With all the hoopla surrounding program cost growth and schedule slips, and the resulting calls for “acquisition reform”—and even some **statutory steps** in that direction—one might think there have been put forward some innovative suggestions. Nope. As we **posted** recently, most of the “conventional wisdom” in this area is wrong, and most “reformers” are more aptly **described** as PWACs—Persons Without A Clue.

So it is with a great deal of satisfaction that we can finally point to one recommended acquisition reform step that, if implemented, would save the taxpayers a great deal of money—as well as increasing efficiency within program supply chains. What makes this step even more interesting is that it comes from an unlikely source: the Defense Department Inspector General (DOD IG). Talk about adding value!

Here's the **DOD IG report** that caught our eye and sparked our fascination. It's a report from October 2009, just released (in redacted form) in mid-February 2010. It discusses the volatility of titanium pricing, and suggests some ways in which the DOD could better control the pricing it receives for this commodity. Why in the world would it take auditors to recommend such a fundamental—nay, basic—strategic acquisition approach? But before we get too wrapped up the obviousness of the recommendation, let's look at what the DOD IG had to say.

First, the IG noted that certain contracts (notably the multi-year contract for the Navy F/A-18 E/F Super Hornet) contained economic price adjustment contract clauses. These clauses are designed to provide automatic contract price adjustments based "on changes in the economic behavior of the national economy." Without these contracts, contractors would have to price in the risk that certain commodities would suffer price increases; should those increases not materialize then the contractors would receive a windfall. Essentially, the clauses turn otherwise fixed-price contracts into limited forms of cost-reimbursement contract—but only for the commodity covered and only to the extent that the market price for that commodity moves outside certain bounds, as reported by the Bureau of Labor Statistics (BLS) in its producer price index (PPI) reports.

In this case, the commodity in question is titanium. Titanium is a strong, lightweight metal with an exceptional strength-to-weight ratio, elevated temperature performance, and corrosion resistance. It is used in a variety of applications, most notably in jet engines and airframe components. The IG reported that, in 2007, “an estimated 76 percent of domestic titanium metal was used in aerospace applications.” There are three major domestic titanium suppliers: TIMET, ATI, and RTI.

The IG found that “the BLS producer price index for titanium mill shapes, used in the economic price adjustment clause of the Navy F/A-18 E/F Super Hornet contract, was outdated and subject to extreme market volatility, as it was primarily based on spot market prices. The index was also too narrow to be used in DOD multiyear contracts…”
But the DOD IG had more to say on the subject of titanium pricing.

It reported that “DOD had not effectively mitigated its risk for titanium material price increases… As a result, Defense aerospace weapons systems were subject to higher market prices for titanium material based on supply and demand of titanium in the commercial marketplace.” It provided three root causes for this situation:

1. DOD suppliers of titanium components had not always secured titanium material on long-term contracts and material purchased at market prices carried a significantly higher price that got passed through to DOD contracts.

2. DOD multiyear contracts that used the BLS producer price index for titanium mill shapes were not effective because the BLS index was outdated, primarily based on spot market prices, and too narrow an index.

3. DOD does not have a strategic purchasing program for titanium to leverage buying power, take advantage of economies of scale, and secure prices on longterm contracts when acquiring titanium products.

The DOD IG noted that the DOD requires between 20 and 30 million pounds of titanium annually. Importantly, the Pentagon could save "from $100 million to $300 million annually" if it purchased half of its needs via a long-term contract instead of having its contractors purchase it at market prices. As evidence for that assertion, the IG reported on how the titanium price volatility had affected the F/A-18 contract prices, noting that "The material price increase related to titanium costs for the FY 2007 through FY 2009 performance period was $129 million, which accounted for more than 66 percent of the total material cost increases during that period of performance."

The IG concluded:

DOD was subject to market volatility in titanium material pricing because DOD did not have a strategic purchasing program for titanium to leverage buying power, take advantage of economies of scale, and secure prices on long-term contracts when acquiring titanium products. Also, DOD had limited options when purchasing titanium because of the restriction on the acquisition of specialty metals under title 10, United States Code, section 2533b.

The IG recommended that the DOD adopt a strategic materials management process with respect to titanium, and noted that DOD had requested this step in an April 2008 report to Congress. The IG reported:

The Strategic Materials Protection Board concluded that the National Defense Stockpile should reshape into the Strategic Materials Security Program. They stated that this program could have the programmatic flexibility to efficiently and effectively acquire the right materials and to ensure that essential strategic materials are available to respond to current and future needs and threats, including the ability to more fully project material needs and the ability to leverage the buying power of DOD and other Federal agencies by aggregating materials requirements and negotiating long-term strategic procurement arrangements. In line with the conclusions of the National Defense Stockpile April 2009 Report to Congress, the Deputy Under Secretary of Defense for Industrial Policy, in conjunction with the Administrator, Defense National Stockpile Center, Defense Logistics Agency, should develop a strategic purchasing program for titanium with U.S. titanium producers to leverage buying power, take advantage of economies of scale, and secure prices on long-term contracts when acquiring titanium products.

This is real acquisition reform, folks. This is a relatively simple two-step process that could save the DOD from $100 to $300 million *each year*. That money could go to other needs, or back to the taxpayers. So what is Congress waiting for?