THE UNDER SECRETARY OF DEFENSE

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ACQUISITION,
TECHNOLOGY
AND LOGISTICS

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MEMORANDUM FOR SECRETARIES OF THE MILITARY DEPARTMENTS
ATTENTION: SERVICE ACQUISITION EXECUTIVES
DIRECTORS OF DEFENSE AGENCIES

SUBJECT: Selection of Contractors for Subsystems and Components

The Defense Acquisition System is built on the premise that the government benefits from innovation, flexibility, reduced life cycle costs, and increased quality when Major Defense Acquisition Programs provide for competition at the prime contractor and subcontractor levels. Meeting this objective requires prime contractors foster a robust competitive environment for the selection of major and critical products and technologies as major systems are designed and developed. As the defense industry consolidated, large defense conglomerates are faced more often with the choice of selecting either one of their own divisions or an unaffiliated company to furnish subsystems or components on Department of Defense (DoD) contracts. Because of the potential for bias in such decisions, government insight into the subcontractor selection process may be necessary to ensure fairness and the best value for DoD.

When developing acquisition strategies, program managers and contracting officers shall establish insight into a prime contractor's plan for assembling a team to deliver the required system capability, as well as foster competition. For example, when establishing the contract fee structure, credit should be given for a contractor's effective use of competition to assemble its team. If the weighted guidelines method is used to establish the negotiation objective for profit, the value assigned to performance risk with respect to management/cost control is an appropriate location for providing the appropriate credit.

When an offeror or prime contractor proposes to use its own capability without considering other sources, it should demonstrate why this is in the government's best interest, particularly where similar capabilities exist in outside sources. For example, as a program design proceeds through the system engineering process, close attention should be paid to challenging designs that unnecessarily restrict subsystem or component choices. Also, consideration should be given to investing in alternate capabilities to increase the material choices available for the system design.

When another division of a potential offeror might be a competitor for a potential subsystem, the subcontractor selection process should be subject to government oversight. The solicitation should ask offerors to submit a plan explaining how they will ensure that the subcontractor competition will be conducted fairly and result in the best value for DoD. The government shall review these plans to determine if the offeror has taken adequate steps to ensure that a fair competition will be conducted for a specified subsystem, not to act as a surrogate source selection official or to approve the selection of a particular source. The Defense Contract Management Agency, which is in a position to provide insight into the full range of contractor capabilities, is available to assist with the review of these plans. The plan should address:

- How the offeror will ensure the subcontractor selection process results in the best value to DoD (e.g., the subcontractor selection criteria or evaluation process should not provide any benefit to a company merely because it is another division of the same company as the offeror);
- How the offeror will protect intellectual property rights of unaffiliated companies competing for a specified subcontract;
- Whether any independent advisors will be used in the subcontractor selection process;
- Whether any measures (commonly referred to as firewalls) will be implemented to isolate the source selection personnel from any other personnel in the company that could influence a subcontractor selection for reasons other than obtaining the best value; and
- An assessment of whether the benefits of having two sources for a specified subsystem outweigh the costs.

Similar review of the subcontract selection process after contract award can be accomplished pursuant to Federal Acquisition Regulation (FAR) subpart 44.2, "Consent to Subcontracts," which permits the government to reserve the right to consent to specified subcontracts. This avenue is available if the Components believe that DoD management review at the Acquisition Executive or other appropriate level is necessary for determining consent to significant subcontracts. FAR section 44.202-2 provides that particularly careful consideration of subcontracts is necessary when close working relationships or ownership affiliations between the prime contractor and the subcontractor may preclude robust competition or result in higher prices.

If, after reviewing an offeror's plan for ensuring the best value during the source selection for a particular subsystem or component, government personnel conclude that it is likely that the offeror will show bias in the selection of a subcontractor, they should seek appropriate revision of the plan. If bias cannot be mitigated adequately, then they

should consider procuring the subsystem or component and furnishing it as Government Furnished Equipment (GFE). Furnishing a subsystem as GFE, however, should be a last resort because of the adverse impact of GFE on the total system responsibility assumed by a prime contractor.

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