

Top 10 Block Buy Multi-Year Contract Implementation Questions for Equipment/Service Supplier Provisions

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Switching from traditional year-to-year contracts with suppliers to bulk purchases or multiyear procurements can reduce DoD costs by allowing contractors to improve long-term planning. Multiyear procurement and block buy contracting are special contracting mechanisms used for limited number of DoD acquisition programs, at congressional direction. In planning for future acquisitions, Congress must weigh the potential cost savings and advantages of new capacities in Supplier Base from multiyear procurements and block buy contracting against the flexibility of contracts with option years.

Using Multiyear procurement and block buy contracting more frequently would further reduce flexibility of Congress and DoD for making changes to future years military equipment procurement programmes years in response to changing strategic or budget scenarios. But multiyear procurements, which usually authorise 2-5 years worth of purchases without requiring DoD to exercise contract options for later years, can save an estimated 5-10 percent on contract costs, or even more in some instances.

Under multiyear agreements, DoD can front-load its purchases of components with long lead times, such as aircraft engines, rather than buying each engine with each plane over a number of years. This allows component suppliers to maximise economies of scale associated with batch orders.

Multiyear deals also reduce uncertainty for suppliers, providing more incentive to invest in process improvements at the start of contracts, because DoD must certify at the start that its minimum need for the product won't change over the course of the procurement.

This confidence can permit the contractor to make investments in training workers, or for building, expanding or modernise/optimize capacity of site operations facilities for production of items being procured by DoD under the contract.

Here we outline the main changes proposed for multi-year contracting and advanced procurement together with establishment of new DoD rules. Several advantages result from improved production scheduling, productivity increasing front end investments and economies of scale could be achieved if the restrictions on multi-year contracts were relaxed. Proponents of expanded multi-year contracting have sought a number of advantages including 1) Reduced procurement quotes values 2) Increased supplier productivity 3) Broadening of supplier base.

Advanced procurement has been limited in principle to small quantities of long lead time components for the purpose of shortening the time required to finish assembly of the complete end item. In other words, advanced procurement originally utilised by DoD initially aimed at schedule projection rather than cost savings. Now, however, advanced procurement is perceived

as method for achieving both these objectives, and others as well.

We have proposed DoD consider authorised advanced procurement contracts to: 1) Be used for multi-year advanced procurements with sequential funding, 2) Include raw materiel and parts as well as components, 3) Buy in economic order quantities, 4) Encourage subcontractors to produce at more efficient rates, 5) Empower subcontractors to enter and continue in defence markets in order to strengthen supplier base and improve opportunities to buy competitively.

It appears, therefore, that advance procurement contracts can be used by DoD widely in the future, in both the annual and multi-year form. Advanced procurement contracts in the multi-year form may also be used to either to support multi-year, complete end item contracts or partly to substitute for them as means for achieving production efficiencies and cost savings.

In other words, procurement of complete end items could continue to be handled in the normal way by means of annually funded annual contracts, while multi-year advance contracts could be used to exploit opportunities for production capacity/efficiency and cost savings in purchasing selected inputs to production of the complete end item. Thus, it may be possible for DoD to achieve substantial savings through multi-year advance procurement while continuing to enjoy the advantages of annual contracting for the bulk of a procurement programme.

There is, however, always some risk to DoD bottom line that programmed number of complete end items will not be produced, and therefore the inputs contracted for in advance procurement will turn out to be excess for production needs. The consequences are generally not serious when the advance procurement contract is limited to single year requirements of inputs that are themselves end items, or can be used as spare parts or like some raw materiel, can find a commercial market.

But the risk to DoD of overbuying potentially increases as advance procurement contracts are expanded to provide for additional future years of requirements. And the consequences of overbuying can become more serious as the contract is extended to include “bits and pieces” for which, apart from their role as inputs to end item production there is neither military use or potential to be successful in commercial markets. The achievement of net savings through expanded use of advance procurement will require a careful weighing of these risks and their consequences.

DoD will now be able to pursue a richer set of procurement objectives and in doing so to use a greater variety of funding/contract modes. Annual contracts would probably be used somewhat less frequently, being partly replaced by contracts for multiyear procurement sometimes full front funded but usually funded consecutively to sometimes be used for purchase of major weapons systems.

Advanced procurements will be multiyear as well as annual. Many different combinations of advanced procurement contracts will be possible. These opportunities will probably lead to a period of experimentation by DoD acquisition professionals.

Today, DoD procurement obligations are characterised by a high percentage of full funding and

partial but increasing element of advanced procurement; ie, procurement of items other than complete end items. In the future, unfunded liabilities and liabilities for non-end item can be expected to increase, perhaps only modestly, but possibly dramatically. Careful risk assessments will be required.

DoD may consider pursuit of new/multiple objectives in purchasing major weapon systems and even smaller items like spare parts. As we have highlighted, advanced procurement was authorised only as means of shortening period required to obtain complete end items. Now this method of contracting can be used for objectives as diverse as cost increase avoidance in procuring raw materiel, establishing efficient production rates, and strengthening lower tiers of supplier base.

We have highlighted results of innovative contracting advances in DoD processes designed to open up many new choices for Site Visit Executive in presenting appearance and exercising solutions for future challenging procurement questions:

1. How will existing process direction be revised to implement new broad guidelines we have presented, promoting use of multiyear and advanced procurement contracting?
2. How will critical specifics be used in determination of risk distribution between stakeholders in acquisition process so suppliers are motivated to make required front end adjustments?
3. Will Site Visit Executive utilise discretionary authorities to remove or modify existing requirements that sequentially funded multiyear contracts must address fixed/level prices?
4. If level pricing is no longer required, what kinds of quote profiles can be substituted, and how will they relate to expected cost/quantity models?
5. To what extent should advance procurement substitute for multiyear contracting for complete end items?
6. How should funding options be evaluated for multiyear advance procurement contract models?
7. How will multiyear contracts affect price competition between suppliers in production of items contracted for?
8. How can effective supplier competition be best achieved in multiyear procurement?
9. How will suitable procurements be selected for multiyear contracting, prescribed criteria applied and risks identified of assessing expected cost/benefit tradeoffs?
10. To what extent should multiyear contracting be used to enhance programme stability, as well as to exploit inherent stability?