasks, which may be assigned to a non-conflicted subcontractor to provide OCI avoidance from the prime contractor.
<i>Performance Review</i>	A review panel composed of contractors, Government, and/or FFRDC personnel is charged with responsibility to review work product for potential bias OCI issues.
<i>OCI Working Group</i>	OCI sensitive programs are reviewed on a regular basis by an integrated panel to ensure no OCI situations are created through addition of new work or changes in the program office acquisition environment.
<i>Performance Objectives</i>	Performance objectives for specific leaders in the performing and parent organizations include effective OCI mitigation.

In addition, multiple-award indefinite delivery/indefinite quantity (ID/IQ) contracts must permit awardees to decline to respond to task order solicitations if the work presents a bias or impaired objectivity OCI that cannot be mitigated by the contractor.

For particularly sensitive OCI situations involving bias and impaired objectivity, where none of the practices and procedures outlined above in Charts 1 and 2 are considered sufficiently stringent to mitigate OCI concerns, the Government should adopt a policy that allows a Department or Agency to approve organizational barriers to prevent influence by the prime contractor.

Such an approach – which we term a Special Independence Agreement (SIA) – would allow the establishment of barriers around an entity engaged in work that could potentially raise concerns about bias and impaired objectivity. As described in the recommendations below, the SIA structurally isolates the entity from its parent and affiliated organizations, utilizing a selected subset of the provisions generally available under the regulations governing foreign-owned and controlled firms that would be appropriate and necessary to mitigate concerns about influence by a parent or affiliated organization on that entity. (Note: This proposal was the basis of the OCI “structural remedies” mitigation technique that was included in the Senate-passed version of the WSARA, but was not included in the final bill because the conferees expressly gave DOD the discretion to review the concept and directed that it be considered when issuing regulations to implement Section 207.) In particular, removing any ties between the compensation of the entity’s employees and the financial performance of the parent and affiliated organizations would eliminate concerns that compensation creates a bias in favor of the parent or

affiliated organizations. The new entity operating under the SIA would have its own compensation programs that focus solely on performance of the entity, not the parent or affiliated organizations. This separation of compensation structures would ensure that employees performing OCI-sensitive work do not have economic incentives to favor the parent or affiliated organizations. We also believe provisions such as establishing a separate board of directors, with one or more independent directors and an OCI compliance committee, would be appropriate to make an entity operating under an SIA effective at mitigating OCI concerns.

Utilization of the SIA option described in Chart 3 would be limited to the most sensitive situations; the options in Charts 1 and 2 should be sufficient to mitigate OCI concerns in the majority of circumstances.

Recommendations. To mitigate the most significant cases of potential bias and impaired objectivity concerns, we recommend additional revisions to the FAR and DFARS to authorize the Government to approve an SIA that isolates a portion of a contractor’s business for OCI mitigation purposes. The elements of the SIA are outlined in Chart 3 below.

CHART 3 – Establishment of an Entity under an SIA

<i>Separate Legal Entity</i>	Transfer OCI-sensitive work to a separate legal entity subject to the oversight of a board of directors with at least one member with no prior relationship to the parent or affiliated organizations.
<i>Compliance Committee of the Board</i>	Require oversight of all OCI compliance matters by a Board-level committee, chaired by the independent director with veto power over any OCI compliance decision.
<i>Compliance Officer</i>	Appoint a Compliance Officer responsible for ensuring OCI compliance who reports directly to the Board-level compliance committee.
<i>Separate Incentive Compensation Structures</i>	Prohibit employees of the entity from participating in incentive compensation plans tied to the performance of the parent or affiliated organizations, specifically, bonuses, profit-sharing, and stock or stock options.
<i>Audit</i>	Require periodic audit and certification of compliance with the terms of the SIA, under the oversight of the Compliance Officer.

If the Government directs the use of an entity under an SIA as a condition of competing for a Government contract, that direction must be approved by the Department or Agency senior acquisition executive. However, a contractor could request review and approval by the senior acquisition executive of an SIA, and if approved, the contractor would be permitted to compete for contracts with that agency and be considered “non-conflicted” for OCI purposes for the duration of the SIA. Such Government approval of an entity under an SIA as a “non-conflicted” contractor in one Department or Agency should be considered an approved SIA for all Government contracting work.

The SIA option would be available for situations where a prime contractor has the ability to control another entity performing OCI-sensitive work. In circumstances where the prime contractor owns less than 50 percent of the outstanding equity of the entity performing the OCI work, the prime contractor would not have the ability to control the OCI entity, and thus, use of the SIA to negate control would be unnecessary. We believe the simple fact of a prime contractor’s minority ownership of an entity performing OCI-sensitive work should not, in and of itself, raise OCI concerns; however, if necessary, such concerns would be effectively mitigated by utilizing some or all of the options available in Charts 1 and 2.

Finally, in any instance where OCI concerns are raised, whether unequal access to information or biased ground rules and impaired objectivity, a contractor may only be disqualified from competing in response to a solicitation if all of the practices, procedures, and organizational barriers outlined above have been

considered and rejected by a contracting officer as insufficient to mitigate OCI concerns, and that disqualification decision has been approved by the senior acquisition executive of the Department or Agency.

OCI Avoidance

We believe there are certain activities that require strict OCI avoidance. OCI concerns with respect to the following acquisition support tasks cannot be mitigated by a prime contractor, and thus a contractor should be precluded from participating in the related competitive solicitation.

- Preparing a work statement to be used in competitively acquiring a system or services;
- Providing material leading directly, predictably, and without delay to such a work statement;
- Assisting in source selection evaluations; or
- Providing technical evaluation of proposals.

In addition, multiple-award ID/IQ contracts must permit awardees to decline to respond to task order solicitations that could create OCI concerns related specifically to the acquisition support tasks listed above.

Award of Major Subsystems to Affiliated Business Units

The DFARS revision required by WSARA must address OCI that could arise as a result of “award of major subsystem contracts by the prime contractor for a major defense acquisition program to affiliated business units for software integration or development of proprietary software system architecture.” Contractors must be given the right to select the best source for software integration or development of the software system architecture. The FAR recognizes that the prime contractor is responsible for managing contract performance, including planning, placing, and administering subcontracts as necessary to ensure the lowest overall cost and technical risk to the Government. The Government is advocating shifting additional risk to contractors by increasing the use of fixed-price contracts. Because the prime contractor is responsible for overall performance, including the performance of its subcontractors, the prime contractor must be given the opportunity to select its subcontractors, particularly in critical areas such as software development and integration. The FAR permits Government review and approval of make-or-buy plans and consent to subcontracts in limited circumstances. The current policies balance appropriately contractor responsibility for performance with Government oversight.

Section 202 of WSARA imposes requirements in statute that require contractors to provide “full and fair” consideration to qualified sources for the development or construction of major subsystems and components of major weapon systems. For major defense contractors, this is not a new policy. Lockheed Martin’s “make or buy” policy, embodied in a corporate policy statement, already states that “our business units will not be advantaged or disadvantaged as a result of make or buy decisions, and all potential suppliers will have the opportunity to be fairly selected.”

Recommendations. Implementation of WSARA section 202 should provide sufficient safeguards for the Government. We do not believe that additional DFARS coverage in response to subsection 207(b)(1)(C) is needed. Lockheed Martin already provides “full and fair consideration” to qualified sources. Any Government oversight imposed in response to subsection 202(c)(2) should be unobtrusive and recognize the contractor’s responsibility for contract performance.

Providing Technical Evaluations on MDAPs

The DFARS revision required by WSARA also must address OCI that could arise as a result of providing technical evaluations on major defense acquisition programs. The term “technical evaluations” is encompassed by the existing FAR definition of systems engineering and technical assistance (SETA), which states:

“Systems engineering includes a combination of substantially all of the following activities: determining specifications, identifying and resolving interface problems, developing test requirements, evaluating test data, and supervising design.”

The FAR addresses OCI mitigation strategies for SETA work. The implementation of WSARA subsections 207(b)(3) and (4) for SETA work will apply to providing technical evaluations on MDAPs.

Recommendation. The OCI mitigation processes and procedures outlined in Charts 1 and 2 above should apply to SETA work, including technical evaluations.

Summary

Creating a Government-wide, structured approach to mitigating OCI in the FAR and DFARS, as suggested above, will provide contracting officers with the tools necessary to address OCI issues in a more consistent and effective manner. This approach will also provide contractors with a more predictable OCI environment in which to make investments and decisions whether to pursue a business opportunity. Finally, this approach will result in increased competition and allow the Government to capitalize on its investment in technology and technical expertise which resides in large multifaceted contractors, while protecting the integrity of the acquisition process.

We recognize the Government’s OCI concerns. This issue deserves the best efforts of all interested parties to resolve in a manner that serves the best interests of the Government and the taxpayer.