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NAVY DEPARTMENT ORGANIZATION FOR PROCUREMENT
1 February 1946.

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GENERAL ARMSTRONG:

Gentlemen, we shall continue indoctrinating officers of the Army with the principles of organization and methods of operation of the Navy. Possibly the Army can get a lot of good points from the way our sister service operates. At all events it is, you have already observed, a little different from the way we operate in the Army. It does not mean it is a better or worse way. You can decide that question yourself.

But we have been looking forward in the College to learning more about the Navy organization and methods. The Navy, some people in industry seem to think, did a better job than the Army. I would say that we have to look at the good points in both methods, analyze the results, and see where changes and improvements can be made in the light of the success or failure of either one of the services.

The speaker this morning was born in Texas and therefore belongs to that part of the United States that won the war, apparently. He is a graduate of Princeton. He has taught, and he has had a great deal of experience in civil life with, the kind of work he did in the Navy. He has had a particularly suitable background for it. Today he is the Acting Chief of the Procurement Branch in the Office of the Assistant Secretary of the Navy. His subject is "Navy Department Organization for Procurement". Gentlemen, Captain Andrews, U.S. Navy Reserve.

CAPTAIN ANDREWS:

Gentlemen, I assure you it is a privilege to speak to the officers of both the Army and the Navy. I greatly appreciate the honor.

The subject that I have been assigned to discuss is the Navy procurement organization. I want to go back a little bit behind the organization and give you the reasons for its development.

As you can well imagine, the legislation under which the Army and the Navy operate is the most important factor in determining the policy which will be adopted by the Army and Navy for their procurement. The policy which is adopted is the means by which or through which the organization is developed. Therefore, I want to touch briefly on the procurement legislation for the Army and the Navy.

As you perhaps know, we have operated under the War Powers Acts during the present emergency. These acts have given all the services very great latitude not only in the negotiation of contracts, but also in the type of contracts used for a particular procurement. When these War Powers Acts expire, or are repealed, unless we have something to take their place, we will be forced to go back to the competitive bid statutes-- basically Article 3709.

The procurement legislation is based upon competitive bid statutes going way back to 1869. Our basic legislation was enacted about that time. There have been grafted on to the basic legislation exceptions, modifications and interpretations by the Comptroller General and other governmental agencies to broaden that legislation in some fields. But it was never broadened to the extent that we have broadened it during the War Powers Acts.

It was about two and a half or three months ago that Mr. Hensel (The Assistant Secretary of the Navy) asked me to prepare the recommendations for the Navy postwar procurement policy and for the organization to implement that policy. At that time I pointed out to Mr. Hensel that the legislation under which we would be forced to operate was the keystone to the whole problem and that we should make a study of the legislation to see if it could be revised and brought up-to-date. This was also included in the task that was assigned to me and to Mr. Neals, General Counsel for the Navy.

We used the Procurement Policy Board, which was set up by Mr. Donald Nelson under the War Production Board. We had here an instrument through which we could work. This Procurement Policy Board consists of a member from the Army, the Navy, the Maritime Commission, Treasury, Smaller War Plants, OPA and WPB. Through the Procurement Policy Board we began the struggle of trying to develop one procurement statute that would meet the requirements of all the procuring agencies, that is, the Army, the Navy, Maritime and the Treasury, those being the main ones.

After about two and a half months of very hard work, just last week we finally agreed, the Army, Navy, Maritime Commission, the Treasury and Smaller War Plants, on one statute, which we hope to be able to have the Congress enact.

That statute, as drafted, is a compromise. There are some things in it that the Army wanted that the Navy was not particularly anxious to have. There are certain things in it that the Navy wanted that the Army was not particularly anxious to have. The final result is, I think, a statute which will meet the needs of the Army and the Navy and the other agencies. This is the first time in all our legislative history that we have had as many agencies all saying: "This is the one bill that we want. If we can get that bill, it will do our job".

I want briefly to touch on the bill, because, as I say, it is the instrument that will shape our policy, and then our policy will be the means by which we will shape our organization.

In the special committee of the Procurement Policy Board we drafted two bills--one we call the A Bill and one call the B Bill. The A Bill is a very short bill, which in substance provides that the basis of procurement shall be the competitive bid statutes and the competitive bid procedure except in those cases where the chief of the agency--we used the term "chief of the agency" to cover civilian agencies--determines that it is in the interest of national defense and sound business judgment to allow the negotiation of contracts.

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The A Bill called for very broad authority. We call that the "broad bill". We limited in the broad bill or the A Bill the delegation of that power; and the determination of whether a contract should be negotiated or not to a very high level, to the secretary level.

We ourselves thought that the A Bill was too broad and that it would have two results if it were passed: one, that there would be less uniformity in the exercise of this broad power by the agencies; and, two, this lack of uniformity in the end would defeat the purpose for which the bill was designed. Therefore, we also drafted the B Bill, which we call the "specific exception bill." That is the bill that we very decidedly want, and that is the one I first want to take just a few minutes to discuss.

This B Bill sets forth the same first statement; that advertisement and competitive bidding shall be the basis of Army and Navy procurement except in certain following exceptions, where negotiation may be used. And, briefly, I want to touch on those following exceptions.

The first one provides for the occurrence of a national emergency. It, in substance, is putting into the statute now the War Powers Acts; so that, if we do have another national emergency, we do not have to go through the painful process of hurriedly enacting war power legislation.

The second exception is permissible when public exigencies will not admit delay. That is not novel, and the competitive bid statutes have contained such a provision for many years.

The third exception provides for purchases under one thousand dollars. There have been various limitations on the right to negotiate purchases without advertising and competitive bidding. Some agencies are now limited to fifty and some to twenty-five dollars. The Navy limit is five hundred and I think the Army is five hundred dollars. We raised that limit to one thousand; so that the Services can buy anything under a thousand dollars without advertising and competitive bidding.

The fourth exception relates to personal services. That also has been an exception in the competitive bid statutes, because it has long been recognized that you cannot buy personal services by competitive bidding.

The fifth exception covers purchases outside the United States to be used outside the United States. That is primarily a Navy requirement. For example, when a ship puts into port in some foreign country and something has to be repaired, they do not have to resort to competitive bidding. They may buy what they need according to the customs of the country.

The sixth exception relates to medical supplies, medicines and so forth. This was included at the request of the Army. Such supplies in varying degrees have been the subject of negotiation in the past.

The seventh exception covers the purchases for authorized resale in PXs and ships service stores where "Name brands" are bought. Those are the first seven exceptions, which are not broad in scope and have been more or less covered by prior statutes. Exceptions eight, nine and ten are broader and the authority to use these is more limited than for the first seven.

So far as delegation of the right to use these first seven exceptions is concerned, they may be used by the contracting officer or one responsible for the procurement. The next group, eight, nine, ten and eleven, contains broader authority; and delegation for the use of these powers is restricted at a higher level--the Bureau Chief level or the Chief of the Technical Service level.

The eighth exception relates to proprietary or other items where it is impractical to secure competitive bids. There may be only one builder or one manufacturer of the particular material and to secure it by competitive bidding is impossible. It takes more than one to compete.

The ninth covers experimental, developmental or research work or supplies therefor. Again I wish to stress that it is impossible to procure research through competitive bidding. For example, the Navy or the Army may have some idea of what it wants in some entirely new field of science. Then upon that conception of the "idea" the Navy or the Army must go to the right concern, it may be the Massachusetts Institute of Technology or some other technical organization, and work out the procurement of the "idea" by negotiation. Procurements to transform "ideas" into new weapons are not possible by competitive bidding.

The tenth exception involves procurements where security would be compromised--secret and confidential matter such as another "Manhattan Project".

The eleventh covers standardization of equipment and spare parts. For example, let us take a battleship that has four General Electric shafts in its propulsion equipment. Suppose it is damaged in battle and one shaft is destroyed. It is perfectly obvious that it is better to replace that shaft by negotiating a contract for another General Electric shaft rather than to get a Westinghouse shaft by competitive bidding and then have the ship with one Westinghouse unit and three General Electric units.

The last two or three exceptions are the broad ones. The use of these in the bill is held to the secretary level.

Exceptions twelve and thirteen control where a reasonable price or suitable quality cannot be obtained except through negotiation. In such cases it must be determined at the secretary level that negotiation is appropriate. The fourteenth exception in the "B Bill" covers those situations where availability of a plant for this exception makes it possible to use negotiations as a dynamic force in national preparedness. If the Army wants to keep Curtis-Wright in business or the Navy thinks it

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essential to keep United Aircraft or some company like that in business as a going concern, it may be necessary to resort to the negotiation of specific contracts with those companies in order to keep them in existence in case of a future national emergency.

The fifteenth and last exception preserves the right to place contracts by negotiation when otherwise specifically authorized by law. Under it, one exception would be the Aircraft Procurement Act of 1936, wherein the right to negotiate contracts has already been enacted into law.

With that background of the legislation and summarization of the exceptions in the B Bill, I want to take up the future procurement organization of the Navy Department as we plan it at the present time.

The organization is based upon the assumption that the Navy will get the legislation that it requires.

So much for the legislation. We now come to the statements of policy that the Navy hopes to put into operation in its post war procurement. There are seven of these statements of policy.

The first statement of policy is the simple statement: "It should be the policy of the Navy Department to award contracts by negotiation where national defense or sound business judgment dictates its use. In the award of other contracts competitive bidding should be used.

There are various degrees of negotiation. You may ask for informal quotations and on the basis of those informal quotations may negotiate a deal. During the war, under the War Powers Act, we frequently told the contractor, "We are asking you for a quotation. This quotation does not bind or obligate the Navy in any way. We may award this contract to you if that quotation is low enough. If your quotation is not low enough, we may not negotiate further with you, because those who submit the low quotations will be the ones to be first considered and a negotiation with the contractor submitting the lowest quote may result in placing the contract with that supplier at a figure lower than his original quotation".

The next statement of policy covers the use of various types of contracts. Under competitive bidding we only have the fixed price contract. That is the only tool we have. Through negotiation of contracts and through the lessons that we have learned we have developed several different types of contracts. We now have, besides the fixed price contract, the estimated cost-plus-a-fixed-fee contract, the maximum-price-fixed-price contract, the fixed-price-incentive contract and the letter of intent.

I am going to discuss, I am told, at some later date the estimated cost-plus-a-fixed-fee contract and the fixed-price-incentive contract so I will, therefore, touch them briefly here. The fixed-price contract is simple and will be the type most used by the Navy. In this type of contract the contractor agrees to do the job for a fixed sum of money and that is all there is to it.

The estimated cost-plus-a-fixed-fee contract is one wherein the best estimate possible is made of the cost. Then based upon that estimated cost the Navy agrees upon a certain fee for the contractor. The fee, by law, cannot exceed seven percent of the estimated cost. If we agree on a fee of seven percent of the estimated cost and the actual costs are twice that much or one-half that much, the fee will still be the same dollar amount or seven percent of the original estimated cost.

In the Navy we worked out an incentive on a cost-plus-a-fixed-fee contract. If the contractor did a better job than the estimated cost, he got a bonus for doing the better job. In no event could his fee and bonus exceed seven percent of the estimated cost.

I hope next to discuss the fixed-price-incentive contract. That contract is a little more complicated than the others; but in the end it, I think, is the best solution for long-range production contracts. Briefly it is this:

After a careful negotiation based on all available cost and agreement as to a ceiling price is reached with the contractor, and he agrees to do the job for that price, if his costs go over that, he loses one hundred cents on every dollar by which they exceed the ceiling price. If he gets his costs below that ceiling, the Navy will pay him, as his profit, twenty cents out of every dollar that he gets below the ceiling, and the Navy gets back eighty cents out of each such dollar reduction in cost. In order for the contractor to make each twenty cents in profit, he must save the Navy eighty cents.

Then, of course, we have the letter of intent. When the history of the war is written, the letter of intent is going to stand high on the record of those things which contributed toward the winning of the war. I do not think there is much need for the letter of intent during peacetime; but it is a very handy tool, and I think we should have it. It is most valuable to get a contractor started towards production before the final deal can be made.

The next statement of Navy policy deals with inspection of plants and audit of the books of the contractor. This authority is contained in the Aircraft Procurement Act of 1926 for aircraft construction. It is also in the Second War Powers Act. However, we are not asking in the proposed legislation for a continuance of the right to inspect plants or audit the books of manufacturers except as it exists in the Aircraft Procurement Act.

The reason we are not doing that is because in peacetime we feel that industry would strenuously resent it and Congress would oppose it. We think we can get along without it, provided we insist on one thing. Namely, that in those contracts where such authority is necessary, the cost-plus-a-fixed-fee contract or the maximum-price contract or the incentive contract, we get that right of inspection and audit of books by contractual provisions--by including specifically in the contract an article that the contractor thereby grants the Navy Department or the War

Department the right to inspect the plant and audit the books. We are not asking that right by statute, but we are stating in our Navy policy that in those contracts where that information is necessary we must have that right by contractual provision.

The fourth statement of policy is that the Navy should not seek to recapture excessive profits by renegotiation. In other words, we say we should not, in peacetimes, have over-all renegotiation of Army and Navy contracts. The legislation that I have discussed does not provide for any recapture of excessive profits through renegotiation. We will have to stand or fall on the job we do through competitive bids or through negotiation or through specific contractual provisions for recapture.

The fifth statement of policy is one which deals with advance and progress payments. Some agencies have had the right to make progress payments, I think, in some instances since 1890. The Navy has had the right to make advance payments in the Navy since 1911. The Army, I think, got its authority for advance payments somewhat later than that. We are not seeking in the legislation, nor are we advocating in the Navy policy, the authority to make V-loans of any kind. These are outright loans to the manufacturer. But we do feel it essential and we do ask in the legislation for the right to make advance payments. The constantly increasing importance of Research and Development is the reason for this. The best that the Navy and the Army can be expected to do in maintaining a scientific research organization is to maintain men in the various fields who are sufficiently well informed scientifically to recognize the problems that are going to confront the Navy and the Army. In some fields the Army and the Navy will have outstanding scientists who are as great as or greater than those in industry. Generally speaking industry does not have the scientific or engineering staff in one company that knows all the fields of scientific knowledge nor can this be expected of the Services. Thus, when a particular problem of technical significance comes up, the Army or the Navy in their engineering or in their technical organization will have one or two or a group of men who are able to say, "This is the problem". "If we can solve this problem, it will be a great step in the right direction". They suggest, for instance, that M.I.T. has the organization to solve it. The Service cannot go to M.I.T. and ask for a competitive bid to make an "idea" or a problem into a reality. If you go to M.I.T. to negotiate a contract, they may say, "We are sorry, gentlemen, but this will take one hundred thousand dollars. By our charter we are limited in the use of our funds. We cannot set aside one hundred thousand dollars to do this job". This whole project may be abandoned unless the service can make an advance payment. So we provide that under certain circumstances where the Secretary of the Navy or the Assistant Secretary thinks it is appropriate, advance payments can be made to industry, or educational institutions if they really need the money to carry on the project. However, it is to be the policy of the Navy Department not to make these advance payments unless they are absolutely necessary.

The sixth statement of policy deals with insurance and bonds. It was the policy of the Navy Department during World War II not to require

a contractor or a subcontractor having custody over Government-owned material to insure the Navy against his own negligence or against willful acts of any of his employees.

The seventh statement covers coordination of procurement between the War and Navy Departments. In my opinion that is a very important statement of policy. We made great progress in joint procurement as the war developed. Few people realize how much of the Navy's supplies were brought by the Army and how much of the Army's supplies were bought by the Navy.

Briefly, we employ three methods of joint procurement. We employ an organization where one service buys for itself and for the other service. That is what we call cross procurement. An example of that is that the Navy generally speaking bought fuels and lubricants for the Navy and the Army. The Army generally speaking bought subsistence supplies for the Army and the Navy.

Joint procurement is typified by the setup in the Navy for medicine and surgical supplies, where we have really a joint operation. There is a staff of Army officers and Navy officers operating as a unit. They buy anything that the Bureau of Medicine and Surgery wants or that the Army wants. All requirements go to that joint operating unit and they do the procurement for the Army or the Navy.

The third type of joint procurement is called the collaboration of buyers. That method employs two separate staffs geographically close together, like the Army and Navy textiles office in New York. The officers of the Army and Navy buying blankets, for instance, are all on the same floor in the same building; they are constantly in touch with each other on prices, contract terms, deliveries, requirements, etc.

So much, then, for the policies that the Navy hopes to follow in postwar procurement.

If that policy is followed, we then come to the Navy's postwar procurement organization. Very briefly, it is a continuation of the organization in the Navy that was developed during the war. Prior to the directive of 13 December 1942 procurement in the Navy generally speaking was centralized in the Bureau of Supplies and Accounts. The various technical bureaus that wanted material purchased placed requisitions on the Bureau of Supplies and Accounts. The Bureau of Supplies and Accounts then carried on the purchase functions of that procurement.

Because of the tremendous increase in procurement at that time there was a slowdown in the placing of the orders and in the negotiation of deal

in the Bureau of Supplies and Accounts. On 13 December the Secretary revised the procurement organization of the Navy and, briefly, gave to the technical bureaus the right to determine what materials they would buy and to set up the organization for buying that material. All other material was bought by the Bureau of Supplies and Accounts.

That meant setting up in the technical bureaus a purchase organization, a legal staff, and so forth to administer the contracts and similar allied activities.

Prior to the 13 December directive if the Bureau of Ships wanted particular items, a paper had to be written; it had to be sent to the Bureau of Supplies and Accounts; and the Bureau of Supplies and Accounts had to act on it. If there was any change in the specifications, this had to be done by memoranda back and forth. At one time there were one hundred officers in the Bureau of Supplies and Accounts, I am told, whose sole duty it was to keep up with the incoming and outgoing requisitions of the bureau.

After the 13 December directive each bureau did its own technical procurement.

The basic decision, then, for the postwar Navy organization is: One, that the technical bureaus will continue the procurement of technical items over which they have cognizance.

Now, when that decision is made, decision has been made which requires a decentralization of procurement. And, as we all know, if the function is decentralized, there must be some coordinating activity to keep things in balance. If all the procurement in the Navy were done by the Bureau of Supplies and Accounts or any other bureau, there would not be this necessity for this over-all control organization. But since we have made the decision that procurement is to be decentralized, it follows that we must have some over-all control organization. That over-all control organization will be in the office of the Secretary of the Navy. It is called the Material Division of the Office of the Assistant Secretary. It is a continuation of the Office of Procurement and Material, which was set up during the war.

The Material Division--and I am only talking now about the procurement function of the Material Division--will contain a Procurement Branch. That Procurement Branch will be responsible for the Navy policy in procurement primarily related to the purchase functions.

The Procurement Branch will be under a chief of that branch. At the present time the chief of that branch is a Supply Corps officer. There are three other branches in the Material Division, one of which will be headed by an officer with shipbuilding, Bureau of Ships, background; another by an officer with ordnance experience, and one will be headed by an officer with aeronautic background. So in the office of the Secretary in the Material Division we will have a team under the chief, a Supply Corps officer, an Aeronautics officer, a Ships officer, and an Ordnance officer.

The Procurement Branch will have a Negotiation Section, under the Chief of Procurement. That Negotiation Section will continue the work that was done by the Negotiation Section during the war. Negotiators will be assigned to the various bureaus to assist the bureaus in the negotiation of their contracts.

During the war these negotiators were in the bureaus continuously, and they assisted the bureaus continuously in the negotiation of contracts. It is contemplated in peacetime that there may be some variation of that procedure. The bureaus will have their own purchase officers; and, from time to time, if the bureaus request a negotiator to help them on a large procurement, a negotiator from the office of the Secretary will help them. Or, if the office of the Secretary determines that a particular procurement is one that may shape policy or be extremely important, it may advise the bureau that it is sending one of the negotiators to assist in the negotiation.

The negotiators may be in the bureaus all the time or they may be back at the Procurement Branch, going to the bureaus from time to time. But the bureau organization itself will consist of the contracting officer of the bureau, and under him he will have a purchase section, responsible for the purchases of that bureau.

The contracting officer will also have for his assistance a bureau counsel. The bureau counsel will be concerned primarily with procurement legal matters, and is not to be confused with the Judge Advocate General's Office of the Navy, who is responsible for all Navy general legal problems.

These counsel of the bureau will be there permanently. They will only deal with procurement matters, with the drafting of contracts, with the preparation of special clauses, with the administration of contracts and so forth.

There will be an Office of General Counsel in the Assistant Secretary Office of the Navy or in the Secretary's Office of the Navy, which will be the main office for the various bureau counsels. If a matter of extreme importance comes up, the Bureau Counsel may refer that to the General Counsel of the Navy for his determination.

So the bureaus will have the contracting officer, the Purchase Section, and the Bureau Counsel. The Material Division will have a Procurement Branch, as well as three other branches.

The next section in the Procurement Branch is the Contract Clearance Section. This is a continuation of the function that was set up in 1941 or 1942, whereby all Navy contracts over two hundred thousand dollars must be approved by the Secretary of the Navy or the one to whom he has delegated that authority before an award of the contract can be made.

That sounds like putting a veto power in the hands of the Secretary to say that the chief of the bureau or any other contracting officer of

the bureau cannot award a contract over two hundred thousand dollars without getting prior approval. In substance it is veto power. I think the veto power should remain in the Secretary of the Navy, who has the ultimate responsibility. But this contract clearance function during World War II was not used as a veto power. I do not believe any of the bureaus could point to a single case where there was a veto of their procurement. True, there were times when a procurement was held up a few days, when they were told that the Chief of Procurement thought they could make a better deal and would like to have them try to make a better deal, so that was done.

Contract clearance is a two-way street, and the bureaus have realized that the gain from contract clearance, the many benefits, outweighed greatly the delay that was entailed. There was a delay of about one week, normally speaking, between the preparation and the clearance and the award of the contract; and that could be speeded up if the situation really justified it and clearance could be obtained in a few minutes if necessary. That contract clearance function kept the Secretary's Office aware of what was going on at all times in Navy procurement. It is essential for proper coordination of the activities of the various bureaus.

And, more important even than that, a particular manufacturer might be exerting very great pressure on one bureau, because of the pressing need of that bureau, for a special clause or for some special consideration. If the bureau yielded, the next week he was over in another bureau saying "So-and-so gave us this clause. Why don't you do it?" If he could get an entering wedge in one bureau, he would then be in a position where he could use it as a lever on all the other bureaus. Contract clearance was a method by which the bureaus were able to present a united front to industry, and to hold the line in those special cases. I think the bureaus realized that; and, although some of them have complained from time to time about contract clearance, generally speaking they are in favor of it.

Within the Contract Clearance Section of the Procurement Branch there is a Review and Statistics Section. This Review and Statistics Section has the primary duty to keep the Secretary advised of the types of procurement that the Navy was making. This Review and Statistics Section's primary purpose will be to keep the Secretary and the bureaus advised at all times of the status of procurement; in other words, how many developmental contracts are outstanding, who the contractors are and where they are located; how many cost-plus contracts the Navy has, where located, and what the total amount is; how many incentive contracts are outstanding, where located, who has them, and what the amount is. In that way the Secretary is advised of the types of contracts outstanding, the dollar amount of those contracts, and the geographical areas in which they are placed.

Also the Review and Statistics Section will keep the Secretary advised on the broad areas where negotiation was being used and where competitive bidding was being used. For instance, suppose the Navy had been buying towels under competitive bidding over a two-year period and statistics

showed that the Navy was paying ten percent more for towels than other buyers were paying for the same towels. Under these circumstances the Review and Statistics Section would advise the Secretary that competitive bidding was not the solution for the procurement of towels; and that negotiation was the proper method of procurement.

On the other hand, the situation might be reversed. It might be found that the Navy was paying five or ten percent less than anybody else was paying for towels when we were using competitive bidding. Certainly there would be a case where the Navy would continue competitive bidding.

To sum up, this briefly is the procurement organization of the Navy. We have the bureaus, that have cognizance over technical material. We have a contracting officer in the bureau, who is responsible for the procurement in that bureau. He is in charge of the Purchase Section of the bureau, consisting of Bureau of Personnel, who are responsible for carrying out the Navy purchase policy as announced. We have the Office of Counsel, for procurement legal matters. Then in the office of the Secretary we have the Material Division and within this division there are the four main branches, one of which is the Procurement Branch. Within the Procurement Branch there is the Negotiation Section, the Contract Clearance Section, the Review and Statistics Section and the Insurance Section.

We are confident that these policies and this organization will make it possible for the Navy to continue the effective use of the lessons we have learned by wartime procurement.

I want to leave just a few more thoughts. Then I will be through.

It is easy to say that competitive bidding is the natural solution; just let the law of supply and demand take its course come what will, and the fellow who is the low bidder gets the business. That is very true, and it is a very efficient method of production, provided there is competition for the business and to have such competition there must be three factors and all present: one, there must be exact specifications, so that everybody knows what he is bidding on; two, there must be a product that is susceptible to production by many people, whether it is a manufactured product or a supply item; three, it is necessary to be in that phase of the business cycle where there is real, anxious competition to get the business.

If we do not have all three factors, competitive bidding is a snare and a delusion, because there cannot be real competitive bidding unless all three factors are present. When all three factors are not present, the best results are obtainable by negotiating a contract with one of the several available suppliers or, if there is only one supplier, with that supplier.

Then there is this other thought that I want to leave with you: The Navy and the Army are going to be greatly concerned with technical procurement. I am not worried about the bacon, beans, shoes, shirts and similar things; but I am worried about the procurement of supersonic planes, guided missiles, atomic power, and electronics.

Frequently such items do not start with clear specifications. They start out when the "idea" is conceived someone in the navy must know what institution or company can best develop that idea and engineer and design it into a piece of usable equipment. The institution may be M.I.T. or one of a number of universities or it may be a large or small company. In this type of procurement there are no formal specifications. There are only performance specifications and the only suitable contractual form maybe a letter of intent. Then, as the project progresses satisfactorily, we may convert that letter of intent into a cost-plus-a-fixed-fee contract, which still is a type of deal where the contractor cannot lose any money.

Then after the development of the "idea" is complete and the usable item has been tested it may be decided that the service wants large quantities of them. The production contract may be let on competitive bids or it may be a negotiated fixed-price contract or an incentive contract. Thus, the "idea" has developed to reality by the use of the letter of intent and a cost-plus-a-fixed-fee contract; and the production of many of the pieces of equipment has been accomplished by fixed-price contracts. The point is that "ideas" cannot be bought by competitive bidding--they must be bought by careful negotiation with the best qualified source to turn the "idea" into the most advanced weapon, material or device.

I think that covers, so far as I can, the Navy's postwar procurement organization and the proposed Army and Navy procurement legislation.

Thank you very much.

GENERAL ARMSTRONG:

Captain Andrews, I am in complete agreement with you about the importance of the letter of intent as an instrument of procurement. "Letter of intent" is almost self-explanatory; but I think that, nevertheless, the Captain can give you a few words on it to expand the knowledge that you gentlemen have.

CAPTAIN ANDREWS:

The letter of intent is just what it says. It is a very simple instrument. It is addressed to a contractor. After some discussion with him, when sure that he can go ahead with the job, or reasonably sure, the Navy Department sends him a letter of intent, which says, very briefly, "It is the intent of the Navy Department to enter into a contract with your company for such-and-such material. Until this letter is converted into a formal contract you will be allowed to spend so many dollars with the approval of the inspector".

The letter of intent when converted to a contract would be sometimes converted into a fixed-price contract and sometimes into a cost-plus-a-fixed-fee. But in the latter letters of intent we do not generally state what type of contract it will be converted to.

Some letters of intent provided that the contractor shall receive a profit in case the letter of intent is terminated. Some provided that he shall not receive a profit.

What the letter of intent did, it made it possible for the contractor to order material and get started on the job before he or anybody else knew what the cost would be; sometimes before he or anybody else really knew exactly what he was going to make.

The big ship program which started in 1940 and ran through 1945 was started through the use of letters of intent. We had billions of dollars of ships under way and nobody knew what the cost was going to be. Yet the manufacturers and the shipbuilders were building those ships. Then, before the ships were finished, long before they were finished, the contractors knew something about what their costs would be and the Navy also knew more accurately what the costs would be. Then we converted those letters of intent sometimes into cost-plus-fixed-fee contracts, sometimes into fixed-price contracts, and sometimes into fixed-price-incentive contracts.

A STUDENT:

I wonder if you would mind saying a little bit more about joint procurement, as to the progress that is being made and what you think the final answer is going to be on that.

CAPTAIN ANDREWS:

I think we are going to continue that program so far as it is possible to do so.

We must realize that we do not want to get into technical compromises on joint procurement. In other words, we do not want to be in a position where a five-inch gun is made to almost meet the Army's needs and the Navy's needs at the same time, but is not just right for either one. This gun may do the job fairly well for the Army and fairly well for the Navy, but it will not do just the job that is wanted by either one of them. I do not want to see compromises on technical equipment or weapons.

Our field of joint procurement is limited to that extent. But where we have medical supplies and fuels and lubricants, where we have lumber, bacon, beans, potatoes and similar things, I think it is a very sound step forward to have those procurements done in one of three methods: By cross procurement, where one Service does the purchasing for the others; or by joint procurement where a procurement center is set up like the medical organization in New York, where there are Army and Navy officers doing the job for both; or, third, by collaboration of buyers, as we do in the textile office in New York.

A STUDENT:

Would you rule that out altogether on technical supplies?

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CAPTAIN ANDREWS:

No. I would not rule it out. I do not want to give that impression. But I think that it should be approached quite cautiously. We do not want to make compromises in our technical equipment.

A STUDENT:

I think a large number of army binoculars were turned over to the Navy, old army field glasses of World War I, and the Marine Corps was supplied with them during the entire war. They were interchangeable for the same size and power.

CAPTAIN ANDREWS:

Yes. You can make, I think, compromises there without destroying the effectiveness of materiel for either service. What I have in mind is a compromise between land-based fighters and carrier-based fighters. We do not have to have folding wings on land-based fighters, but we must have them on carrier-based fighters. So it might be conceivable that someone would say, "Let us buy all planes with folding wings". We would pay a price for the folding-wing fighter plane for the Army that is not required. Those are the kind of technical compromises that I do not think will be made and that I think should not be made.

A STUDENT:

Captain, do you not think you can go a little further than you go now? I am thinking about the fact that the Navy and the Army do agree on the caliber of small arms weapons, but do not agree on the caliber and range of artillery weapons. I do not think from the professional point of view you will save a lot of money, particularly in ammunition production, in combined ammunition procurement with the Navy for, say, 150 instead of 6-inch or 5.7 instead of 5 inch or vice versa.

CAPTAIN ANDREWS:

I think there again the technical men in the using service should have the final say. We can not get a perfect solution to this problem. But, if we go back to industry we will find the answer. I think we will find that in industry the purchasing organizations for the big industrial corporations definitely do not have the power to set the type of products that will be produced. The engineers, the draftsmen, and the production people are the ones that say "We want this product; you buy the material for its production".

If the Navy people and the procurement people in the Army can get together and say, "We want this type of gun and this type of plane", we can save money by buying them together.

But we must be careful that we do not put in the hands of the procurement people the veto power on the technical quality of weapons. That is my own personal feeling.

A STUDENT:

That is not the point I am making.

CAPTAIN ANDREWS:

The point you are making is, Why should the Army use a few millimeters or centimeters difference in their shells from the Navy. Is not that it?

A STUDENT:

Yes, or vice versa.

CAPTAIN ANDREWS:

I say this: If the technical people can give a good reason for it, then they should be the ones to have the say.

A STUDENT:

But that has already been done with the small caliber hand guns.

CAPTAIN ANDREWS:

Maybe in the small calibers a slight difference in dimensions does not make so much difference. I do not know.

GENERAL ARMSTRONG:

Gentlemen, we are getting into a technical discussion. That question is at least obsolescent, because in rockets the Army and the Navy are getting together very closely. It is a problem that we are going to have solved for the next war. So I think we are talking about something that does not have too much significance.

Captain Andrews, I want to say to you, sir, that you have given us one of the most lucid and effective presentations--and we have had some good ones--that we have listened to so far. I want to congratulate you on the very splendid contribution that you have made.

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(4 June 1946--200.)S