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February 2021

FIXED-PRICE-INCENTIVE CONTRACTS

DOD Has Increased Their Use but Should Assess Contributions to Outcomes

GAO@100

A Century of Non-Partisan Fact-Based Work

GAO-21-181

GAO@100 Highlights

Highlights of GAO-21-181, a report to congressional committees

February 2021

FIXED-PRICE-INCENTIVE CONTRACTS

DOD Has Increased Their Use but Should Assess Contributions to Outcomes

Why GAO Did This Study

DOD spends billions of dollars annually using fixed-price type contracts to acquire its MDAPs, among other things. In 2010, DOD's Better Buying Power guidance encouraged the use of FPI contracts as a way to obtain greater efficiency and productivity in defense spending.

Congress included a provision in statute for GAO to report on DOD's use of fixed-price type contracts, including FPI. This report examines (1) the extent to which DOD has awarded FPI contracts associated with MDAPs from fiscal years 2010 through 2019, and (2) the factors that influenced DOD's decision to use FPI contracts and the extent to which DOD assesses their use, among other objectives.

GAO analyzed government contracting data by contract type for fiscal years 2010 through 2019 on contracts for 101 MDAPs. GAO further analyzed a non-generalizable sample of 12 contracts including six FPI and six firm-fixed-price (two of each type from each of the three military departments); conducted file reviews; reviewed policy documentation; and interviewed DOD officials.

What GAO Recommends

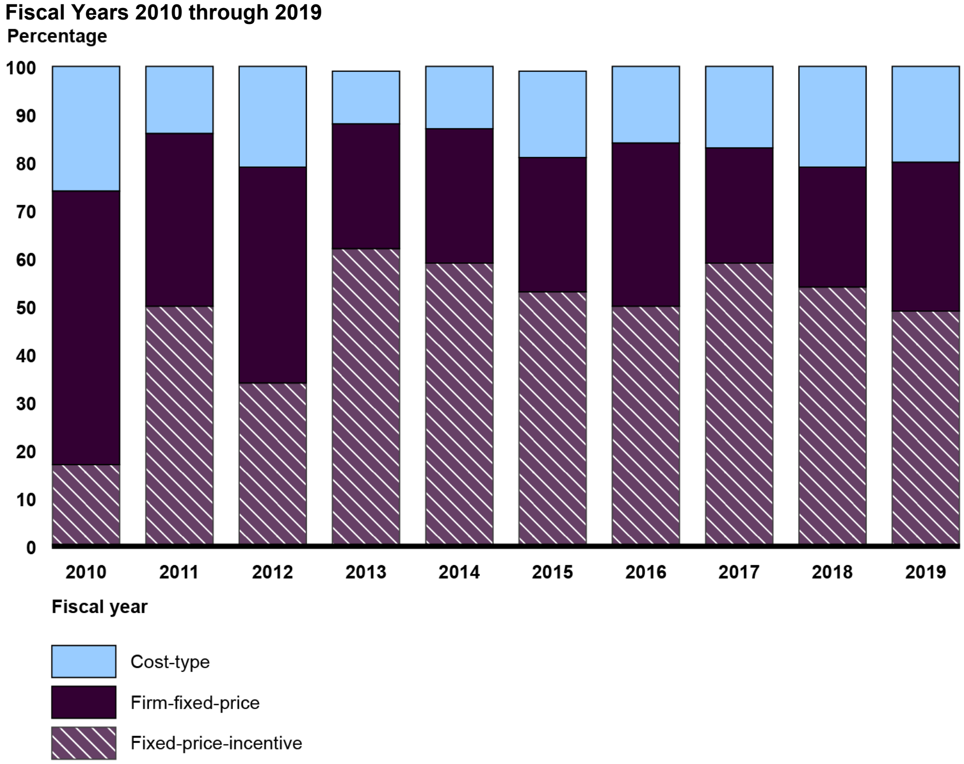
GAO recommends that DOD conduct an assessment of its use of FPI contracts for major defense acquisition programs, including the extent to which share lines and other contract elements contributed to achieving desired cost and schedule performance outcomes. DOD agreed with GAO's recommendation.

View GAO-21-181. For more information, contact W. William Russell at (202) 512-4841 or russellw@gao.gov.

What GAO Found

The Department of Defense (DOD) has encouraged the use of fixed-price-incentive (FPI) contracts where appropriate. These contracts can provide defense contractors with a profit incentive for effective cost control and performance depending on how they are structured. Over the 10-year period from fiscal years 2010 through 2019, obligations on FPI contracts for major defense acquisition programs (MDAPs) grew to account for almost half of the $65 billion in obligations for fiscal year 2019.

Percentage of Obligations by Contract Type for Major Defense Acquisition Programs from Fiscal Years 2010 through 2019



Source: GAO analysis of Federal Procurement Data System – Next Generation data. | GAO-21-181

DOD guidance, including Better Buying Power initiatives, influenced DOD's use of FPI contracts over the last decade for the selected contracts GAO reviewed. In addition, when selecting a contract type, contracting officers also considered factors including the availability of cost or pricing data, previous experience with the contractor, and the previously used contract type. DOD has not assessed the extent to which use of FPI contracts has contributed to achieving desired cost and schedule performance outcomes.

Contents

Abbreviations

DAMIR	Defense Acquisition Management Information Retrieval
DCMA	Defense Contract Management Agency
DFARS	Defense Federal Acquisition Regulation Supplement
DOD	Department of Defense
FAR	Federal Acquisition Regulation
FFP	firm-fixed-price
FPDS-NG	Federal Procurement Data System-Next Generation
FPI	fixed-price-incentive
MDAP	Major Defense Acquisition Program
MOCAS	Mechanization of Contract Administration Services
NDAA	National Defense Authorization Act

U.S. GOVERNMENT ACCOUNTABILITY OFFICE
A Century of Non-Partisan Fact-Based Work
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Congressional Committees

The Department of Defense (DOD) spends billions of dollars annually using fixed-price-type contracts to acquire its major defense acquisition programs (MDAPs)—including aircraft, ground vehicles, missiles, ships, and satellites. In 2010, DOD's Better Buying Power initiative encouraged the use of fixed-price-incentive (FPI) contracts, particularly for efforts moving from development to production, as a way to obtain greater efficiency and productivity in defense spending. These contracts can provide defense contractors with a profit incentive for effective cost control and performance, depending on how they are structured. The other major contract type, cost-reimbursement contracts, generally provide less incentive for cost control as the government pays the contractor's allowable costs incurred, to the extent prescribed by the contract. The selection of contract type may also affect the contract closeout process since the amount of information required to close out a contract varies by contract type.

Section 807(b) of the National Defense Authorization Act (NDAA) for Fiscal Year 2020 included a provision for us to report on DOD's use of fixed-price-type contracts, including FPI.[1] This report examines (1) the extent to which DOD has awarded FPI contracts associated with MDAPs from fiscal years 2010 through 2019, (2) the factors that influenced DOD's decision to use FPI contracts and the extent to which DOD has assessed their use, and (3) the extent to which DOD has faced challenges in closing out fixed-price-type contracts. This report also contains information on DOD's use of fixed-price contracts in general.

To examine the extent to which DOD awarded FPI contracts, we identified a population of 374 contracts associated with Acquisition Category I MDAPs awarded from fiscal years 2010 through 2019 and reported in DOD's Defense Acquisition Management Information

[1]Pub L. No. 116-92, § 807(b) (2019).

Retrieval (DAMIR) system.[2] This population included firm-fixed-price (FFP), FPI, and combination contracts and excluded contracts with values below $40 million.[3] Next, we analyzed Federal Procurement Data System-Next Generation (FPDS-NG) data on obligations by contract type for the contract population. We assessed data reliability for the contract population by comparing the contract types identified in FPDS-NG for each contract with information on contract types contained in DAMIR, and determined the DAMIR and FPDS-NG data were sufficiently reliable for the purposes of analyzing the extent of DOD's use of fixed-price-type contracts for MDAPs.

To determine the factors that influenced DOD's decision to use FPI contracts and the extent to which DOD has assessed their use, we selected a stratified, non-generalizable sample of 12 contracts from the 374 contracts identified from Acquisition Category I programs for in-depth review, including two FFP contracts and two FPI contracts from each of the three military departments.[4] Specifically, we reviewed six FPI contracts—two from each of the three military departments. We also reviewed six FFP contracts—two from each of the military departments—to understand factors that influenced the use of fixed-price contracts more broadly. For the 12 selected contracts, we analyzed documentation including acquisition strategies and additional documentation stating the rationale for contract type. Further, for FPI contracts, we analyzed the structure and elements negotiated prior to award, which included the formula used to adjust earned profit known as the share line, the agreed

[2]In general, MDAPs are designated programs that, among other things, meet or exceed Acquisition Category I thresholds, which are $525 million in research, development, test, and evaluation, or $3.065 billion in procurement in fiscal year 2020 constant dollars. Department of Defense Instruction No. 5000.02, *Operation of the Adaptive Acquisition Framework* (Jan. 23, 2020); Department of Defense Instruction No. 5000.85, *Major Capability Acquisition* (Aug. 6, 2020).

[3]"Combination contracts," which may be called "hybrid contracts" at some agencies, contain two or more contract types in their line items, such as cost-reimbursement and firm-fixed-price. Under a cost reimbursement contract, the government agrees to pay the contractor's allowable incurred costs to the extent prescribed in the contract. The contract establishes a ceiling that the contractor may not exceed (except at their own risk) without the approval of the contracting officer. FAR § 16.301-1. Under a firm-fixed-price contract, the price is not subject to any adjustment on the basis of the contractor's cost experience in performing the contract. FAR § 16.202-1. It may be beneficial for the government to use a variety of contract types in the same contract, depending on the circumstances.

[4]We did not include jointly-managed and Missile Defense Agency-managed MDAPs in our sample set of 12 contracts. Those programs included the F-35 and the Ballistic Missile Defense System.

upon target cost, and the ceiling price. We also reviewed relevant contracting regulations and DOD guidance, including the Better Buying Power initiatives. Finally, to obtain additional context on the use of fixed-price-type contracts, we conducted interviews with the cognizant commands and contracting officers responsible for the selected contracts as well as officials from the Defense Contract Management Agency (DCMA), the Defense Acquisition University, and the Office of the Secretary of Defense's Defense Pricing and Contracting Directorate. To assess the extent to which DOD had evaluated the results of the use of FPI contracts we interviewed DOD officials, including those from each military service, and requested information on any analysis completed in this area since 2010. We compared this information to federal internal control standards related to defining objectives and assessing performance toward achieving those objectives.[5]

To determine the extent to which DOD has faced challenges in closing out fixed-price-type contracts, we obtained data from DCMA's Mechanization of Contract Administrative Services (MOCAS) data system and conducted analysis to determine which contracts in our population were closed, and whether they were closed within the time frames specified by the Federal Acquisition Regulation (FAR). We also interviewed DOD officials responsible for managing the contract close out process and discussed factors that affect the closeout process time frames, including contract type. To assess the reliability of the DCMA closeout data, we reviewed documentation about this system and interviewed officials responsible for contract closeout. We determined that the data reported by DCMA were sufficiently reliable for identifying contract closeout status. Appendix I provides additional details on our scope and methodology.

We conducted this performance audit from November 2019 to January 2021 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

[5]GAO, *Standards for Internal Control in the Federal Government,* GAO-14-704G (Washington, D.C.: Sept. 10, 2014).

Background

Contract Type and the Acquisition Life Cycle

DOD acquires MDAPs through a framework that allows DOD officials to develop acquisition strategies and employ acquisition processes that match the characteristics of the capability being acquired.[6] Programs typically complete a series of milestone reviews and other key decision points as they move from research and development to production. Programs may also have multiple contracts and may use different contract types across the acquisition life cycle. The primary contract types described by the FAR fall into two broad categories—cost-type and fixed-price-type—and table 1 summarizes key features of each.

Table 1: Key Features of Cost-Type and Fixed-Price-Type Contracts

Feature	Cost-type	Fixed-price-type
Payment and incentive arrangements	• Government pays allowable costs incurred by contractor, to the extent prescribed by the contract, such as certain compensation costs for work performed. • Incentive arrangements included in the contract can allow the contractor to earn fees tied to performance, such as for performing at lower costs.	• Government generally pays a firm price. • Incentive arrangements included in the contract can allow the government to share in cost savings and can also allow the contractor to earn profit tied to performance. • Additional incentives, such as performance incentives, can also be included.
Risk assumption	• Government generally assumes the risk of a cost overrun.	• Contractor generally assumes the risk of a cost overrun.
Expectations of contractor	• Contractor is to make a good-faith effort to meet contract requirements within the estimated cost; however, the government is not promised a completed item or service within that cost.	• Contractor must meet contract requirements, including specified schedules, at firm prices or, in some cases, an adjustable price.

Source: GAO analysis of Federal Acquisition Regulation and Department of Defense data. | GAO-21-181

In general, the government assumes the greatest risk in research and development efforts using cost-type contracts where the government agrees to pay the contractor's allowable, allocable, and reasonable incurred costs, up to an established ceiling, which may be difficult to estimate in advance when requirements are still unknown or there are other uncertainties. As programs move from development to production and requirements become more stable and costs become better

[6]Department of Defense Directive No. 5000.01, *The Defense Acquisition System* (May 12, 2003, Incorporating change 2, Aug. 31, 2018); Department of Defense Instruction No. 5000.02, *Operation of the Adaptive Acquisition Framework* (Jan. 23, 2020); Department of Defense Instruction No. 5000.02T, *Operation of the Defense Acquisition System* (Jan. 7, 2015, Incorporating change 6, Jan. 23, 2020).

understood, the FAR and DOD guidance indicate that fixed-price-type contracts may be in the government's best interest.

In our audit, we focused on two primary types of fixed-price-type contracts:[7]

- **FFP Contracts:** Under this contract type, the government may agree to purchase an item or services for a firm price and the contractor is required to deliver the item or provide the services regardless of its actual costs. The contractor bears the maximum risk and full responsibility for all costs and resulting profit or loss. This contract type is suitable for situations where the government and contractor have a clear understanding of the scope of work and are confident in the cost of the item. With some exceptions, all DOD purchases of commercial items use FFP contracts.[8]
- **FPI Contracts:** Under this contract type, the contractor is incentivized to control costs since the contractor's profit is linked to actual performance. FPI contracts are appropriate when an FFP contract is not suitable or when the contractor's portion of cost responsibility will provide a positive incentive for effective cost control and performance.[9] FPI (firm target) contracts specify a target cost, target profit, target price, ceiling price, and a profit adjustment formula, referred to as a share ratio, or a share line.[10] The share line is intended to be the primary incentive for the contractor to control costs. However, the FAR states that the contract may include incentives on technical performance and/or delivery. If performance and/or delivery incentives are included, the performance requirements should provide a reasonable opportunity for the incentives to have a meaningful effect on the contractor's management of the work. The final negotiated total price payable to the contractor is subject to a ceiling

[7]Other fixed-price-type contracts include fixed-price contracts with economic price adjustment, fixed-price contracts with prospective price redetermination, fixed-ceiling-price contracts with retroactive price redetermination, and firm-fixed-price level-of-effort term contracts.

[8] With some exceptions, agencies shall use firm-fixed-price contracts or fixed-price contracts with economic price adjustment for the acquisition of commercial items. FAR § 12.207(a). DOD has reported that it only uses FFP contracts when purchasing commercial items.

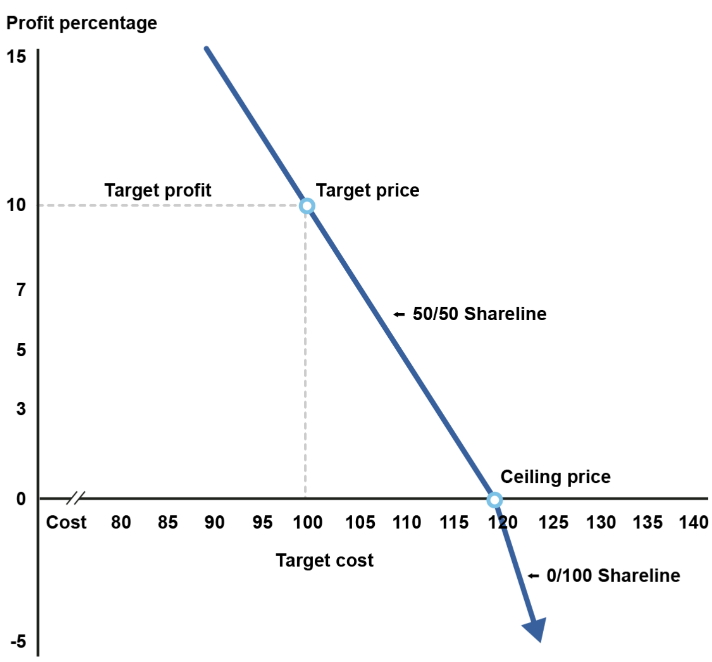
[9]FAR § 16.403(b)(1), (2).

[10]For the purposes of this report, unless otherwise noted, when we refer to FPI contracts, we mean FPI (firm target) contracts. FPI (firm target) contracts are commonly used for DOD MDAPs. In contrast, the other type of FPI contract, successive target, is rarely used.

price, which is the maximum that may be paid to the contractor, except for any adjustment under other contract clauses. Generally, the share line functions to decrease the contractor's profit as actual costs exceed the target cost. Likewise, the contractor's profit increases when actual costs are less than the target cost. These elements are all negotiated and can result in more or less risk for both the government and contractor.

Figure 1 depicts an example of an FPI contract and the elements that are negotiated at the outset. The example has a 50/50 share line above and below the target cost, which means that a cost overrun or cost underrun savings would be shared equally between the government and the contractor. The ceiling price, set at 120 percent of target cost, represents the government's maximum liability under the contract.

Figure 1: Example Depicting the Elements of a Fixed-Price-Incentive Contract



Target cost
The contract value against which final actual costs are measured in order to determine the final contract price. It should represent the point in the range of probable cost outcomes, from the most optimistic cost estimate to the most pessimistic cost estimate, that is considered to be the "most likely" cost outcome and at which there is an equal probability of either a cost underrun or overrun.

Target profit
A reasonable profit for target cost at target performance, determined by using a structured approach on negotiated contract actions when cost or pricing data is obtained.

Target price
The sum of the target cost and target profit which provides the basis for funding the contract.

Ceiling price
The maximum dollar liability for the government under the contract.

Share line
The formula used to adjust earned profit based on the variance of the final negotiated cost (either increase or decrease) from the target cost to determine the final price. It represents the allocation of cost risk between the government and the contractor. Expressed as a ratio that adds to 100, the first number is the government's share and the second number is the contractor's.

Source: GAO analysis of Defense Acquisition University information. | GAO-21-181

In 2017, we found that the Navy did not consistently collect data on the outcomes of FPI contracts, which makes it difficult to determine if they are improving contractor performance.[11] We recommended that DOD direct the Navy to issue an alert to contracting officials to ensure they followed guidance on documenting the rationale for using FPI contracts, and, in April 2017, the Navy issued a memorandum addressing this issue. We also recommended that the Navy conduct an assessment on the use of incentives on these contracts to enable contracting officials to share proven strategies for achieving intended cost, schedule, and quality outcomes. The Navy agreed with our recommendation but told us that an extended period of study was necessary. Following that period, the Navy plans to provide recommendations regarding the use of additional incentives on FPI contracts across its shipbuilding programs.

Additionally, in 2017, we found that since 2010, DOD had made changes to its regulations, policies, and guidance, and had taken other steps to improve its use of incentive contracts for all types of DOD acquisitions, but faced challenges in determining the benefits of those incentives.[12] DOD agreed with our recommendation to begin collecting and analyzing relevant data as contracts were sufficiently complete. As of July 2020, DOD had developed a template for the military departments to use to collect relevant information for its analysis of these types of incentive contracts.

DOD Guidance and Regulations on the Use of FPI Contracts

Starting in September 2010, DOD introduced a series of Better Buying Power initiatives. Subsequent guidance and regulations were issued, legislation was enacted, and tools were developed to encourage or facilitate the use of FPI contracts, in some instances focusing specifically on acquisitions moving from development to production as a way to obtain greater efficiency and productivity.[13] For example:

- A September 2010 memorandum issued by DOD's Office of the Under Secretary of Defense for Acquisition, Technology, and Logistics

[11]GAO, *Navy Shipbuilding: Need to Document Rationale for the Use of Fixed-Price Incentive Contracts and Study Effectiveness of Added Incentives*, GAO-17-211 (Washington, D.C.: Mar. 1, 2017).

[12]GAO, *Defense Contracting: DOD Needs Better Information on Incentive Outcomes*, GAO-17-291 (Washington, D.C.: July 11, 2017).

[13]Better Buying Power is department-level guidance directed at acquisition professionals, and seeks to obtain greater efficiency and productivity in defense spending through a number of different areas.

encouraged the use of FPI contracts for acquisition programs in early production. DOD encouraged the use of FPI contracts, in part, because it had previously awarded some cost-plus-award-fee contracts with subjective measures of award fee not clearly tied to cost control.[14]

- Another Better Buying Power memorandum in November 2010 outlined the expectation that acquisition teams pay particular attention to share lines and ceiling prices, and that FPI contracts with a 50/50 share line and 120 percent ceiling price should be the norm, or starting point for negotiations.[15] The Defense Federal Acquisition Regulation Supplement (DFARS) was also updated in 2011 to implement this guidance.[16]
- A September 2014 Better Buying Power white paper stated that one of its draft initiatives included increasing the use of incentive-type contracts, but noted the Department did not want exclusive use of those types of contracts. Instead, the white paper said these contract types should be used whenever appropriate and given explicit consideration and some preference over other contract types.
- In April 2015, an additional Better Buying Power memorandum stated, based on limited Department analysis, that the use of cost-plus-incentive-fee and FPI contracts was highly correlated with better cost and schedule performance.[17]
- In response to DOD's Better Buying Power initiatives, the Office of the Secretary of Defense's Defense Procurement Acquisition Policy Office

[14]Office of the Under Secretary of Defense for Acquisition, Technology and Logistics Memorandum, Subject: *Better Buying Power: Guidance for Obtaining Greater Efficiency and Productivity in Defense Spending* (Washington, D.C.: Sept. 14, 2010). A cost-plus-award-fee contract is a cost-reimbursement contract that generally provides for a fee consisting of a base amount (which may be zero) fixed at inception of the contract, and an award amount, based upon a judgmental evaluation by the government, sufficient to provide motivation for excellence in contract performance.

[15]Office of the Under Secretary of Defense for Acquisition, Technology and Logistics Memorandum, Subject: *Implementation Directive for Better Buying Power – Obtaining Greater Efficiency and Productivity in Defense Spending* (Washington, D.C.: Nov. 3, 2010).

[16]DFARS § 216.403-1(b)(3).

[17]A cost-plus-incentive-fee contract is a cost-reimbursement contract that provides for an initially negotiated fee to be adjusted later by a formula based on the relationship of total allowable costs to total target costs.

released guidance for using incentive contracts in April 2016.[18] The guidance sets forth a process for establishing an appropriate incentive arrangement for each acquisition's specific circumstances, providing insight into establishing share ratios and ceiling prices based on those unique circumstances.

- The NDAA for Fiscal Year 2017 required DOD to establish a preference for any fixed-price-type contract in the determination of contract type and specified approval requirements for use of cost-type contracts above certain dollar thresholds.[19] In response, DOD updated the DFARS in November 2019.[20]
- The DOD Sole Source Streamlining Toolbox, a living document encompassing over 40 techniques first used DOD-wide in 2018, can be leveraged to increase efficiency throughout the acquisition process. It provides information on considering the incorporation of FPI contracts in requests for proposals in lieu of FFP contracts, as well as using FPI contracts to close major gaps in cost differences.

Contract Closeout and Prior Related GAO Recommendation to DOD

Closing completed contracts within expected time frames is a key step in the contracting process and can help limit the government's exposure to certain financial risks by identifying and recovering improper payments. Contract closeout includes a number of administrative actions, which are performed by the contracting officials within the agencies or offices that have been delegated authority to perform these actions, such as DCMA within DOD. The FAR has different requirements for contract closeout time frames for different contract types—generally within 6 months for FFP contracts, and up to 36 months for contracts requiring settlement of indirect cost rates, subject to certain considerations, which includes FPI contracts.[21]

We previously made recommendations to DOD regarding contract closeout. For example, in September 2017 we recommended DOD develop a means for Department-wide oversight into components'

[18]Defense Procurement Acquisition Policy, Subject: *Guidance Using Incentive and Other Contract Types*, (Washington, D.C.: Apr. 1, 2016).

[19]National Defense Authorization Act for Fiscal Year 2017, Pub. L. No. 114-328, § 829 (2016).

[20]DFARS § 216.102.

[21]FAR §§ 4.804-1(a)(2), (3). Contracts requiring settlement of indirect cost rates should be closed within 36 months of the month in which the contracting officer receives evidence of physical completion.

progress in meeting their goals on closing contracts and the status of contracts eligible for closeout.[22] Specifically, we reported that DOD did not have critical elements agency-wide that would help track and oversee the contract closeout process—the number and type of contracts to be closed, where the contracts were in the process, and goals and performance measures. Since then, DOD has taken action to better track contracts due for closeout in its data system, including creating the ability to centrally track the number of contracts eligible to be closed and contracts that are overdue for closeout.

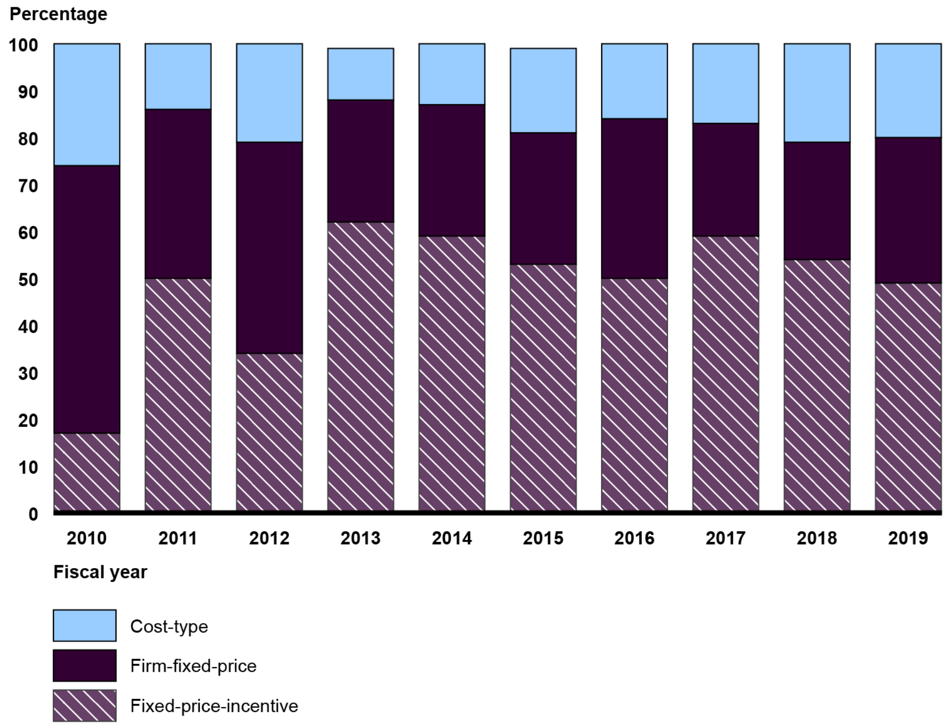
DOD Obligations on FPI Contracts for MDAPs Increased Over the Past 10 Years, While Use across Military Departments Varied

Use of FPI Contracts for MDAPs Increased from Fiscal Years 2010 through 2019

Over a 10-year period, DOD's obligations on FPI contracts associated with MDAPs grew to account for almost half of the $65 billion in obligations for fiscal year 2019. Specifically, obligations on FPI contracts for MDAPs increased from $1.3 billion, or 17 percent, in fiscal year 2010 to $32 billion, or 49 percent, in fiscal year 2019. The obligations on FFP contracts decreased, and obligations on cost-type contracts fluctuated between 11 percent and 26 percent during the same time period (see fig. 2).

[22]GAO, *Federal Contracting: Additional Management Attention and Action Needed to Close Contracts and Reduce Audit Backlog*, GAO-17-738 (Washington, D.C.: Sept. 28, 2017).

Figure 2: Percentage of Obligations by Contract Type for Major Defense Acquisition Programs from Fiscal Years 2010 through 2019



Source: GAO analysis of Federal Procurement Data System – Next Generation data. | GAO-21-181

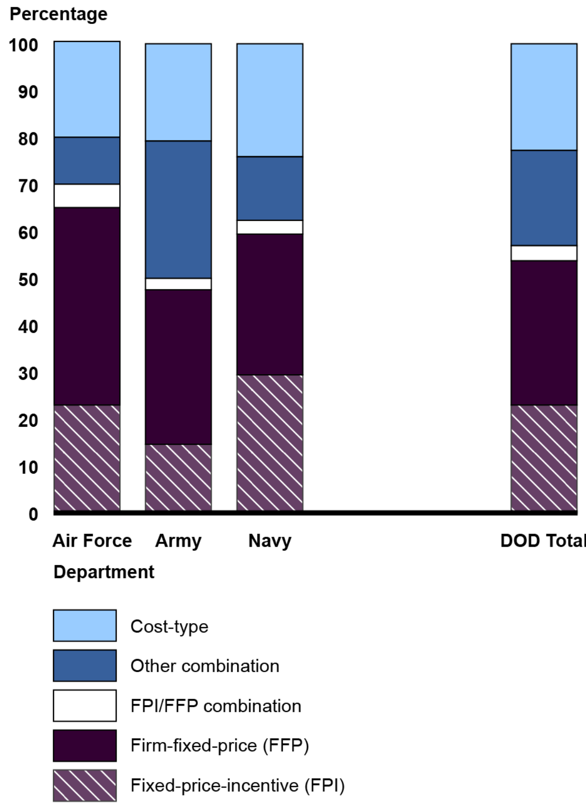
A similar trend holds true for DOD obligations overall. Specifically, DOD-wide obligations on FPI contracts increased from $16 billion, or 4 percent, in 2010 to $50 billion, or 13 percent, while obligations on FFP contracts decreased, and obligations on cost-type contracts stayed about the same (see appendix II).

Frequency of FPI Contract Usage to Acquire MDAPs Varied across Military Departments

The frequency of the use of FPI contract types varied across military departments for the 10-year period from fiscal years 2010 through 2019. During this period, DOD awarded 374 contracts associated with MDAPs and 86 of those, or 23 percent, were FPI contracts. While the Army awarded fewer contracts associated with MDAPs, it also used FPI contracts less frequently than the Air Force and the Navy as a percentage of the total contracts awarded in the selected time period. Specifically, for the 10-year period, the Navy had the largest proportion of FPI contracts at 29 percent. The Navy has used FPI contracts for shipbuilding programs for over 40 years. Twenty-three percent of the Air Force contracts were

FPI. In comparison, 15 percent of the Army's contracts were FPI. Army officials told us that prior to 2010, the Army had little experience in awarding FPI contracts. Figure 3 illustrates the percentage of contracts by contract type awarded by each of the military departments for the 10-year period.

Figure 3: Percentage of DOD MDAP Contracts by Contract Type and Military Department for the 10-Year Time Period from Fiscal Years 2010 to 2019



Source: GAO analysis of Department of Defense's (DOD) Defense Acquisition Management Information Retrieval (DAMIR) System data on Major Defense Acquisition Programs (MDAP) . | GAO-21-181

Note: The basic types of contracts described by the Federal Acquisition Regulation (FAR) may be used in combination, unless otherwise prohibited. The combination category includes contracts that used both cost-type and fixed-price-type structures on the same contract. DOD total includes jointly-managed contracts and Missile Defense Agency contracts.

DOD Guidance and Other Factors Influenced the Use of Selected FPI Contracts, but Use Has Not Been Assessed

Various Factors Influenced Contract Type Selection

Based on our review of 12 selected fixed-price-type contracts and interviews with DOD officials, we found that a variety of factors influenced contract type selection. For the six FPI contracts, we found that reasons for using this contract type were often related to addressing cost concerns. DOD's Better Buying Power guidance also identifies cost considerations as a reason for considering FPI contracts. Additionally, contracting officers we interviewed told us that department or service level leadership encouraged this contract type as a way to address cost concerns. For example,

- For a $132 million Air Force FPI Global Positioning System contract, a previous cost-type contract provided visibility into costs for the system's space vehicle development and engineering changes, among other things. This information allowed for the use of an FPI contract. In addition, Air Force officials told us that the decision to use an FPI contract was heavily influenced by the Better Buying Power initiative and Air Force leadership. Officials said that Air Force leadership was trying to incentivize the contractor to save costs by consolidating its supply chain across three different Air Force programs and, therefore, wanted to use FPI contracts for all three programs.
- For a $1.5 billion Army FPI contract for a family of ground vehicles, according to Army documentation, the contractor was overrunning costs on the preceding FPI contract, having difficulty with its cost estimating system, and the contract costs were not stable, according to officials. In addition to these concerns, Army officials said they decided to use an FPI contract because they believed this contract type would incentivize the contractor to decrease costs.
- For a $55 million Navy FPI contract for infrared search and track systems, the contracting officer told us that DOD guidance led to the

use of a fixed-price-type contract. Additionally, an FPI contract type was used because a previous contract for infrared search and track systems was FPI. The contracting officer told us that as of March 2020, the contract was experiencing a cost underrun.

For our six selected FFP contracts, we found that these contracts were often used when the program was mature and well into production, where requirements and costs were understood. For example:

- For a $205 million Air Force FFP contract for guided vehicle munition kits, the Air Force had already purchased multiple lots under a similar contract arrangement and the design and quantities were stable. Therefore, the Air Force decided an FFP contract would provide the contractor with the maximum incentive for cost control and effective performance. In addition, the contracting officer told us that there was no risk in awarding an FFP contract because they had actual cost data from previous contracts.
- For a $335 million Army FFP contract for sensors, Army officials stated that they were able to use an FFP contract because the Army had actual cost data from previous contracts that showed the contractor's proposed cost was within 4 percent of the actual costs in most instances over the last 5 years.
- For a $475 million Navy FFP contract for helicopters, the contractor had extensive experience with the helicopter weapon system and the Navy had reasonable certainty of contract costs and performance requirements, which enabled the selection of this contract type. The preceding production lot contract was also FFP and the contracting officer stated that the program had cost and pricing data on hand when it negotiated this production lot contract.

DOD guidance states that switching contract type from FFP to FPI during negotiations may help parties get past a negotiation impasse or expedite negotiations, and may help the parties come to an agreement on large differences in costs. This was the case in one of our selected contracts. Specifically, in a $1.3 billion Army FPI contract for helicopter airframes, the Army had originally begun negotiating an FFP contract. The contracting officer who negotiated the contract told us that there was a $100 million difference between what the contractor and government thought the price should be. During a Department-level review, the Director of Defense Procurement and Acquisition Policy Defense Pricing suggested that the contracting officer consider using an FPI contract to resolve cost differences. Switching to an FPI contract provided more room for negotiation and allowed the government to come to an agreement on that difference.

Structure of FPI Contracts Varied

For FPI contracts, a combination of elements, including the share line and ceiling price, determines the amount of cost risk placed on the government and the contractor. According to DOD, the combination of these elements can affect the cost and schedule performance outcomes of the contract. DOD's 2010 Better Buying Power initiative recommended a 50/50 share line and a 120 percent ceiling be used as the point of departure for establishing the incentive arrangement. It is important to note that these elements must be considered together as a whole to determine the amount of risk placed on the government. Additionally, since the contractor's profit is linked to actual performance, FPI contracts provide an incentive for the contractor to control costs.

We found that the structure of the FPI contracts we reviewed varied.

Share lines. Our review of six selected DOD FPI contracts indicated that five had share lines that could put more risk on the government. For example, both Army contract overrun share lines were 80/20, which means that the government would be responsible for 80 percent of the cost overrun up to a specified amount. A contracting officer for one of these contracts told us they negotiated these share lines because they were confident in the target cost and did not believe there would be an overrun. However, one of the two contracts was experiencing an overrun as of June 2020, according to contracting officials.

Ceiling Prices. Three of the six selected FPI contracts had ceiling prices that were less than the 120 percent starting point listed in Department guidance, which could reduce the risk on the government. A Department level official and a Navy official told us that the government has been able to negotiate lower ceiling prices in recent years, closer to 115 percent. As an example, a Navy FPI contract for infrared search and track systems had a ceiling price of nearly 115 percent. However, for our selected FPI contracts, the government did not always establish a ceiling price closer to 115 percent and three of the contracts had ceiling prices that were 120 percent or higher. For example, an Air Force FPI contract had a ceiling price of 127 percent and an overrun share line of 70/30, which means that the government would be responsible for 70 percent of the cost overrun up to a specified amount.

While the cost incentive of the share line is intended to be the primary incentive, three of our selected FPI contracts had incentives in addition to the share line, all of which were performance incentives. For example, the Air Force used a negative incentive in an FPI Global Positioning System contract. Air Force officials said that the contractor would be paid an incentive for the time the system's space vehicle orbited and would have to pay money back to the government if the space vehicle failed within a given period. We were told this incentive was used because it is not possible to determine if the space vehicle would function successfully until it was in orbit.

DOD Has Not Assessed the Use of FPI Contracts

Although the Better Buying Power initiatives encouraged the use of FPI contracts, and the use of FPI contracts has increased over the past 10 years, DOD has not assessed the extent to which its use of FPI contracts has helped achieve desired cost and schedule performance outcomes. DOD's Better Buying Power initiatives issued in 2010, 2013, 2014, and 2015 encouraged the use of FPI contracts to improve cost and schedule performance. The 2010 memorandum stated the measure of the success for using this contract type, with the parameters of a 50/50 share line and a 120 percent ceiling as a point of departure, would be fewer programs overrunning their cost targets.

The Director, Price, Cost, and Finance, Defense Pricing and Contracting, told us that one of the reasons DOD began emphasizing FPI contracts through the Better Buying Power initiatives was because the Department had found that on most major programs, there was a wide variance between the cost considered negotiated and the actual cost of performance on prior contracts. In the majority of cases, the actual cost was significantly lower than the cost considered negotiated. Therefore, the Department encouraged greater use of FPI contracts since the contractor is incentivized to reduce costs, but both parties share the risk and reward of actual cost performance. The Director further noted that DOD provides guidance on when FPI contracts should be considered in production and sole source follow-on programs. Specifically, this guidance states FPI contracts should be considered in these circumstances when actual costs on prior FFP contracts have varied by more than 3-4 percent from the costs considered negotiated.[23]

DOD's Defense Pricing and Contracting officials told us that DOD has not done an assessment of DOD's use of FPI contracts to determine whether

[23]DFARS Procedures, Guidance, and Information § 216.403-1.

the anticipated outcomes have been achieved. In addition, Air Force, Army, and Navy officials told us that they have not assessed outcomes from their use of FPI contracts at the military department level. The Director, Price, Cost, and Finance, Defense Pricing and Contracting stated that the information exists for the Department to assess its use of FPI contracts. Federal internal control standards state management should define objectives and assess performance toward achieving those objectives. [24] In the case of DOD's use of FPI contracts for MDAPs, this would include conducting an assessment of the desired cost and schedule performance outcomes, such as fewer programs overrunning target costs. Until DOD assesses its use of FPI contracts, it will be difficult to determine if this contract type—and the parameters set up for its use—are helping to achieve the desired cost and schedule performance outcomes at an agency-wide level.

Ten Percent of the MDAP Contracts Are Overdue for Closure, and DOD Faces Challenges in the Contract Closeout Process

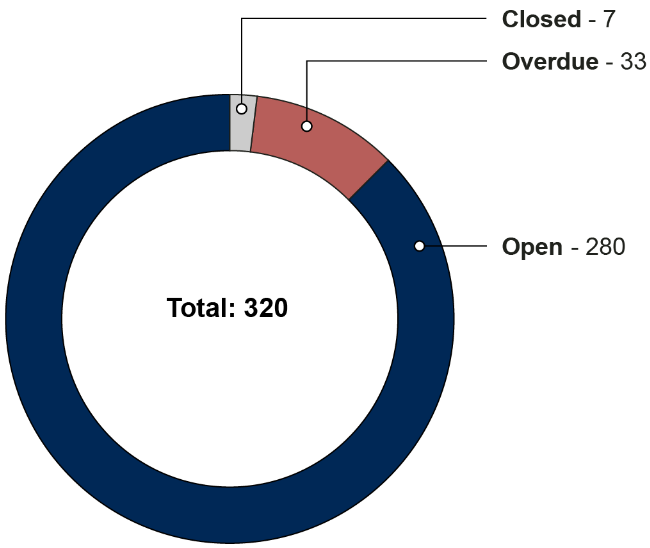
Of the 320 MDAP contracts we reviewed that are also tracked by DCMA, 10 percent (or 33 contracts) were overdue for closure as of November 2020.[25] More than half of these 33 contracts were more than a year overdue.[26] While the FAR has different requirements for contract closeout time frames for different contract types, we identified multiple factors that affected the closeout process within our selected contracts regardless of contract type. Figure 4 illustrates the status of DCMA-tracked contracts associated with MDAPs in our population awarded in fiscal years 2010-2019.

[24] GAO-14-704G.

[25] Of the 374 MDAP-related contracts we identified as being awarded from fiscal years 2010 through 2019, 320 were included in DCMA's Mechanization of Contract Administrative Services (MOCAS) payment system. The others were either closed more than 6 months ago, or DCMA was not involved in the closure of the contract and, as a result, the contract would not be included in the MOCAS system. For additional details see appendix I.

[26] Eighty-eight percent of the contracts in our population that were also tracked by DCMA were not due for closure as of November 2020 because the period of performance was still ongoing or the contract was still within the allowable time frame for closure, and thus the contract had not yet reached the point of closeout.

Figure 4: Closeout Status of Contracts Associated with Major Defense Acquisition Programs Awarded in Fiscal Years 2010-2019



Source: Defense Contract Mangement Agency's Mechanization of Contract Administration Services (MOCAS) database. | GAO-21-181

Note: These data represent the closeout status of those contracts in our population that were also tracked by the Defense Contract Management Agency.

Our review of selected DOD contracts found several factors that affected the closeout process regardless of contract type. Some factors affecting the closeout process are the transfer of government equipment, contracts with more than one contract type, and workforce issues.

Transfer of government-furnished equipment and property: According to an Army contracting officer, part of the reason why a 2009 helicopter FFP contract has not been closed out is because there is a large amount of government property that has to be transferred over from the contractor and this takes time. In addition, the contracting officer stated that the size of the program or acquisition, in terms of how much equipment it may have, can factor into contract closeout time frames as well. For example, missiles do not have as much government equipment so there is less property to transfer back to the government at the end of the contract, thus it takes less time to close out these contracts.

Combination contracts, or those contracts that contain more than one contract type across different contract line items: Combination contracts allow the government to award a contract in which portions of that contract (i.e., contract line items) have different contract types and therefore different pricing and payment terms.[27] This can provide more flexibility for the government in negotiating prices. For example, according to the Section 809 Panel, the government might award part of a contract based on adequate price competition with no certified cost or pricing data provided by the contractor, but not include other parts of the same contract in the evaluated price for contract award. This might happen when the government intends to negotiate pricing for the other parts of the contract after award, possibly with the submission of certified cost or pricing data.[28]

Combination contracts can affect contract closeout time frames. For example, if the contract primarily has FFP contract line items, but it also has cost-type contract line items, the contracting officer would need incurred costs and rate data to close out the cost-type contract line items and therefore the whole contract. As an example, according to officials, closeout for a Navy helicopter contract in our sample was to be completed in April 2016 but the contract still is not closed out because, while the contract is an FFP contract, it also contains cost contract line items. The Navy and DCMA are awaiting final rates from the contractor for those cost contract line items and are unable to close the contract without this information. A DCMA official told us if the overall contract type is fixed-price, the contractor may believe it does not owe the government specific cost data, even for cost-type contract line items, because that information is not required for fixed-price-type contracts.

Contracting workforce issues: Officials from each of the military departments told us contract closeout has been affected by contracting workforce issues. For example, Army officials identified multiple reasons for a backlog of contracts eligible for closeout at the Army Contracting Command-Redstone Arsenal, which has delayed the closeout of these contracts for this buying center. These reasons include a lack of contracting officers, particularly experienced contracting officers, to complete the work. The backlog includes all contract types and officials stated all contracts are taking a longer time to close now, regardless of type. According to Army officials, as a result of a shift in the Army's focus

[27]These contracts are referred to as both combination and hybrid contracts in DOD documentation. For the purposes of this report, we are using the term combination contract.

[28]The Advisory Panel on Streamlining and Codifying Acquisition Regulations (Section 809 Panel), *Report of the Advisory Panel on Streamlining and Codifying Acquisition Regulations—Volume* 2, (Arlington, VA.: June 2018).

from execution to administration of contracts, the Army Contracting Command-Redstone Arsenal established a Post Award Division, which has six priorities; contract closeout is the lowest priority. When the Post Award Division was set up, the Army Contracting Command-Redstone Arsenal had 30,000 contract actions that were waiting to be closed out. An Air Force official also stated the Air Force had contracting workforce issues and that prior to 2017, the focus was on executing contracts and not close out.

Additionally, another more general factor that affects contract close-out is contracts under investigation or in litigation. Contracts cannot be closed while they are involved in litigation or under investigation.

Conclusions

When selecting a contract type the government aims to negotiate a contract type that will result in reasonably low government risk and provide the contractor with the greatest incentive for efficient and economical performance. DOD and Congress have encouraged or facilitated the use of fixed-price-type contracts, and specifically FPI contracts that use share lines and other incentives to encourage better cost and schedule performance. DOD's obligations on FPI contracts associated with MDAPs have grown over the past 10 years to account for almost half of the $63.5 billion in obligations for fiscal year 2019. However, the Department has not assessed its use of FPI contracts, which makes it difficult to determine if this contract type is helping to achieve the desired cost and schedule performance outcomes at an agency-wide level.

Recommendation for Executive Action

The Secretary of Defense should conduct an assessment of DOD's use of FPI contracts for MDAPs, including the extent to which share lines and other contract elements contributed to achieving desired cost and schedule performance outcomes. (Recommendation 1)

Agency Comments and Our Evaluation

We provided a draft of this report to DOD for review and comment. In written comments, reprinted in appendix III, DOD concurred with our recommendation, stating it plans to refine the assessment recommended in GAO-17-291, "DOD Needs Better Information on Incentive Outcomes," to address the performance outcomes for Major Defense Acquisition Programs. That report recommended DOD collect and analyze relevant data after contract performance is sufficiently complete to determine the extent to which contracts with incentives achieved their desired outcomes. We believe that refining the assessment to include cost and schedule performance outcomes from fixed-price-incentive contracts on major defense acquisition programs meets the intent of our recommendation. DOD also provided technical comments, which we incorporated as appropriate.

We are sending copies of this report to the appropriate congressional committees, the Secretary of Defense, and other interested parties. In addition, the report is available at no charge on the GAO website at http://www.gao.gov.

If you or your staff have any questions about this report, please contact me at (202) 512-4841 or russellw@gao.gov. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this report. GAO staff who made key contributions to this report are listed in appendix IV.

Sincerely yours,

W. William Russell
Director, Contracting and National Security Acquisitions

List of Committees

Chair
Ranking Member
Committee on Armed Services
United States Senate

Chair
Ranking Member
Subcommittee on Defense
Committee on Appropriations
United States Senate

The Honorable Adam Smith
Chairman
The Honorable Mike Rogers
Ranking Member
Committee on Armed Services
House of Representatives

Chair
Ranking Member
Subcommittee on Defense
Committee on Appropriations
House of Representatives

Appendix I: Objectives, Scope, and Methodology

Section 807(b) of the National Defense Authorization Act (NDAA) for Fiscal Year 2020 included a provision that we report on the Department of Defense's (DOD) use of fixed-price contracts, including fixed-price-incentive (FPI) contracts.[1] This report describes (1) the extent to which DOD awarded FPI contracts associated with major defense acquisition programs (MDAPs) from fiscal years 2010 through 2019; (2) the factors that influenced DOD's decision to use FPI contracts and the extent to which DOD has assessed their use; and (3) the extent to which DOD has faced challenges in closing out fixed-price-type contracts. This report also contains information on DOD's use of fixed-price contracts in general.

To examine the extent to which DOD awarded FPI contracts, we identified a population of 374 contracts associated with 101 Acquisition Category I MDAPs awarded from fiscal years 2010 through 2019.[2] This population included firm-fixed-price (FFP), FPI, FFP/FPI combination contracts, and other combination contracts.[3] These contracts were reported in DOD's Selected Acquisition Reports from fiscal year 2010 through fiscal year 2019. For our contract population selection, we excluded contracts with values below $40 million. Selected Acquisition Reports require data to be reported on the largest six active contracts associated with the program. The dollar threshold for reporting contracts in the SAR is $40 million. We used the Defense Acquisition Management Information Retrieval (DAMIR) system to identify those contracts reported in Selected Acquisition Reports. The data from this system reflect programs that were included in Selected Acquisition Reports at any point during this 10-year period. We chose this time frame so as to select

[1]Pub L. No. 116-92, § 807(b) (2019).

[2]In general, MDAPs are designated programs that, among other things, meet or exceed Acquisition Category I thresholds, which are $525 million in research, development, test, and evaluation, or $3.065 billion in procurement in fiscal year 2020 constant dollars. Department of Defense Instruction No. 5000.02, *Operation of the Adaptive Acquisition Framework* (Jan. 23, 2020); Department of Defense Instruction No. 5000.85, *Major Capability Acquisition* (Aug. 6, 2020). Defense acquisition programs have multiple contracts associated with them. For example, one weapon system program for a ship or aircraft would have a contract for research and development of the system, and other contracts for production of the system and its various subcomponents.

[3]"Combination contracts," which may be called "hybrid contracts" at some agencies, contain two or more contract types in their line items, such as cost-reimbursement and firm-fixed-price. Under a cost-reimbursement contract, the government agrees to pay the contractor's allowable incurred costs to the extent prescribed in the contract. FAR § 16.301-1. Under a firm-fixed-price contract, the price is not subject to any adjustment on the basis of the contractor's cost experience in performing the contract. FAR § 16.202-1. It may be beneficial for the government to use both contract types in the same contract, depending on the circumstances.

contract awards that were made after regulatory and policy changes starting in 2010 and had completed performance by the time of our review.

Next, we analyzed Federal Procurement Data System-Next Generation (FPDS-NG) data on DOD-wide obligations, and obligations by contract type for the population of MDAP contracts identified in DAMIR, which were awarded from fiscal years 2010 through 2019. Per the DFARS Procedures, Guidance, and Information, when entering contract type information info FPDS-NG, the data entrant is to choose the contract type that is applicable to the predominant amount of the contract action, based on the value of the line items; the selected contract type automatically populates for any subsequent contract action report for modifications.

We assessed data reliability for the contract population by comparing the contract types identified in FPDS-NG for each contract with information on contract types contained in DAMIR, and determined the DAMIR and FPDS-NG data were sufficiently reliable for the purposes of analyzing the extent of DOD's use of fixed-price-type contracts for MDAPs. We included obligations associated with contract types contained in FPDS-NG if they matched contract types contained in DAMIR. When there was not a match with either source, we reviewed the contract types contained in Selected Acquisition Reports and contract documentation to determine the most appropriate contract type with which to label those obligations.

To determine the factors that influenced DOD's decision to use FPI contracts and the extent to which DOD has assessed their use, we selected a non-generalizable sample of 12 contracts from the 374 identified Acquisition Category I contracts for an in-depth review. Specifically, we reviewed six FPI contracts—two from each of the three military departments. We also reviewed six FFP contracts—two from each of the military departments—to understand factors that influenced the use of fixed-price contracts more broadly.[4] We used a purposeful stratified sampling procedure in which we intentionally chose contracts with particular characteristics to capture two common fixed-price-type contracts and important variations by military department. We did not include Navy shipbuilding contracts in our sample set, because we issued

[4]We specifically reviewed FPI (firm target) contracts. We did not include FPI (successive target) contracts in our sample. We also did not include jointly-managed and Missile Defense Agency-managed major defense acquisition programs in our sample set of 12 contracts. Those programs included the F-35 and the Ballistic Missile Defense System.

a report in fiscal year 2017 that specifically examined the extent to which the Navy entered into FPI contracts over 10 years.[5] In addition, we replaced two contracts in the sample because Army officials told us that they were the subject of an ongoing investigation. Finally, one selected contract was identified as FPI in the DAMIR system but was actually a combination contract, which included both FPI and cost-type contract line items. This contract was included in the review because a portion of the contract was structured as FPI. Because we used a non-generalizable sample of contracts, results from this sample cannot be used to make inferences about all fixed-price contracts that DOD awarded.

We conducted file reviews for the 12 selected contracts. Specifically, we analyzed documents such as price negotiation memorandums, business clearance memorandums, acquisition strategies and additional documentation stating the rationale for contract type.[6] Further, for FPI contracts, we analyzed how responsibility was shared between the government and contractor for cost overruns or underruns, which is indicated in the share line, compared to the agreed upon target cost, and ceiling price. Next, we reviewed relevant contracting regulations and DOD policy documentation, including Federal Acquisition Regulation (FAR) Part 16: Types of Contracts; Better Buying Power initiatives; DFARS Procedures, Guidance, and Information 216: Types of Contracts; and DOD Guidance on Using Incentive and Other Contract Types. We also conducted interviews with the contracting officers and several cognizant commands responsible for the selected contracts. We obtained information regarding their use of fixed-price-type contracts, including the conditions under which fixed-price-type contracts were used, their rationale for deciding to utilize such contract types as well as the effects of the selected contract type.

We determined that the risk assessment component of internal control was significant to this objective, along with the underlying principles that management should define objectives and assess performance toward achieving those objectives.[7] To assess the extent to which DOD had

[5]GAO, *Navy Shipbuilding: Need to Document Rationale for the Use of Fixed-Price Incentive Contracts and Study Effectiveness of Added Incentives,* GAO-17-211 (Washington, D.C.: Mar. 1, 2017)

[6]Price negotiation memos and similar documentation may also be referred to as business clearance memorandums or pre-negotiation memorandums. The title of the document varies.

[7]GAO, *Standards for Internal Control in the Federal Government,* GAO-14-704G (Washington, D.C.: Sept. 10, 2014).

evaluated the results of the use of FPI contracts we interviewed DOD officials, including those from each military service, and requested information on any analysis completed in this area since 2010. We compared this information to federal internal control standards related to defining objectives and assessing performance toward achieving those objectives. We also reviewed DOD memorandums and policies related to the use of FPI contracts.

To determine the extent to which DOD has faced challenges in closing out fixed-price-type contracts, we obtained data from DCMA's Mechanization of Contract Administrative Services (MOCAS) data system and conducted analysis to determine which contracts in our population were closed, and whether they were closed within the time frames specified by the FAR.[8] Of the 374 MDAP-related contracts we identified as being awarded from fiscal years 2010 through 2019, 320 were found in DCMA's MOCAS payment system.[9] The others were either closed more than 6 months ago, or DCMA was not involved in the closure of the contract and, as a result, would not be included in the MOCAS system. The data we used to determine if the contracts in our population were open or closed are only representative of the 320 contracts that were found in DCMA's MOCAS payment system. Fifty-four contracts in our population were not identified in the MOCAS database as of May 2020. We also interviewed DOD officials responsible for managing the contract close out process and discussed factors that affect the closeout process time frames, including contract type. To assess the reliability of the DCMA closeout data, we reviewed documentation about this system and interviewed officials responsible for contract closeout. We determined that the data reported by DCMA were sufficiently reliable for identifying contract closeout status.

To address all three objectives, we interviewed contracting officials and contracting officers for our 12 selected contracts, officials from the Defense Contract Management Agency, the Defense Acquisition

[8]We matched data from DAMIR with data from MOCAS to determine the closure status of the contracts in our population. These data and associated contract status were current as of May 2020. In November 2020, we requested an update specifically on the contracts that were listed as overdue for closure on MOCAS. As of November 2020, 33 contracts that were listed as overdue for closure had not been closed.

[9]MOCAS is an integrated contract administration and payment system. The system is designed to provide DCMA and the Defense Financial Accounting Services with electronic information necessary to accomplish their mission of contract and payment administration.

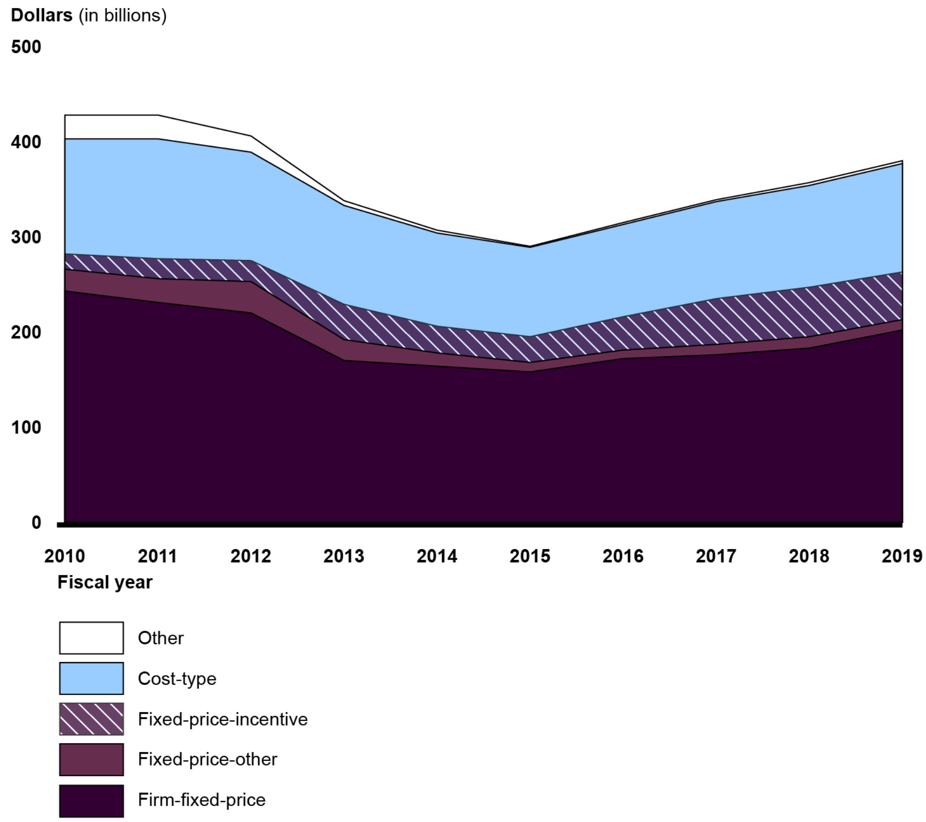
University, and the Office of the Secretary of Defense’s Defense Pricing and Contracting Directorate.

We conducted this performance audit from November 2019 to January 2021 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Appendix II: Defense-Wide Use of Fixed-Price-Type Contracts

From fiscal year 2010 to fiscal year 2019, DOD-wide obligations on fixed-price-type contracts decreased slightly. However, within that time frame, DOD obligations on fixed-price-incentive contracts increased from $16 billion to $50 billion. Obligations on firm-fixed-price contracts decreased, and obligations on cost-type contracts stayed about the same for this same time period (see fig. 5).

Figure 5: Defense-Wide Obligations by Contract Type, Fiscal Years 2010 through 2019



Source: GAO analysis of Federal Procurement Data System – Next Generation data. | GAO-21-181

Note: While contract types may be used in combination in accordance with the Federal Acquisition Regulation (FAR), per the Defense FAR Supplement (DFARS) Procedures, Guidance, and Information, when entering contract type information into Federal Procurement Data System-Next Generation, the data entrant is to choose the contract type that is applicable to the predominant amount of the contract action, based on the value of the line items. Dollar amounts are adjusted for inflation.

Appendix III: Comments from the Department of Defense

OFFICE OF THE UNDER SECRETARY OF DEFENSE
3010 DEFENSE PENTAGON
WASHINGTON, DC 20301-3010

ACQUISITION
AND SUSTAINMENT

Mr. W. William Russell
Director, Contracting and National Security Acquisitions
U.S. Government Accountability Office
441 G Street, NW
Washington DC 20548

Dear Mr. Russell:

This is the Department of Defense (DoD) response to Government Accountability Office (GAO) Draft Report, GAO-21-181, "FIXED-PRICE-INCENTIVE CONTRACTS: DoD Has Increased Their Use but Should Assess Contributions to Outcomes," dated January 2021 (GAO Code 103947).

The Department's official written response for inclusion in the report is enclosed. My point of contact is Sara Higgins, who can be reached at sara.a.higgins2.civ@mail.mil.

Sincerely,

TENAGLIA.JOHN.M.1154945926
Digitally signed by TENAGLIA.JOHN.M.1154945926
Date: 2021.01.15 13:13:03 -05'00'

John M. Tenaglia
Principal Director,
Defense Pricing and Contracting

Attachment:
As stated

GAO DRAFT REPORT DATED JANUARY, 2021
GAO-21-181 (GAO CODE 103947)

"FIXED-PRICE-INCENTIVE CONTRACTS: DOD HAS INCREASED THEIR USE BUT SHOULD ASSESS CONTRIBUTIONS TO OUTCOMES"

DEPARTMENT OF DEFENSE COMMENTS
TO THE GAO RECOMMENDATION

RECOMMENDATION 1: The GAO recommends that the Secretary of Defense should conduct an assessment of the Department of Defense's use of Fixed Price Incentive contracts for Major Defense Acquisition Programs, including the extent to which share lines and other contract elements contributed to achieving desired cost and schedule performance outcomes.

DoD RESPONSE: DoD concurs. To reduce duplication of effort and leverage previous analyses, the Department plans to refine the assessment recommended in GAO-17-291, "DoD Needs Better Information on Incentive Outcomes," to address the performance outcomes for Major Defense Acquisition Programs.

Appendix IV: GAO Contact and Staff Acknowledgments

GAO Contact

W. William Russell at (202) 512-4841 or russellw@gao.gov

Staff Acknowledgements

In addition to the contact named above, Angie Nichols-Friedman (Assistant Director), C. James Madar (Assistant Director), Julie A. Clark (Analyst-in-Charge), Jenny Chanley, Suellen Foth, Stephanie Gustafson, Scott Hiromoto, Heather B. Miller, Miranda Riemer, Miranda Wickham, and Robin Wilson made key contributions to this report.

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