OFFICE OF THE SECRETARY OF WAR
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WASHINGTON, DC 20301-1000

MEMORANDUM FOR: SEE DISTRIBUTION

SUBJECT: Efficiency Assurance for Fixed-Price Contracts and Other Transactions

A secure, agile, and technologically superior industrial base is essential to safeguarding our nation and delivering capabilities to the warfighter. Fulfilling modern defense imperatives demands close alignment between the acquisition strategy (including the contracting strategy), financial stewardship, and industry partnership. In furtherance of the memoranda on "Fostering One Strong Industrial Base," from the Deputy Secretary of War dated September 14, 2026, and the Under Secretary of War for Acquisition and Sustainment on October 14, 2026, this posture statement reflects our joint commitment to encouraging private-sector innovation, rewarding enterprise productivity gains, and honoring our foundational obligation to manage public resources with integrity and discipline.

Efficiency Retention on Risk-Based Awards

In fixed-price contracts, fixed-price incentive arrangements, and Other Transaction Agreements, industry partners assume performance, technological, and cost risks. Sound stewardship recognizes that when industry invests internal capital, modernizes workflows, adopts sound commercial practices, and achieves manufacturing efficiencies, both national security and the taxpayer directly benefit.

Where a fair and reasonable negotiated price is established, whether through robust market competition, commercial price analysis, or cost evaluation, industry is motivated to maximize efficiency in performance. Their financial benefits, resulting from ingenuity and operational discipline, are rightfully retained by industry. Realized margin achieved through superior execution, productivity gains, or private investment represents the intended outcome of risk-based contracting and is not, by itself, an indicator of waste.

While efficiency retention serves as a foundational principle for risk-based, fixed-price awards, it does not preclude the use of alternative incentive structures. For fixed-price incentive (firm target) contracts, the Department negotiates share lines and industry retains their pre-negotiated share of the cost savings. For certain contractual arrangements, such as long-term sole-source production programs, acquisition teams are encouraged to consider tailored mechanisms, including tiered profit-sharing models, to align long-term incentives and ensure mutual benefit from realized efficiencies.

Prospective Capture of Efficiencies for Long-Term Affordability

The Department will determine how prior efficiencies should inform the price for future procurements such as follow-on production lots. When negotiating follow-on

efforts, acquisition and financial teams will account for learning curves and other efficiencies while also incentivizing industry to continue to pursue innovation.

Enforcement Priorities

This posture statement will inform the Department's enforcement priorities. It does not supersede law, alter any authority vested by statute, limit or direct the specific findings or conclusions of any audit, or diminish the Department's resolve to combat fraud, waste, and abuse under the False Claims Act (31 U.S.C. § 3729, *et seq*.) and related federal procurement integrity statutes. Furthermore, it does not waive statutory remedies for defective pricing under 10 U.S.C. Chapter 271 when certified cost or pricing data is required by law, price adjustments where Cost Accounting Standards apply, or the final indirect-cost rate settlements and incurred-cost audits required for cost-reimbursement work where the Department shares financial exposure.

Modernized Profit Policy

These precepts will be reflected in the Department's forthcoming profit modernization initiative, as outlined in the October 1, 2026, Principal Director, Defense Pricing, Contracting, and Acquisition Policy (DPCAP) memorandum, "Implementation of Supplier Cost and Pricing Transparency."

Please direct any questions regarding this memorandum to the Price, Cost and Finance directorate within DPCAP at osd.pentagon.ousd-a-s.mbx.dpc-pcf@mail.mil.

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John M. Tenaglia
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Office of the Under Secretary of War for Acquisition and Sustainment

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Jennifer L. Desautel
Director, Defense Contract Audit Agency
Office of the Under Secretary of War (Comptroller)

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