



DEPARTMENT OF THE AIR FORCE

Office Of The Assistant Secretary

JUL 11 2001

MEMORANDUM FOR ALMAJCOM - FOA - DRU (FOR CONTRACTING)
SAF/AQI/AQP/AQR/AQQ/AQS/AQX
AFPEO/AT/FB/C2&CS/WP/SP

FROM: SAF/AQ
1060 Air Force Pentagon
Washington DC 20330-1060

SUBJECT: Contractor Cost Sharing

Establishing appropriate financial arrangements in contracts with our defense industry partners is extremely important to the Air Force and the Department of Defense. There are various contract funding/finance tools and methods available to fit each unique procurement situation. Sometimes we have relied on substantial commitments from defense contractors to either share in research and development costs or partially fund production and sustainment contracts due to defense budgetary shortfalls. Neither method is an acceptable form of contract financing. This memorandum provides two specific elements of guidance regarding contractor funding of defense procurements.

First, all Air Force acquisition strategies for research and development must follow the direction contained in the attached Under Secretary of Defense for Acquisition, Technology, and Logistics (USD(AT&L)) memorandum. It forbids contractor investment in defense research and development contracts through: 1) use of independent research and development (IR&D) funds to subsidize defense research and development (R&D); 2) cost ceilings that effectively convert cost-type contracts into fixed-price contracts, or 3) unreasonable annual funding increment capping on R&D contracts.

Second, Air Force acquisition strategies shall not require contractor investment in any contract nor serve as a method of covering government funding shortfalls. Air Force source selections will exclude any such contractor-proposed investments from its best value considerations. Air Force solicitations must clearly state that contractor-proposed investments will be excluded from consideration during the source selection process.

This issue requires the full support and understanding of the entire Air Force acquisition community, including users and customers in the operational MAJCOMs. We must eliminate any dependence we may have on contractor investment in Air Force programs.

A handwritten signature in cursive script, reading "Darleen A. Druyun".

DARLEEN A. DRUYUN
Principal Deputy Assistant Secretary
(Acquisition and Management)

Attachment:
USD(AT&L) Memo, 16 May 01



ACQUISITION AND
TECHNOLOGY

THE UNDER SECRETARY OF DEFENSE
3010 DEFENSE PENTAGON
WASHINGTON, D.C. 20301-3010



MAY 16 2001

MEMORANDUM FOR SECRETARIES OF THE MILITARY DEPARTMENTS
DIRECTOR, DEFENSE RESEARCH AND ENGINEERING
DIRECTORS OF DEFENSE AGENCIES

SUBJECT: Contractor Cost Sharing

In order to ensure that the companies the Department of Defense does business with are able to provide innovative, technologically excellent weapons and equipment at affordable prices, we must be concerned about the financial health of the defense industry. Financially sound companies are able to attract the resources and talent necessary to provide best value solutions to warfighters and taxpayers alike.

One of the ways to ensure these companies remain financially sound is to consider carefully the degree of investment they are making in defense programs. In today's environment of reduced defense spending and fewer new program starts, it is short-sighted to require contractor investment in defense research and development contracts. Instead, we should permit contractors to earn a reasonable return on these contracts in exchange for good performance. The only exception to this policy would be unusual situations where there is a reasonable probability of a potential commercial application related to the research and development effort.

Contractor investment in defense programs may take the following forms:

- Use of contractor independent research and development (IR&D) funds to subsidize defense contract research and development.
- Cost ceilings that in essence convert cost-type contracts into fixed-price contracts.
- Unreasonable capping of annual funding increments on research and development contracts.



- Award of development contracts at prices that are known to be less than the contractors' probable costs of performance.

None of these is an acceptable practice. Contractors should not be encouraged or required to supplement DoD appropriations by bearing a portion of defense contract costs, whether through use of their IR&D funds or profit dollars. I have asked my staff to carefully examine the acquisition strategy and execution for ACAT I programs to ensure that contractor cost sharing is not included, and to revise the DoD 5000 series directives to more completely incorporate this policy.

I believe this is a particularly important issue, and I expect the full support of the Military Departments and Defense Agencies to ensure that contractor investment is curtailed.

A handwritten signature in cursive script, appearing to read "E. C. Aldridge, Jr.", written in black ink.

E. C. Aldridge, Jr.