AMERICAN ECONOMIC LIBERTIES PROJECT

Antimonopoly Proposals for the National Defense Authorization Act (NDAA)

May 2024

The 2025 National Defense Authorization Act (NDAA) is an opportunity for the United States to reintroduce competition into the defense industrial base, into federal contracting, and into the markets for services offered to American servicemembers and veterans.

There is a well-recognized crisis in the defense base, with multiple conflicts putting strain on dramatically weakened industrial capacity. The primary reason for the reduced capacity is that defense consolidation is out of control. Since the end of the Cold War, the more than 50 firms that once made up the U.S. defense base have been reduced to the five prime contractors left today: Lockheed Martin, Boeing, Northrop Grumman, General Dynamics, and Raytheon, (now known as RTX.) In February 2022, the Pentagon released a report that detailed the extreme consolidation in the defense industry, outlined the risks it posed to the country's national and economic security, and identified the number of companies in the defense industrial base as insufficient.

As this consolidation occurred, the rules around federal procurement for defense contractors also changed. They now favor a handful of consolidated prime contractors and are stacked against the government. Prices are often opaque, and charges can be inappropriately billed to the government. Moreover, the government is frequently unable to maintain its own essential military equipment. At the same time, monopolistic middlemen in other industries, like pharmacy benefit managers (PBMs), have been able to change government rules and benefits to degrade the services that American servicemembers receive, by, for example, cutting off their access to independent pharmacies.

This memo outlines a series of straightforward policy proposals to include in the NDAA to fix the federal rules around defense procurement, ensure the government retains ownership and control over critical military systems, and restore servicemembers' benefits. Where legislative text is available for such an amendment, it is included in an appendix.

AMENDMENT TO LIMIT COMMERCIAL PRODUCT OR SERVICE EXCEPTION TO CERTIFIED COST OR PRICING DATA REQUIREMENTS

Explanation: In contexts where a defense contractor faces no effective competition—either as a result of consolidation or where the component is highly specialized—the federal government often lacks a basis to understand the cost and prices for contracts with defense contractors. Normally, contractors are required to submit certified cost and pricing data to the government. But as of now, federal statutes and regulations include an exception for "commercial items." The idea is that, with a private market for the items pricing data is readily available.

Both defense contractors and government contractors more generally have fought meaningful pricing disclosure for decades. In recent years, they've turned to a tortured definition of "commercial items or services." This definition effectively prohibits making pricing disclosures because the definition is so broad that an item or service may qualify for "commercial" treatment so long as it relates to something available in the commercial sector. For example, military aircraft may be labeled as commercial because they are aircraft. Traditionally, before the expansion and exploitation of the "commercial item or service" definition, high value goods and services purchased on a sole-source basis and not otherwise sold in substantial quantities to the general public had to be justified by the submission of certified cost or pricing data.

However, the current "commercial item and services" statutory and regulatory definitions contain no requirement that an item or service, in order to be labeled "commercial," have any actual sales in the marketplace. As such, the exemption is largely used by defense contractors to sell government unique goods and services without providing any meaningful basis for costs or pricing. Under this warped, "anything goes" definition, major weapons systems and subsystems are often sold to the government on a sole-source basis without the contractor providing any cost data to justify price. In some limited circumstances, contractors may provide uncertified data to the government, but this uncertified data provides no remedy if the contractors overstate their costs. The Truthful Cost and Pricing data statute does provide remedies for contract overpricing (referred to as "defective pricing"), but only when the data are certified.

The purpose of this amendment is to require that "commercial item" contracts awarded by the Department of Defense under Federal Acquisition Regulation Part 12 (48 CFR, Chap.1, Part 12) on a sole-source basis exceeding $5 million in value be justified by the submission of certified cost or pricing data under the Truthful Cost and Pricing Data statute(s) so that that government contract negotiators have an understanding of the basis of the contractor's price when there is no competition. This amendment partially restores that concept for sole-source "commercial item" contracts exceeding $5 million while exempting contracts from the requirement where there are substantial sales to the general public, e.g., off-the-shelf items such as furniture, computers, etc.

Legislative Text Available in Appendix A

IMPOSE PROGRESS PAYMENTS LIMITATIONS

Explanation: "Progress payments" are a form of financing provided by the government to contractors on fixed-price contracts, in lieu of contractors having to borrow money from the private sector or use in-house capital.

Progress payments are usually expressed as a percentage of contractor-incurred costs on a specific contract. For example, if a contractor incurs $9 million in costs on a $10 million contract, it may receive progress payments representing a percentage of the $9 million in incurred costs. Progress payment rates have varied over time, from a low of about 75% to as much as 95% for small businesses. On average, large contractors receive progress payments of about 80% of incurred costs, with the remainder of the contractor price (the difference between the agreed-upon fixed price and progress payments already paid) upon completion of the work or delivery of the goods.

Congress has been looking for a way to incentivize better contractor performance by adjusting the progress payment rate. Various Department of Defense officials have suggested lowering the "default rate" for progress payments for large business to 50% of incurred costs. This could include upward adjustments in this rate permitted for superior or exceptional contractor performance, including appropriate and timely disclosure of certified cost or pricing data.

The proposed amendment effectively sets a default progress payment rate of 50% with upward adjustments permitted when appropriate.

Legislative Text Available in Appendix B

COST OR PRICING DATA AMENDMENTS

(DEFENSE AND CIVILIAN AGENCIES)

Explanation: The proposed amendments primarily accomplish two goals. They lower the threshold for which contractors must disclose their estimated costs, and they close a loophole in the civilian procurement statute that had allowed contractors to entirely avoid such disclosures.

For the first, there are two separate Truthful Cost or Pricing Data statutes: one for DoD and another for the civilian procurement agencies. They are similar in most respects but not identical. Regardless, when the government purchases a noncommercial good or service on a sole-source basis exceeding a certain threshold, contractors are generally required to submit certified cost or pricing data. The threshold was raised several years ago, first to $750,000, and then suddenly to $2 million, which represents an increase of 2,000% over the past 30 years. (The initial threshold was $100,000.) This means that for a range of items and services for which contractors previously needed to disclose their costs, now the government simply has to believe the prices it's given. While there may be some justification for raising the Truthful Cost or Pricing Data thresholds based on inflation, an increase of 2,000% cannot be justified except on account of contractor greed. For both DoD and the civilian agencies, the amendments establish a $500,000 contract threshold, meaning that when the government purchases a sole-source, noncommercial good or service exceeding $500,000, contractors must submit certified cost or pricing data.

To explain the second change, during the various bouts of "acquisition reform" in the past several years, contractors were able to have both statutes amended to exclude even sole-source contract awards from the requirement to submit certified cost or pricing data, as long as the government contracting officer had a reasonable belief that the sole-source awardee based its price on the notion that it would have to compete with at least one other contractor. These were often referred to as "competitive, one bid" contract awards. Fortunately, Congress saw fit to effectively eliminate this loophole by amending the DoD statute to require that all sole-source awards subject to DoD's version of the Truthful Cost or Pricing Data statute include the submission of certified cost or pricing data. This dispensed with the hypothetical that another contractor might have submitted its own pricing proposal. However, the civilian agency statute was never similarly amended to close this loophole. The second change made by these amendments is simply to conform the civilian agency statute to the DoD statute.

Legislative Text Available in Appendix C

REINSTATE PAID COST RULE

Explanation: As a part of "acquisition reform," over recent decades, contractors have been able to convince the drafters of the Federal Acquisition Regulation (FAR) to eliminate the long-standing "paid cost rule." This rule simply required prime contractors to have actually paid their subcontractors in cash before submitting invoices or vouchers for subcontractor costs to the government for payment or reimbursement.

The "paid cost rule" should be reinstated. Elimination of the rule serves no purpose other than to increase large contractor cash flows.

Although the elimination of the paid cost rule was done through regulation, the Federal Acquisition Regulation drafting agencies show no indication that they will act. Therefore, the proposed amendment below statutorily requires that the paid cost rule be reinstated.

Legislative Text Available in Appendix D

RIGHT TO REPAIR FOR GOVERNMENT CONTRACTING:

ACCESS TO TECHNICAL DATA FOR WEAPONS SYSTEMS

AND COMPONENT PARTS

Explanation: As with many other areas of the economy, government contractors have opposed the right to repair. The basic thrust is that contractors do not want to share technical data, even for weapons systems, with the government, and prefer that such equipment be returned to the manufacturer for repair or overhaul. This situation is particularly disadvantageous when national security is involved.

Although DoD has taken some steps to ensure basic repair capability, contractors attempt to stymie the department at every opportunity. The proposed amendment provides DoD with unlimited contracting authority to require the submission of technical data and permit its use to repair and maintain weapons systems.

Legislative Text Available in Appendix E.

RESTORE TRICARE COVERAGE FOR INDEPENDENT PHARMACIES

Explanation: TRICARE—the civilian health care program for armed forces personnel, retirees, and their dependents—contracts for pharmacy services through a pharmacy benefit manager. The current vendor is Express Scripts. However, in the most recent pharmacy contracting phase, Express Scripts offered independent network pharmacies terms for participation that are uneconomical for ANY pharmacy, requiring pharmacy operators to choose between serving servicemembers and their families and having a financially sustainable practice. Predictably, as many independent pharmacies opted out of TRICARE, the TRICARE pharmacy network shrank dramatically, by more than 15,000 pharmacies, forcing more servicemembers to use Express Scripts' mail-order service. With its mail-order pharmacy, Express Scripts is both the purchaser and the supplier of pharmacy services, to the benefit of the company's shareholders and at the expense of the government and small-business pharmacies.

Medicaid generally requires that pharmacies be paid on a cost-accounting model using cost surveys for both product reimbursement and professional pharmacist services rendered. Requiring TRICARE to pay pharmacies on the same basis should allow TRICARE to have more confidence that it is paying a fair cost and restore the economics that would allow small-business pharmacies to participate.

The proposed amendment would:

1) Prohibit TRICARE from contracting with any PBM that also owns their own pharmacy.
2) Require any PBM that contracts with TRICARE to meet minimum network adequacy standards and reimburse pharmacies on reasonable and relevant terms based on Medicaid pharmacy reimbursement rates.

SECTION 230 EXCEPTION FOR MILITARY SCAMS

Explanation: Section 230, which provides immunity for online platforms with respect to third-party content generated by its users, allows social media companies like Meta, Twitter, and Tik Tok to avoid responsibility for the content posted by users on their sites. This exemption applies even to scams and other fraudulent behavior that causes financial harm to consumers and small businesses. According to the Federal Trade Commission, Americans lost over $1.4 billion to scams on social media sites in 2023 alone.

Meta, which owns Facebook, Instagram and WhatsApp, has refused to crack down on financial predators using its platforms to target individuals. From allowing fake accounts to run rampant to allowing users to create and share fake links to harvest account information, the company has refused to protect its users. When users submit complaints about specific scams, or detail the financial harm they've suffered because of them, they are almost always sent to a customer service page or ignored.

The so-called military "love scams" are particularly outrageous. These are scammers – which can often be located outside of the United States -- who pretend they are members of the U.S. military, using fake profiles to assume a false identity as a deployed service members to financially swindle unsuspecting members of the general public.

A proposed amendment would:

1) Put a limited Section 230 exemption in the legislation that would allow for social media companies to be held responsible when they fail to take action to put a stop to the theft of the identities of military service members and veterans.

APPENDIX A: LEGISLATIVE TEXT TO

LIMIT COMMERCIAL PRODUCT OR SERVICE EXCEPTION

SEC. __. LIMITATION ON COMMERCIAL PRODUCT OR SERVICE EXCEPTION TO CERTIFIED COST OR PRICING DATA REQUIREMENTS.

Section 3703(a)(2) of title 10, United States Code, is amended by inserting ", unless it is a sole-source product or service with a value in excess of $5,000,000 or the goods or services are sold in substantial quantities to the general public at readily ascertainable market prices" after "commercial product or commercial service."

APPENDIX B: LEGISLATIVE TEXT TO

IMPOSE PROGRESS PAYMENTS LIMITATIONS

PROGRESS PAYMENT INCENTIVE PILOT.

(a) Program.—The Secretary of Defense, acting through the Under Secretary of Defense for Acquisition and Sustainment, shall establish and implement a program, to be known as the "Progress Payment Incentive Program," to establish progress payments contingent upon responsiveness to Department of Defense requests for cost or pricing data.

(b) Purpose.—The purpose of the program is to reward Department of Defense contractors who work with the Department in the pre-award process to prevent excessive costs and establish guardrails against excessive prices.

(c) Progress Payments.—

(1) LIMITATIONS FOR TRADITIONAL CONTRACTORS.—Under the program, the Department of Defense may not award to traditional business contractors progress payments in excess of 50 percent.

(2) EXCEPTIONS.—The Department of Defense may increase the rate of progress payments to 80 percent if the division of the company provides certified cost or pricing data within 30 days of the Department's request for the information. The progress payment rate may not exceed 90 percent.

(d) Definitions.—In this section:

(1) TRADITIONAL DEFENSE CONTRACTOR.—The term "traditional defense contractor" means a contractor (other than an institute of higher education) that is currently performing or has currently performed for at least the one-year period preceding the solicitation of sources by the Department of Defense for the procurement or transaction, any contract or subcontract for the Department of Defense that is subject to any coverage under the cost accounting standards prescribed pursuant to section 1502 of title 41, United States Code, and the regulations implementing such section.

(2) PROGRESS PAYMENTS.—The term "progress payments" means payments provided for under section 3804 of title 10, United States Code.

APPENDIX C: LEGISLATIVE TEXT FOR

COST OR PRICING DATA AMENDMENTS

10 §2306a. Cost or pricing data: truth in negotiations

(a) Required Cost or Pricing Data and Certification.–1) The head of an agency shall require offerors, contractors, and subcontractors to make cost or pricing data available as follows:

(A) An offeror for a prime contract under this chapter to be entered into using procedures other than sealed-bid procedures that only receives one bid shall be required to submit cost or pricing data before the award of a contract if–

(i) in the case of a prime contract entered into after ~~December 5, 1990~~June 30, 2025, the price of the contract to the United States is expected to exceed $500,000; ~~and~~

(ii) in the case of a prime contract entered into ~~on or before December 5, 1990~~after June 30, 2018, but prior to June 30, 2025, the price of the contract to the United States is expected to exceed $~~100~~2,000~~.~~,000; and

(iii) in the case of a prime contract entered into on or before June 30, 2018, the price of the contract to the United States is expected to exceed $750,000.

(B) The contractor for a prime contract under this chapter shall be required to submit cost or pricing data before the pricing of a change or modification to the contract if the price adjustment is expected to exceed $500,000.

~~(i) in the case of a change or modification made to a prime contract referred to in subparagraph (A)(i), the price adjustment is expected to exceed $500,000;~~

~~(ii) in the case of a change or modification made after December 5, 1991, to a prime contract that was entered into on or before December 5, 1990, and that has been modified pursuant to paragraph (6), the price adjustment is expected to exceed $500,000; and~~

~~(iii) in the case of a change or modification not covered by clause (i) or (ii), the price adjustment is expected to exceed $100,000.~~

(C) An offeror for a subcontract (at any tier) of a contract under this chapter shall be required to submit cost or pricing data before the award of the subcontract if the prime contractor and each higher-tier subcontractor have been required to make available cost or pricing data under this section and the price of the subcontract is expected to exceed $500,000.

~~(i) in the case of a subcontract under a prime contract referred to in subparagraph (A)(i), the price of the subcontract is expected to exceed $500,000;~~

~~(ii) in the case of a subcontract entered into after December 5, 1991, under a prime contract that was entered into on or before December 5, 1990, and that has been modified pursuant to paragraph (6), the price of the subcontract is expected to exceed $500,000; and~~

~~(iii) in the case of a subcontract not covered by clause (i) or (ii), the price of the subcontract is expected to exceed $100,000.~~

(D) The subcontractor for a subcontract covered by subparagraph (C) shall be required to submit cost or pricing data before the pricing of a change or modification to the subcontract if the price adjustment is expected to exceed $500,000.

~~(i) in the case of a change or modification to a subcontract referred to in subparagraph (C)(i) or (C)(ii), the price adjustment is expected to exceed $500,000; and~~

~~(ii) in the case of a change or modification to a subcontract referred to in subparagraph (C)(iii), the price adjustment is expected to exceed $100,000.~~

41 U.S. Code § 3502 - Required cost or pricing data and certification

(a) ~~When~~ Required.~~—~~ Cost or Pricing Data and Certification.–(1) The head of an ~~executive~~ agency shall require offerors, contractors, and subcontractors to make cost or pricing data available as follows:

~~(1) Offeror for prime contract.—~~(A) An offeror for a prime contract under this ~~division~~chapter to be entered into using procedures other than sealed-bid procedures that only receives one bid shall be required to submit cost or pricing data before the award of a contract if

~~(A~~(i) in the case of a prime contract entered into after June 30, 2025, the price of the contract to the United States is expected to exceed $500,000;

(ii) in the case of a prime contract entered into after June 30, 2018, but prior to June 30, 2025, the price of the contract to the ~~Federal Government~~United States is expected to exceed $2,000,000; and

(~~B~~iii) in the case of a prime contract entered into on or before June 30, 2018, the price of the contract to the ~~Federal Government~~United States is expected to exceed $750,000.

~~(2) Contractor.—~~B) The contractor for a prime contract under this ~~division~~chapter shall be required to submit cost or pricing data before the pricing of a change or modification to the contract if~~—~~ the price adjustment is expected to exceed $500,000.

~~(A) in the case of a change or modification made to a prime contract referred to in paragraph (1)(A), the price adjustment is expected to exceed $2,000,000;~~

~~(B) in the case of a change or modification made to a prime contract that was entered into on or before June 30, 2018, and that has been modified pursuant to subsection (f), the price adjustment is expected to exceed $750,000; and~~

(C) ~~in the case of a change or modification not covered by subparagraph (A) or (B), the price adjustment is expected to exceed $750,000.~~

~~(3) Offeror for subcontract.—~~An offeror for a subcontract (at any tier) of a contract under this ~~division~~chapter shall be required to submit cost or pricing data before the award of the

subcontract if the prime contractor and each higher-tier subcontractor have been required to make available cost or pricing data under this ~~chapter and—~~section and the price of the subcontract is expected to exceed $500,000.

~~(A) in the case of a subcontract under a prime contract referred to in paragraph (1)(A), the price of the subcontract is expected to exceed $2,000,000;~~

~~(B) in the case of a subcontract entered into under a prime contract that was entered into on or before June 30, 2018, and that has been modified pursuant to subsection (f), the price of the subcontract is expected to exceed $2,000,000; and~~

~~(C) in the case of a subcontract not covered by subparagraph (A) or (B), the price of the subcontract is expected to exceed $750,000.~~

~~(4) Subcontractor.—~~D) The subcontractor for a subcontract covered by ~~paragraph (3~~subparagraph (C) shall be required to submit cost or pricing data before the pricing of a change or modification to the subcontract if the price adjustment is expected to exceed $500,000.

~~(A) in the case of a change or modification to a subcontract referred to in paragraph (3)(A) or (B), the price adjustment is expected to exceed $2,000,000; and~~

~~(B) in the case of a change or modification to a subcontract referred to in paragraph (3)(C), the price adjustment is expected to exceed $750,000.~~

APPENDIX D: LEGISLATIVE TEXT TO

REINSTATE PAID COST RULE

10 U.S.C. xxxx and 41 U.S.C. xxxx -- <u>Reinstate Paid Cost Rule</u>

(a) The Federal Acquisition Regulation shall be amended to require that a prime contractor has actually paid a subcontractor prior to including the subcontractor's claimed costs in any billings.

(b) The necessary amendments to the Federal Acquisition Regulation to implement this section shall be made within 180 days of enactment of this statute.

APPENDIX D: LEGISLATIVE TEXT TO ESTABLISH

RIGHT TO REPAIR FOR GOVERNMENT CONTRACTING

10 U.S.C. XXXX, ACCESS TO TECHNICAL DATA FOR WEAPONS SYSTEMS AND COMPONENT PARTS.

As required by the Secretary of Defense, or any designee of the Secretary, as a condition of contracting, the contractor shall provide to the Department all technical data necessary to repair or maintain the weapons system(s), including component parts.