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DASN (AP)
Attn: Clarence Belton
1000 Navy Pentagon, Room BF992
Washington, D.C. 20350-1000
Via email: ssip@navy.mil

Ref: Navy Proposed Policy Letter: Superior Supplier Incentive Program
CODSIA Case 03-13

Dear Mr. Belton:

The undersigned members of the Council of Defense and Space Industry Associations (CODSIA)[1] appreciate the opportunity to comment on the Navy's (DoN) proposed policy letter establishing the Navy Superior Supplier Incentive Program (SSIP), published in the *Federal Register* on April 9, 2013.[2] This is the second time that the Navy has solicited public comments on an SSIP. On May 24, 2010, the Navy published a similar notice requesting public comments on a "preferred supplier program."[3] On June 11, 2010, the Navy withdrew any further consideration of that 2010 program[4] but regrettably never published any further information on the comments received. Nevertheless, on July 30, 2010, CODSIA submitted extensive comments in response to that 2010 notice;[5] in those comments we raised numerous questions and concerns with the proposed preferred supplier program and we recommend that the Navy consider our prior comments during the development of this current initiative.

However, we are concerned with the guidance on Better Buying Power (BBP) 2.0, issued by the Under Secretary (AT&L) on April 24, 2013, that directs the DoN to implement a Navy pilot SSIP by June 1, 2013 and announce the first recipients of the Superior Supplier designation by July 1, 2013. There is a lack of information in the April 2013 *Federal Register* notice regarding the selection criteria for the pilot program, other than evaluating the top 15 DoN contractors on the basis of the value of contract awards in the most recent fiscal year. Information regarding implementation of the pilot program and the criteria the Navy will use to select and announce

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[1] CODSIA was formed in 1964 by industry associations with common interests in federal procurement policy issues, at the suggestion of the Department of Defense. CODSIA consists of six associations – the Aerospace Industries Association (AIA), the National Defense Industrial Association (NDIA), the Professional Services Council (PSC), the American Council of Engineering Companies (ACEC), TechAmerica, and the U.S. Chamber of Commerce. CODSIA's member associations represent thousands of government contractors nationwide. The Council acts as an institutional focal point for coordination of its members' positions regarding policies, regulations, directives, and procedures that affect them. A decision by any member association to abstain from participation in a particular case is not necessarily an indication of dissent.
[2] Available at http://www.gpo.gov/fdsys/pkg/FR-2013-04-09/pdf/2013-08190.pdf
[3] Available at http://www.gpo.gov/fdsys/pkg/FR-2010-05-24/pdf/2010-12349.pdf
[4] Available at http://www.gpo.gov/fdsys/pkg/FR-2010-05-24/pdf/2010-12349.pdf
[5] Available at http://www.pscouncil.org/PolicyIssues/AcquisitionPolicy/AcquisitionPolicyIssues/CODSIA_Comments_on_N.aspx. On July 23, 2010, the Aerospace Industries Association also submitted comments on the 2010 notice.

the first recipients of the Superior Supplier designation must be issued well in advance of implementation and announcing the first recipients of the designation. Several CODSIA associations submitted comments this year to the Under Secretary on the treatment of an SSIP in response to the BBP 2.0 draft; those comments addressed the need for the SSIP selection process and program to be fair and transparent to allow the entire acquisition community to comment and offer recommendations. Specifically, we believe it will be critical to structure the program in such a way as to ensure fairness while providing meaningful incentives for good performance against established criteria.

The 2013 Notice

According to the 2013 *Federal Register* notice, under the SSIP, contractors that have demonstrated exemplary performance at the business unit level in the areas of cost, schedule, performance, quality, and business relations would be granted Superior Supplier Status (SSS). Contractors that achieve SSS could receive more favorable contract terms and conditions in DoN contracts. In addition to recognition of SSS at the business unit level, multi-business unit corporations that have several business units which attain SSS may receive additional recognition by the DoN at the corporate level. This additional corporate recognition will not result in the receipt of more favorable terms and conditions in DoN contracts but may result in the use of more favorable business practices by the DoN in its relations at the corporate level.

The notice provides for creation of a pilot program with the top 15 DON contractors based on the most recent fiscal year sales to DoN in either goods or services. It establishes SSS and a process by which companies are evaluated to obtain that status. As envisioned for the pilot program, once a contractor is designated as a SSS, DoN contracting officers will be authorized to offer the contractor more favorable contract terms and conditions including, but not limited to, those listed below:

- More favorable progress payments. Adjustments may be made to progress payment percentages or retention percentages.
- Priority for adjudication of final labor and indirect cost rates.
- Increase in the intervals between business system reviews.

However, it is unclear whether the regulatory authority to implement these more favorable terms and conditions currently exists and we urge the DoN, in coordination with the Office of the Secretary of Defense, to establish any such necessary legal authority if it is absent, and/or plan to modify the existing acquisition regulations to create the proper authorities in the planning for implementation beyond the pilot program.

The 2013 notice solicits comments on seven questions below and we address each of them.

What clauses are currently being used in government subcontracts, and commercial contracts and subcontracts, to incentivize superior performance, at the corporate level, in the areas of cost, schedule, performance, quality, and business relations?

Typically, industry does not provide incentives to its suppliers at the corporate level. On a case-by-case basis, industry does analyze subcontracts and purchase orders with suppliers to determine if any contract specific incentives are warranted. Companies generally use cost incentives (e.g. CPI or FPI) to address cost performance. For schedule and performance incentives, companies generally write specific incentives clauses that provide incentives for on-time/early delivery or achieving above target performance/technical requirements when these attributes are considered essential to prime contract performance. Additionally, companies generally find that performance-based payments are a significant incentive to performance in that the supplier understands that payment depends on completing specified criteria. Further, many companies have a Supplier Rating System that provides added incentives when a supplier achieves certain criteria (e.g., 4 consecutive quarters of 4-star performance) such as relief of supplier source inspections and automatic inclusion of the supplier in RFQs, RFIs and RFPs. The intent should be to incentivize the supplier to top performance in each of these categories through a combination of government actions.

What solicitation provisions, contract clauses, and performance incentives will provide contractors with the greatest motivation to achieve SSS?

It is difficult to provide specific examples until we understand more about the specifics of the SSIP and the questions we pose below are answered. However, as general principles, participation in the program must provide:

- **Transparency** to the participating companies - they must be able to see what the DoN is considering in making a determination.
- **Due Process** – companies must be afforded the opportunity to respond to information being considered and there must be a way of resolving differences of opinion on matters under consideration between DoN and the companies.
- **Returns** commensurate with the efforts by the companies to become and maintain an SSS. Returns must be measured by performance, not by rigid adherence to weighted guidelines when applicable.
- **Business Growth –** a significant incentive to maintaining SSS status is the certainty or increased certainty of business growth by, for example, establishing award-term like conditions for contractors who maintain SSS status over a period of time or providing follow-on work. SSS should be awarded the opportunity for increased business.

Some examples of these principles are:

- Award Term Incentive (extends contract period of performance without additional competition);
- FAR Part 12 commercial item contracts that incentivize the supplier to reduce costs by inserting the most current technologies that also enhance product performance and reliability;
- Cost Reimbursement Incentive Contracts (FAR 16.405);
- Cost Incentive (contractor retains a pre-determined portion of any cost under-run);
- Schedule Incentive (contractor receives a reward in terms of additional fee/profit for improving a delivery schedule);
- Technical Performance Incentive (contractor receives a reward for improving some performance of product or service).

What contract terms and conditions increase cost or impair performance and could be removed from contracts with Superior Suppliers without significant risk to the Government?

The proliferation of regulatory reporting requirements embedded throughout a contract is one area that drives up contractor costs, but the number and scope of clauses eligible for elimination is idiosyncratic to different offerors and for different acquisition conditions. We recommend that the Navy considerer modulating the scale of such embedded reporting requirements and relieve superior suppliers of that burden while continuing to engage with industry to identify clauses subject to elimination as the pilot gains traction and as individual requirements are solicited.

The currently identified "favorable" terms and conditions would not equally benefit all contractors; thus, the selected terms and conditions should encourage all contractors to strive to achieve SSS. Additional contract terms and conditions that could be provided or removed for top suppliers include:

- Authorize progress payment and interim cost type billings on a more frequent basis than normal practice permits (FAR clauses 52.232-16 and 52.216-7) without additional consideration. This option represents a considerable incentive as it permits the supplier to reduce invested capital balances required to perform. Performance-based payments are another form of incentives and should be offered with a more accommodating and flexible cash model.

- Eliminate or reduce fee withholding requirements on cost type programs (FAR clauses 52.216-8, 52.216-10, and 52.232-7).The current withhold process is costly to administer and places a significant amount of Navy funds at risk of cancellation.

- Provide unusual progress payment rates up to 99% of incurred cost on contracts that would not otherwise qualify for unusual financing under the requirements established by FAR 32.501-2 (Unusual Progress Payments).

- Accelerate payments of invoices normally subject to Net 30 day terms.

- Add a greater return for those who maintain consecutive quarters of 3- and/or 4-star ratings over either the contract period of performance or another defined contract performance interval.

- Work with strategic suppliers to ensure equitable commercial item determinations are made, including the use of FAR Part 12 contracts to motivate supplier performance.

- Provide relief from both source and destination inspections and from other government oversight actions, including audits, which will provide cost savings for both parties.

- Consider the potential for follow-on work that provides sustained superior performance; this will reduce cost to the government with little risk. Look into more frequent use of award term contracts as an entitlement mechanism to reward superior performance. For example, guaranteeing the top suppliers are afforded automatic inclusion in competitive procurements within their identified product or service areas creates the potential for the supplier to improve its new business capture.

- Provide acknowledgement and benefit in the source selection evaluation of supplier rating; it should cost the government less to manage a top supplier and the top suppliers' costs will be lower due to reduced government oversight. The Navy should want to drive business to top performing suppliers and top rated suppliers should be given a competitive preference.

- Provide for annual public acknowledgement of superior suppliers.

Energy Efficiency is a critical DoN requirement significantly impacting the successful achievement of DoN's missions. How should a contractor's use of energy as it relates to the entire lifecycle of a product—design, manufacture, use, maintenance, and disposal—be considered in the designation of Superior Suppliers?

We agree that life-cycle cost should be a measure of performance by all companies. However, neither DoN or industry is capable of fully measuring or capturing all of those costs because each lacks access to the critical information necessary to complete the measurement, even though there are ways to measure parts of the life-cycle costs that could be used as evaluation factors in specific source selections. Some of those categories already being measured by some include energy and greenhouse gas usage.

It is appropriate to evaluate an energy efficiency program at the corporate level. A life-cycle analysis for individual products should not be assessed as part of a firm's energy efficiency program. In addition, the Navy must determine whether its Energy Efficiency Program will be measured quantitatively or qualitatively. If a quantitative approach is taken, the program should measure greenhouse gas (GHG) emissions that are specifically called out for measurement and reduction in President Obama's Executive Order 13514, although the specific application of such standards are still being determined based on the April 2010 preliminary recommendations from the General Services Administration issued pursuant to Section 13 of that Executive Order.

Nevertheless, not all suppliers will be able to meet this requirement and, under the limited outlines of the program provided, a contractor cannot receive a 5 star rating unless it meets this requirement. Thus, the program should allow a contractor to earn an additional star but not serve to penalize a supplier.

How long should SSS last?

Superior Supplier Status should last a minimum of three (3) years, consistent with the philosophy in FAR Part 42.1503(e) that past performance information should not be older than three (3) years. Alternatively, SSS could be an ongoing evaluation process with the objective to have continuous sustained SSS performance quarter over quarter. Under the 2013 notice, once an SSIP determination is rendered, it is unstated whether there will be a fixed term in effect or if it is a continuous, rolling, evaluation; we recommend the latter.

What criteria, other than CPARS data elements, should DoN use to select companies for evaluation as superior suppliers?

It is unclear how DoN will aggregate all the CPARS activities into a business unit level evaluation rating given that CPARS data is program/project based. In addition, are the Star Ratings at the Business Unit level a simple average of the star ratings for an evaluation area (e.g. technical or schedule, or cost control, etc.) across a business unit?

Again based on the experience of our member companies, we recommend quarterly performance assessments against the published criteria for both objective and subjective assessment elements/sub-categories. CPARS assessments often contain outdated information or are focused on the "issue du-jour" at the expense of underlying trend or longer term performance assessments. As such, quarter-over-quarter performance assessments provide more meaningful performance trend data and should be the basis for determining the supplier rating.

Before initiating any pilot program, we strongly recommend that DoN publish the specific evaluation criteria. Our experience is that there are eight primary defined assessment elements: Management, Technical, Schedule, Cost, Proposal, Supply Chain Management, Mission Assurance and Quality, and Customer Satisfaction. While they often employ a mix of subjective and objective criteria, even the subjective criteria can be described within defined guidelines. Company established assessment criteria are often posted on company websites and reviewed and discussed with suppliers in advance to ensure that they understand the criteria to be used each quarter; the Navy would benefit from a similar approach.

Is there any other aspect of the proposed SSIP on which you wish to comment?

It is unclear from the 2013 notice how DoN will define "Business Unit" for purposes of this program. We concur that supplier performance assessment should be done at the business unit level. In industry's experience there is some variability in the performance of various business units of a large company and, in some instances, even at different locations within business units. In our view, doing the assessments at the business unit level will provide DoN with the correct visibility into relevant contractor performance. We also recommend that Navy consider how it will address business units with multiple contracts – we believe that the most benefit comes from assessment on each contract, with a roll-up of overall performance for that business unit. We do not recommend that a "business unit" be defined by DUNS number as they are identified in CPARS today because DUNS numbers are assigned to physical locations of a contractor, not the business units which may contract at multiple locations.

The 2013 notice states that contractors must achieve a 3-Star rating to be designated a Superior Supplier. Is that 3-Star rating required for each individual evaluation areas or is it a simple or weighted average of the scores against all of those evaluation areas?

Some of our member company supplier performance programs differentiate between suppliers who receive only purchase orders for firm-fixed price, commodity-type, products and one for subcontractors who deliver more complex subsystems, services and products under a variety of contract types. In our view, a single supplier rating system does NOT incentivize both communities because the focus of a company's assessment of the former is mostly on quality and adherence to delivery schedules while the performance analysis of the latter is much more subjective and complex. The Navy must recognize this difference in developing the appropriate incentives for an SSS.

The term "Business Relations" is too subjective and should be deleted from the evaluation criteria.

We agree that teams are needed to provide the appropriate assessment of suppler performance. In our experience, at a minimum, teams should be comprised of program managers, program general managers, contracts managers, quality managers and the applicable subject matter experts.

We recommend providing the performance rating and feedback to suppliers on a quarterly basis. Each quarter, on subcontracts greater than $1 million, performance assessment is made based on published criteria. The more frequent the supplier assessment, the more meaningful and, if needed, correctable, the assessment is.

Further, companies use and we recommend to the Navy that the assessment process allow for feedback between the Navy and the supplier. It is in the mutual best interest when both the customer (i.e., Navy) and supplier are on the same page and fully understand the supplier assessment. We recommend that initial assessments be provided to the supplier and a 3-week response/ discussion period ensue where a supplier can challenge or seek more information regarding the Navy's performance assessment. While it is ultimately the Navy's decision on the final assessment rating, this open dialogue is critical to an effective rating system.

We recommend that supplier evaluations be completed more frequently than CPARS are currently issued. Quarterly assessment provides real-time, meaningful performance data that can be acted upon to effect real performance improvement, if needed. Basing incentives on performance during multiple performance period results in a more meaningful relationship between the performance and the incentive. To this end, companies use trend data to determine the supplier rating and associated incentives; for example, a supplier who has 4 consecutive quarters in the Dark Blue 4-star Cateogry would be eligible to receive greater incentives. A suppler with 4 consecutive quarters with 4-star rating in Quality and a 3-star Purple rating would also receive some incentives, but less than the Dark Blue 4-star performer. Incentives for top rated suppliers are often tiered – incentives increase depending on consecutive quarter ratings in the top categories. For example, the Navy might consider tiered incentives within the Top 3-star Purple and 4-star Dark Blue categories.

It is not clear how the SSS designation would apply to a contractor who performs as a major subcontractor under another's prime contract. We recommend that benefits/incentives of the top 3- and 4-star rating be provided to major subcontractors, even if the prime contractor itself is not a superior supplier.

We recommend that Navy be clear that the performance evaluations and interim ratings of one contractor are not shared by the Navy with others contractors. Given the complex systems, risks and management challenges taken on to provide national security assets for our warfighters, even the best suppliers can face performance challenges. While a supplier is working to improve and turnaround performance issues, these challenges should not be shared with competitors. As we noted above, an annual public recognition of top superior suppliers can be made based on those published criteria (.e.g., 4 consecutive quarters of 3- and/or 4-star performance of a business unit's portfolio of Navy contracts).

Finally, we recognize that the SSIP addresses company capabilities and is not procurement specific. However, the application of the SSS designation to any future procurement for architect and engineering services could create a potential conflict with the qualification-based selection procedures of FAR 36.6 for such procurements.

Conclusion

The Navy's proposed SSIP program is largely undefined and has the potential to be anti-competitive rather than beneficial to companies unless carefully formed and administered. As such, we strongly urge the Navy to carefully outline as many of the program parameters as far in advance as possible and subject those parameters to additional notice and public comment. We believe the advantages to such an approach far outweigh the short delay in launching this potentially significant program for both the Navy and industry.

To further assist the Navy, some of our member companies would welcome an opportunity to brief the Navy on their existing supplier assessment programs.

CODSIA appreciates this opportunity to comment on the proposed policy and we would be pleased to respond to any questions you may have on these comments. We also welcome the opportunity to discuss these comments further. Alan Chvotkin of the Professional Services Council is CODSIA's project lead on this case and he can be reached at 703-875-8059 or at Chvotkin@pscouncil.org. Bettie McCarthy, CODSIA's administrative officer, can serve as an additional point of contact and can be reached at codsia@pscouncil.org or at (703) 875-8059.

Sincerely,

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