U.S. Department of Defense
Office of the Assistant Secretary of Defense (Public Affairs)

News Transcript

Presenter: Deputy Secretary Of Defense William Lynn, Air Force Secretary Michael Donley, and Undersecretary of Defense for Acquisition Technology and Logistics Ashton Carter **February 24, 2010**

DOD News Briefing with Deputy Secretary Lynn, Secretary Donley and Undersecretary Carter from the Pentagon

BRYAN WHITMAN (deputy assistant secretary of defense for media operations): Good afternoon, and welcome. It's my privilege to bring back to the briefing room three individuals that don't need any introduction, really, but I will anyway: Deputy Secretary Lynn, Air Force Secretary Mike Donley and Undersecretary of Defense Ash Carter.

So as we indicated back to you in September when we released the draft RFP [request for proposal], that we would be back here to finalize that process and to put the final RFP out and to bring it to you in as transparent way as we can and to be available to answer your questions. So with that, we're going to present some of the key aspects of this and then take your questions.

So let me turn it over to Deputy Secretary Lynn. Thank you.

MR. LYNN: Thanks, Bryan.

I'm just going to make some opening comments and then ask Mike Donley and Ash Carter to give you a little bit more detail of the final RFP. But before I even get to the RFP itself, let me talk about the three principles that are guiding this acquisition and that haven't changed from draft to final.

First, this is going to be an objective competition. It's going to be fair, it's going to be open, it's going to be transparent. We -- obviously, there are high stakes in this, both in terms of jobs and revenue, high interest.

We're -- we get buffeted from both sides. We are resisting that buffeting, and we are -- we are going to play this straight down the middle.

Second, this is a best-value competition. We actually looked at the alternative of a low-cost technical -- technically-acceptable approach, and we rejected that approach. By saying best-value does not mean that price is not important. Price is important. Price is very important. But it is not the only criteria. We are looking at the war-fighting contribution. We are looking at life-cycle costs. And we will do -- we have the opportunity to do a technical assessment. All of those factors would play in. And the bottom line, the reason you can be sure this isn't a price shoot-out, is that it is actually possible to have a higher price and to win this competition.

Third, we are using this competition as a flagship for acquisition reform. This has some of the key characteristics wise in our acquisition reform agenda. First, it has stable requirements. One of the changes that we made from the prior competition is, in the prior competition there were only 37 mandatory requirements; in this competition there are 372.

Now, why the difference? The difference is that one of the ways you get cost growth is that you add requirements as you go through the program, and you implement them through engineering change proposals and you increase the price. That is exactly what would have happened, had the prior competition gone forward to contract.

The Air Force has a series of requirements, and all of those requirements are now reflected in this RFP from-- and Michael described the core document, the concept-development document. All of the "must's" and" hall's" in that document have been converted into mandatory requirements, so that we don't get to the signing the contract with the winner here and then deciding, okay, we want to add these various requirements.

We're putting them -- the ones that we absolutely have to have, we're putting up front.

Second, we are pursuing this in a fixed-price framework. I'm going to talk a little bit about how we've changed some of the contract pricing provisions. But that doesn't change that this is a fixed-price framework. This is the direction that Congress wants us to go in. And we can't do fixed-price development in every case.

But in cases such as this --where the technology is mature, the contractors have a well-established industrial base, and the Air Force well understands its requirements -- this is a true opportunity for us to pursue a fixed-price contract, and that's what we intend to do.

And then finally this -- we are not looking at just acquisition costs when we look at cost. We are looking at life-cycle costs. We're looking at fuel costs. We're looking at changes in military construction costs. Those are all elements of the president and Secretary Gates' acquisition reform agenda. And they're reflected in this competition.

Now, let me talk about the move from the draft to the final RFP. We got over 350 comments from both -- not --both from industry and from Congress. Weave addressed all of them. And as a consequence of those comments and questions and proposed changes, we have made about 230 changes from the draft to the final RFP.

Now, many of those changes are more in the nature of technical changes we have -- for example, both contractors pointed out that our provision on proprietary data rights probably needed to be shifted some. And we have done that.

Some of the things on FAA certification needed to be adjusted. We have done that. We've moved the LAIRCM [Large Aircraft Infrared Countermeasures] defensive system to government-furnished equipment, because that was a more efficient way to acquire it.

The Microwave Landing System is no longer an Air Force requirement, so we've dropped it. Those are all, I would say, in the nature of technical, relatively standard changes when you go from a draft to a final RFP.

We've made -- in addition to those, we've made one significant change in the contract pricing approach. As I said, we've retained the fixed-price approach, but we have shortened the period over which the competitors would have to specify a fixed future price for the airplane, and we've lowered the threshold for DOD to make future price adjustments if economic conditions change. And Ash is going to explain that in a bit more detail in a second.

Where we haven't changed things is in the basic requirements of the airplane. The warfighter has set out what they need. We think the 372 requirements that we've laid out will bring the Air Force the plane it needs to bring to the war-fight on day one. And we have retained those requirements, and we've retained the structure of the evaluation system that we've used for those requirements.

In the end, this is about what the Air Mobility Command needs to meet the war-fighting needs of the nation. We think that the structure in this RFP is going to get us that, and we're going to proceed in that direction.

Finally, the schedule. We have given a little bit of additional time for the proposals. It's 75 days. The RFP should be on the website now; I think it went on at 4:00. So 75 days from that point is when the proposals are due. We will take about 120 days to evaluate those proposals. If you add that time up, that takes you to about mid-September, and so that's the time frame that we're looking forward to.

We're certainly hopeful that we'll have a robust competition, and we think that competition will get us the best value for the taxpayer and the best airplane for the warfighter.

With that, let me turn it over to Mike Donley to go into a little bit more detail on the requirements.

SEC. DONLEY: Okay. Thank you, sir. As the deputy suggested, the department believes that stability in requirements is very important going forward. There may be circumstances where engineering change proposals soon after contract award --are warranted, but this should be the exception and not the rule -- and this is where cost -- as this is where cost growth often occurs.

So in this case, compared to the last solicitation, as the deputy indicated, we moved many of the factors considered in the last solicitation from nonmandatory to mandatory, but we did that based on our look at the proposals, our understanding of what the contractors could and could not do, and our assessment of what the warfighter needed to go to war on day one. So we do not expect this airplane to come off the line and go into some modifications. We expect it to come off the line ready to go to war under Air Mobility Command.

So in this preparation of this draft, as you recall, when we presented it in September, the last time you saw this slide there were 372 mandatory requirements. This time -- excuse me -- 373. We did eliminate one requirement for the Microwave Landing System, which technology has passed by and is not an essential requirement. So that's fallen away. We're down to 272 (sic).

In addition, in keeping with the best-value approach, the warfighter did identify 93 additional or enhanced capabilities that we're willing to commit a limited amount of resources to acquire.

It's worth noting last -- that last time both offerors had expressed some confusion about what the priorities of the warfighter were and what they specifically needed the aircraft and its systems to do, and in some cases understanding how they would be evaluated on the factors that we had tabled.

The approach we have taken is of benefit to both offerors because we've been very clear about these 372 mandatory requirements, and we have scored the additional 93 enhanced capabilities very specifically so the offerors know exactly how they are going to be evaluated on each of those factors.

I want to go back just to clarify, refresh for you where the requirements came from. There has been a capability development document approved by the JROC [Joint Requirements Oversight Council]. In prior years -- it was reviewed just about a year ago this week, the end of February. There were no changes made to the CDD [Capability Development Document]. That CDD included nine key performance parameters.

Now there's been some suggestion that maybe the Air Force was not interested in anything other than a C-1 --KC-135 replacement, something equivalent to the KC-135. I want to be clear that in eight out of the nine KPPs, the key performance parameters, they exceed the capabilities of theKC-135. I can give you just some examples of those KPPs, which I think we reviewed last time, but just so you're-- you can be refreshed on those, it -- include worldwide communications and commercial navigation capabilities, net-ready capabilities, if you will; force-protection capabilities; additional survivability capabilities.

It needed to be the most --among the most important, obviously, capable of multipoint refuelings, both boom and drogue capabilities, and multipoint refuelings at the same time; and also, to be an air- refueling receiver -- in other words, it can receive fuel as well as give fuel.

So these were the -- several of the KPPs, and they have not changed. What did change was our focus on getting the requirements all down in one block that the -- that the offerors could understand, that represented what we needed on day one. So that's the story behind the 372.

Slide, please.

Now, just to refresh on the source-selection process, the Air Force is responsible for the source selection. The source-selection authority will be a senior career Air Force official. Again, we do not identify who that is. It is the source-selection authority's responsibility to select a KC-X contract winner, using the approved source-selection strategy that we have outlined in this proposal.

There is a new acquisition teaming place in the Air Force, the Source Selection Advisory Council, that will advise the source- selection authority. About 10 of 11 key players there are new. The evaluation teams that support this effort-- there are about 14 teams. At least six of the chairs of those are new players. And we will use three independent review teams to provide -- to provide an independent assessment of how well we have evaluated the offers.

So again they're not doing a separate -- just to be clear, the review teams are not making a separate, independent assessment of the offers. They are making an independent assessment of how well we have evaluated the offers.

They're checking our work, to make sure we have colored all the things that we are required to, by law and regulation, that we have covered every aspect of the source selection process in an appropriate way.

In addition, I want to emphasize that all the levels that I have described -- the advisory council, the evaluation teams, the independent review teams -- are joint teams with experts from across the department.

So the Air Force is not doing this alone. We're supported by Dr. Carter's staff, by legal staff from across the department, even in some cases Navy or Army representation, where they bring independent acquisition expertise to bear.

So with that, I'd just -- I think that's a good segue actually to thank the deputy and Dr. Carter for their strong support, as we put together what we think is a very strong RFP.

As we have looked at this, we believe that both offerors are in a position to win this competition. They -- in previous solicitations, they were very strong on price and other factors. Both offerors were.

We think both offerors can meet the mandatory requirements that we have laid out. And we hope and expect to have a good competition. And with that, I'll turn the next segment over to Dr. Carter.

DR. CARTER: Thank you, Mike.

There are two parts to the RFP: the requirements part that Secretary Donley just spoke to, and then the source selection strategy which I will now speak to, which is the method, the algorithm by which the source selection authority will pick the winner.

And as Secretary Lynn said, clarity and precision is a very important principle of the acquisition reform effort we have here. And so the source selection strategy is crystal clear. We've said that from the beginning. Everybody will know, when a winner is picked, exactly why they won. And up front, both offerors know exactly what they need to do to win.

There were eight issues which arose in our discussions with the -- with industry and with Congress in connection with the source selection strategy. In the annotated briefing that you'll be provided with shortly, there's a chart on each one of these that explains them. But let me go through each of them very briefly

The first one is this mouthful called IFARA [Integrated Fleet Air Refueling Assessment]. What is IFARA? IFARA is the way we measure the warfighting effectiveness of the tanker. And both Secretary Lynn and Secretary Donley made this clear, and I want to emphasize this because there's a lot of misunderstanding around town on this point.

This is not a price shootout, as Secretary Lynn said. Other features of the airplane than it price are taken into account, in several different ways, to such an extent that, as Secretary Lynn said, you can have the lowest price and still lose if you have other features which we value.

How do we go from price to value? We start with the price and then we adjust the price. We adjust it first of all for the warfighting effectiveness of the airplane. And that adjustment is made through this IFARA model. And the IFARA model is unchanged from the draft RFP, except in some very minor technical details. And, by the way, it was used in the last competition as well.

And the output of the IFARA model is used to adjust the offeror's price. If they do well at IFARA, they get their price adjusted down. They get a bonus for it. And I only say that and emphasize that just -- that's one example of the way that non-price factors matter. But we dollarize some of then on-price factors -- I just gave you an example -- and adjust the price accordingly. That's a quantitative way and a very crystal-clear way that we can measure something other than price that matters to us. So just because it's turned into dollars, don't confuse that with price. It's another way of measuring value.

So, also, do we adjust the bid price by the second item up there, cost-of-ownership factors over the 40-yearlifetime of these airplanes. The factors that are in the control of the two offerors are the fuel efficiency of the airplane they offer and the cost in military construction to adjust our bases to accommodate their airplane. So we want to take those two factors into account. And if you burn more fuel or your -- cost more to adjust bases, we will adjust your price up, because we're going to have to pay ultimately more for you, and vice versa.

So you can see that both IFARA and cost of ownership are used to adjust prices.

Systems engineering and technology maturity -- I should say by the way that we had extensive interactions with both offerors on IFARA, fuel burn and MILCON [military construction] -- to make sure that they understood exactly what we're going to do.

We had some, what you might call, training sessions on IFARA so that they could understand, so that everybody knows exactly what is -- how they're going to be evaluated. And in the course of that, we have made some minor adjustments to our methodology but no more.

We had a number of questions from Congress and industry, about how the RFP would treat systems engineering and technology maturity, which are important themes of the Weapon Systems Acquisition Reform Act.

And we tried to be careful, and the briefing is very careful, to explain how we're going to deal with these two issues, in the RFP, and likewise with development and integration risk.

The 1 percent total evaluated price gate is -- was established as a reasonable dollar value for how close the adjusted prices would need to be, in order for the trade space to come into play.

Only if the bids as adjusted are within 1 percent, and this is not different from last time, are those 93 items which the warfighter said were of some value but not a lot of value.

So if the bidders are close, not in price but in adjusted price, then if they're really close, take a look at these other things that don't matter a lot but do matter some. Those things we chose the 1 percent gate because we reckoned that those things -- we didn't reckon; the warfighter reckoned -- that those were worth about $300 (million), $500 million, which is about 1 percent of what we estimate the total cost of this program to be; said differently, that he was willing to pay about an extra 1 percent for those particular extras. And that explains why the 1 percent gate is 1 percent, and we looked at that once again, in going from draft RFP to final RFP, and did not change that because the logic held up.

Let me jump down to the World Trade Organization issue. We reviewed that one. Once again, that is the claims by the United States against the European Union and vice versa. And we had made no changes to the department's position on that issue. It's stated very clearly in the briefing you're about to receive.

Also, the allegation by Northrop Grumman that bid information was released in the last competition that competitively disadvantaged them -- we once again examined that and ascertained, as we said last time, that the release was authorized and appropriate, and does not in fact create an uneven playing field. So no change there.

Now to the issue where there was a significant change, which is the contract structure.

This chart's a little bit complicated, but let me try to give you the gist.

First of all, as Secretary Lynn said, in accordance with our acquisition reform emphasis, both the development phase and the production phase of this program will be fixed-price. And the reason why that's appropriate, as Secretary Lynn said, is that this is a fairly well-defined product. It is a derivative of a commercial product, of which hundreds are made every year. We have -- have had tankers for a long time. Both offerors know how to make tankers, and so there is not any great invention required here. And it's appropriate in the case, even in the development phase, to have a fixed-price structure.

However, we -- and we required in the production phase fixed prices out all the way to 2027, which is the last year, that is Lot 13. That's a long time for the offeror to fix a price for. And both offerors said, you know, that put a financial burden on the offerors, and would we give some consideration to that financial burden. We did, and therefore -- I'm going to walkover and just point to the two places I want you to focus your eyes -- here and here.

Last time, we said: You have to give us a fixed price, and if inflation exceeds 5 percent, we will adjust your price. Five percent. Well, that's a lot in the out-years, year upon year.

So we are now saying, in Lots 3through 5, that if inflation exceeds 2-1/2 percent, we will make an adjustment; and in Lot 6 through 13, if inflation exceeds 1 percent. Well, that allows both offerors to manage risk in the out-years better. We thought that their request that we consider that particular aspect of the contract structure -- we thought it was reasonable that we reconsider that, and upon reconsidering it, we decided to make those changes. And they may seem technical to you, but they're not technical, they're substantive, and they will be very relevant in those years in the future when we're building these tankers.

So that is a major change to the source selection strategy. And I hope you understand it. If you don't, you can read about it in the briefing. But it's as simple as, you know, it's very difficult to project the future, unreasonable to ask people to project, on such a large program, the future that precisely. We're giving some room in that far future to both offerors.

With that, those eight points are the most significant ones that surfaced in connection with the source selection strategy. And once again, there are requirements and source selection strategy, and now you see the whole picture.

Let me turn things back over to Secretary Lynn. And we're prepared to answer your questions.

MR. LYNN: There's one more chart, but I think we've covered everything there. I think we'll just turn it over to your questions.

Tony.

Q One of the biggest hanging issues is whether Northrop will, in fact, bid, even though you've laid out a -- an open kimono here. If Northrop decides not to bid, is it the department's preference that they make a decision relatively quickly, in the next two or three weeks? Or does it matter if this plays out to the 75th day and they say, "We're not going to bid"? What's your preference, if any? And I have a follow-up.

MR. LYNN: It's the department's preference that they do bid. We have -- we have options that we'll address if they choose -- if they choose not to, but we think we've put forward a balanced and fair competition. We've briefed it to them. They're evaluating it. We hope they come to the conclusion that they will bid.

Q If, in fact, you only have one bidder, what review processes will Boeing's bid go through to ensure price reasonableness and that the taxpayer won't be gouged by an overpriced product?

MR. LYNN: As I said, there are options for pursuing a-- an alternative if we don't have two bidders. But our -- very much our hope is that we will have two bidders. We -- Northrop and Boeing both competed very well last time on price and on other factors. We -- our assessment is they'd both be strong competitors this time. And we're focused on having them both bid, and we think that would lead to a robust competition.

MR. WHITMAN: Sure.

Q What happens if this RFP is protested? What's -- how does that affect your timeline here? Do you continue the bid process? Or that freezes things up until there's a -- (inaudible)?

MR. LYNN: We haven't addressed what would happen in that case.

Q (Inaudible) -- answer there.

My next question would be, Lots1 and 2, how many aircraft in those lots? And what's the time frame for those?

MR. LYNN: Is it 19 aircraft, would be --

(Cross talk) Nineteen. Nineteen.

MR. LYNN: And --

Q Total? Total of 19 aircraft?

(Cross talk) Yes. In those two lots. Two lots.

MR. LYNN: In those two lots, yeah.

(Cross talk) The total is 179. Now --

MR. LYNN: So the -- all 13 lots --

DR. CARTER: For all 13 lots.

MR. LYNN: And the first two have nine -- 19.

Q And just to follow up, what is the timeframe for those first two lots?

DR. CARTER: That is -- let's see -- 17 -- five --

(Cross talk) (inaudible) -- the first thousand -- the first aircraft is two years after --

DR. CARTER: It will be '6 and '7 -- '16 and '17, 2016 and'17.

Q (inaudible) Yeah.

DR. CARTER: Yeah, '16, '17.

Q Okay.

Q For delivery, you mean?

DR. CARTER: Yeah --

(Cross talk) No, for -- (inaudible) --

DR. CARTER: For -- you know, that's when -- they'd go in the contracts, those two lots.

MR. LYNN: So the first lot would go on contract in 2016and the second lot would go on contract in 2017.

DR. CARTER: You can count on there all the way up to2027.

Q Okay.

DR. CARTER: -- if the math works right.

Q How many SDD [System Development and Demonstration] aircraft are expected? And are there any limitations on where those aircraft can be produced or final assembled?

DR. CARTER: The --

Q (inaudible) -- the aircraft -- I'm sorry-- not just -- (inaudible).

DR. CARTER: Yes. The -- there aren't any limitations on where they can be assembled. We can only guess from the two -- but the --where the two offerors will do the assembly of the early aircraft -- we obviously know what their plans were last time, but we'll just have to see what their plans are this time. We don't know until we get the bids in.

Q And the question on how many SDD aircraft-- is it four again this time?

DR. CARTER: I don't know the answer to that.

(Cross talk) Four.

DR. CARTER: Shay [Assad], is it four?

MR. ASSAD: It's four.

Q And when is -- are -- is there a schedule on which you have to have those delivered?

DR. CARTER: Yes, within the -- well, we're not going to have -- we don't have an SDD plan now, because we don't have bids. But when we do, we will have an SDD schedule, just like we do for any other program. You're probably thinking of JSF.

Q Okay. So that's up to the bidders to sort of say what they can do.

DR. CARTER: Yes. Well, that'll be discussion between us and them.

MR. LYNN: Jeff.

Q   Yeah, I know this issue's come up many times before, but what is the Air Force's and the department's current position on a dual procurement? And have you done any planning for that option?

MR. LYNN: I think the secretary has been enormously clear on what he thinks of the split buy. And we've evaluated it. We think it will cost the taxpayers more. And we oppose it.

Q   So how would you deal with two aircraft of different capabilities and performance criteria, if they in fact turn out to be of equal value, in terms of acquisition costs and life-cycle costs?

MR. LYNN: Well, I mean, I think, Ash went through the process.

We take their acquisition costs. And then we adjust it for the warfighting analysis, basically give a credit to the aircraft that does better in the warfighting analysis. We adjust it further for the life-cycle costs: fuel and military construction.

That will -- then you put all of that into a net present value, because these are all different years and different -- then you would compare those two. If one of the bidders at that point has a price that's 1 percent or more lower, they are the winner.

If -- that's an evaluated price, in other words, with all those adjustments, not just the pure acquisition cost. If they are within 1 percent, we would then move to the next stage, which are those 93 tradable requirements, those enhanced capabilities that Ash mentioned.

Those each -- we have assigned point values to each of those 93. And we would evaluate whether each of the offerors met the requirements for each of those 93. If they did, we'd give them the points. Then we would add up the points.

At that point, the offeror with the most points would win the competition.

Q   How come you didn't look at -- why did you keep the evaluation criteria pretty much the same? Can you just expand a little bit more on why you didn't change that?

SEC. DONLEY: In terms of how this source-selection strategy was put together, we spent a full eight months reviewing that, alternative strategies, before we unveiled the draft in September.

So we have been through a number of alternatives and discussions about how to structure this competition, always mindful of pressures to adjust the competition, to adjust requirements, in ways that would favor one aircraft or another, and being very sensitive to this idea that there are perceptions that one offeror is favored over another.

After all, the airplanes are different. We can't help that. That's sort of the state of play. We know what our requirements are, and we went through a very careful process to settle on the acquisition strategy that the deputy and Ash have -- have described. So we felt like that was a pretty good strategy and the fundamental elements of that did not need to change.

Q   Hi. You spoke earlier about the number of teams -- a lot of teams are reviewing this, and there are a lot of acquisition people reviewing this. Can you put a number to how many people are on this? And are people being pulled off of other programs to come work on this one?

MR. LYNN: I'm going to ask Ash to address that.

DR. CARTER: Well, let's see, you saw on that chart several tiers of teams. So there are --it's going to be hard to answer your question how many teams there are. I want to say at the technical level, 14.

SEC. DONLEY: Fourteen teams.

DR. CARTER: Fourteen teams that deal with each aspect of the airplane. These are people who are deeply expert at one portion or another.

At each tier, of course, the Air Force is the core of the team. But we supplement them and oversee them in two ways. There are representatives from my office that do that.

And then we also used something called peer review, which is we get non-Air Force, let's say a naval officer who knows a lot about naval aviation. That's a great set of fresh eyes that can look and say, "Hey, wait a minute. Have you guys of thought of this, that or the other thing?"

So we try to make sure that these teams have fresh eyes; that my office oversees the process and makes sure that the source selection authority actually follows the source selection strategy that we have -- we've specified.

(Cross talk.)

MR. WHITMAN: Okay. Oh, sorry.

Q Yeah, what's the status of the current fleet of KC-135s? If there's a problem with this -- awarding this contract, how much longer can these planes fly? You're already talking about a few years out. So what's the status of the current fleet?

SEC. DONLEY: This -- the current status -- the fleet average is about 49 years, so there's some older, there's some few -- a few younger. On the average, it's 49 years across a fleet of 400 and about 14. I can get you probably a -- an exact number for the KC-135. It's roughly that.

Q (Inaudible) -- me that they can keep flying for the next five, 10 years?

MR. LYNN: You usually measure tankers in terms of hours rather than -- I mean, ultimately, obviously you run out of -- run out of gas, so to speak. But the -- when a -- when a large aircraft like this, there -- it's more hours. And there are hours left, but we -- we're very focused on getting this competition resolved this year, and that -- that's certainly the objective. And we think we've set out a path that will do that.

SEC. DONLEY: And we have continued to fund KC-135sustainment robustly going forward, because we know this is a potential vulnerability. As the deputy indicated, there are hours left on these airplanes. They do not take high-G maneuvers, generally speaking.

But we don't know what we don't know about there this fleet is headed.

If the average age is 49 years, it could be as high as 70 years when the end of the KC-X procurement is still under way 17 years from now. So it's an old fleet, and this is why it remains our number-one acquisition priority to get started on its recapitalization.

Q Was the a source selections strategy written with any consideration to the possibility that you might have only one bid?

MR. LYNN: We have written this as a competition, so that's the focus we have right now.

Q Yes. This is a more general question about industry protests. Do you all have any concern more broadly about industry protests? I mean, the Air Force in particular has had a couple of very high-profile protests, on tanker but also on CSAR [Combat Search and Rescue]. They do slow down these development programs, and with the tankers getting old, more broadly looking across your acquisition portfolio, is this a concern for DOD in this and this prospect?

DR. CARTER: It is. It is. And I've said that before. I think all three of us have said that before, that the -- if one gets to a point where there are protests that are routine or frivolous, that's just standing in the way of our providing capability to the warfighter and being fair to the taxpayer, and we would oppose that.

There is a protest process. There is a due process. We do make mistakes. Protests are sometimes sustained on perfectly good grounds that we've made a mistake. We do many of these per year. It's not surprising there are mistakes. So it's absolutely fair for a disappointed bidder to protest. That's within their right. But the bar should be high because one is detaining the acquisition of capability by the nation's armed forces. That's the effect of a protest.

Q Have you expressed that to Congress? Or is there anything formal that you can do, to sort of shore this up and make sure the bar is high?

DR. CARTER: I think the best thing that we can do as a department, and that I can do from the position I'm in, is make sure we don't make mistakes. That's certainly something we can do, so that it's absolutely clear, as I hope we've indicated we intend to make it, in this case, what it is we did when we picked a winner.

In this case of the tanker, everybody will know exactly why offeror A won and offeror B lost. And there shouldn't be any doubt. And there wasn't any doubt where they should aim, if they want to win. That's the way we on our side can deal with the protest issue.

And on the industry's side, it's a matter of restraint and understanding of the impact, on the operations of the department, that frivolous protesting would result in.

Q I'm curious about the issue on fixed-price. My understanding, please correct me if I'm wrong, but with fixed-price contracts, for example, this has been discussed with JSF [Joint Strike Fighter], you lose a certain level of visibility into the pricing and that sort of thing.

I'm curious how that impacts your ability to monitor this program, especially if you only have one bidder, because then you have one bidder that maybe isn't quite as auditable. And what does that mean for your ability to sort of police the contractor?

DR. CARTER: That's a very good question. And that is why it is a falsehood to say that fixed-price contracting shifts risk to the contractor.

It actually makes us assume additional risk also, but all in a good cause. The risk we assume is, we better know what we want, and not change what we want after we've asked for what we want.

That's not always appropriate. If you're developing a new weapons system and you don't know exactly what's possible, you're doing some invention, then you shouldn't be in a fixed-price environment, because neither you nor the contractor knows where you're going.

In a case like the tanker, where it's something we've done for a long time, it's a derivative of an airplane that is made year upon year upon year by these companies, where they have fixed-price arrangements with their commercial customers, where -- in other words, in this case it's perfectly appropriate to have fixed price.

But as Secretary Lynn said, we can't then go change our mind later. And that's one of the things we're trying to avoid by being very specific about all these requirements, is, this is, by gosh, the airplane that the Air Force has said it wants on day one. And that's it, and we're not going to change our mind about it later.

Q So in your chart "Contract Pricing Provisions," where you outline the fixed price for development, you've got 60-40splits on sharing, I guess, the risk of an overrun, and then 125 percent cost mitigates risk -- or -- (inaudible) -- mitigates risk.

DR. CARTER: That -- yeah. That --

Q What does that mean?

DR. CARTER: Okay, I'm sorry. That's a very good question, and that gets in a little bit of contractology here. And apologies for this.

This is the contract structure for the SDD phase, the development phase. And it goes like this. We say, give us a price. And because it's the development phase, the -- it's not reasonable to say we're going to fix that price, because maybe there'll be some reason why that reasonably goes up or down.

If it does go up or down, if it-- let's suppose it goes up.

Then the 60-40 share means for every dollar above that price, we'll pay 60 cents, but you pay 40 cents --

Q Okay.

DR. CARTER: -- we say to the offeror. We're -- in other words, if there's cost escalation in the SDD phase, we're not going to eat it all ourselves. In the production phase, we're at fixed price. We're not going to eat any of it.

Q But why --

MR. LYNN: And then there is -- to just add the one point -- but there's a ceiling. The60-40 share-line goes to 100 and -- if they make a $100 offer, we share to$125. The 126th dollar is now paid for by industry, and every dollar subsequently.

Q (Inaudible) -- assumption.

MR. LYNN: Right. So in other words, the first 25 we share 60- 40. After that, it's -- it becomes an industry risk.

Q Dr. Carter, while you have this chart on, as valiant an attempt as you made to explain this --

DR. CARTER: (Laughs.)

Q -- Lot 3 through 5, does that, in kind of like English, mean if the -- if the fixed price from Lots 1 and 2 exceeds by 2.5percent --

DR. CARTER: No, I'm sorry. Not to exceed -- if I could do this chart over again --

Q In English, yeah. Okay.

DR. CARTER: We were talking about that this morning. We would take "not to exceed out," and put "fixed-price."

Q Okay.

DR. CARTER: Forget the "not to exceed." So what this says is that in Lots 3 through5, we will require a fixed price. And the trigger band means if inflation exceeds 2-1/2 percent, we will give you consideration for the effect of inflation. We will adjust your price, because you have suffered from the effects of inflation. If it's below 2-1/2 percent, it's on you.

Q But the government will pick up the -- if it's over 2-1/2 percent, the government will pay the --

DR. CARTER: Exactly.

Q Oh, boy, that's confusing.

MR. LYNN: Let -- let me add a little bit to that, Tony. When you bid these contracts, the contracts themselves will have an inflation indices in it. Say it's 2 percent per year.

Q Yeah. Okay.

MR. LYNN: What this is saying is that if it varies by a wide amount from that 2 percent, if we have hyper-inflation and material costs are up 10 percent, the government will take that risk.

And what we're trying to establish with this -- and this is why we made the change -- is we want the contractor to take the risk on the things they control. We think the government should take more of the risks on the things they don't control, like material costs and general inflation. Those economic factors.

So this is a fixed price, but when you're going 18 years out, to have them take the risk of where inflation's going to be in 18 years, we didn't think that was appropriate. But we are having them take the risk on --that they can actually hit the production costs, absent unusual inflation, that they can hit the production costs that they bid. And they will be held to that.

Q Fixed price should not say not to exceed, because that's a specific contract mechanism also.

MR. LYNN: it's a technical term, and it has to do with how you do the contract provisions.

Q Fixed price -- (inaudible) -- and then the adjustments for inflation.

MR. LYNN: That's right.

Q But all these -- (inaudible) -- are based on the fixed price from Lot 1 and 2, or they get a new fixed price each time?

MR. LYNN: They bid each lot.

Q Oh. Okay. Okay.

MR. LYNN: So they bid each lot with that inflation indices. If that inflation indices turns out to be wrong, they have some protection. Is that better?

Q When is Lot 3 being bid?

MR. LYNN: (Speaking aside) We should put years on this.

(Off-mike comments and Crosstalk.)

DR. CARTER (?): No, it would be 18 through 20.

Q (Inaudible) -- 18?

MR. LYNN: Oh, yeah. They would be submitted now by year when they would be executed.

I'm sorry, who haven't I -- I guess --

Q Going back, when do you - Secretary Donley, when will you expect to see these KC-Xs begin showing up on operational AMC [Air Mobility Command] bases or, you know, available for -- to train -- (inaudible)?

SEC. DONLEY: IOC [initial operating capability] , I think. Let me double-check.

MR. LYNN: When's the IOC?

SEC. DONLEY: IOC would probably be something like 20 --probably the first squadron, which would be -- let me get you a date.

Q There's a perception among some members of the public that because Boeing is headquartered in Chicago, and President Obama and some of his top associates are from Chicago, that the terms of this RFP have been written to favor the Boeing aircraft.

Could you address that? And also specifically has the White House had any involvement in the drafting and preparation of this RFP?

MR. LYNN: The White House has had absolutely no involvement in the drafting and the preparation, the consideration of the RFP or any other aspect of this competition. All of the requirements were done to meet the needs of the Air Force and to get the best possible deal for the American taxpayer.

Q This is a broader question.

I mean, I know you guys are hoping that there will be two and that you're prepared if there's only one bidder. But what can we expect from you? Obviously there would be a huge outcry from Congress and beyond that. How are you going to -- how would you deal with kind of the reaction if this were to go ahead as a sole-bidder process?

And also on the issue of, you know, partners overseas, if this is just one bidder, I mean, you know, the secretary made -- the secretary made comments yesterday about Europe's need to kind of, you know, ramp up its defense spending and everything else.

How do you see that playing out? How do you think of a sole- bidder process here looking to our defense partners abroad?

MR. LYNN: Well, I mean, obviously Northrop has a choice to make. We're hoping that Northrop chooses, with its European partner, to bid. As I indicated at the beginning, we have options that we could pursue if they don't. But we think -- we think they have a very serious opportunity here.

They were very competitive before. We think they'd be very competitive now. We think it's in their interest to bid. We think it's in our interest for them to bid. And that's the approach that we're taking.

Q But the question is, what if -- I mean, if they don't, what kind of scenario are you guys expecting?

SEC. DONLEY: We -- in our discussions, there have been several scenarios. And the details are-- there are just too many permutations.

We have options, and we're just not in a position to say how we would proceed at this point.

Q (Inaudible) --

Q But you can be sure there'll be transparency -- (inaudible). Sole bidder, you know, this is -- this is the kind of stuff that gets people -- I mean, it could get people in trouble. You know, you can be sure there will be a transparent legal process, you go ahead with it --

SEC. DONLEY: There is a process for how to do that.

MR. LYNN: There is a process for that. We are hoping that we are going to use the competitive process in this case.

Q Are you by law, if there's one bidder, confined to this strategy? Or can you implement additional control over the contractor? I mean, you can't change the strategy mid-course, right, because then you're protestable. (Chuckles.) So if you only get one bidder, are you stuck with this?

SEC. DONLEY: I think -- well, we may not know that until we get to the end of -- (inaudible) -- process --

MR. LYNN: We'll deal that -- when -- when we get to that point, we'll address that question.

Q It's a legitimate question, though. I mean -- it's a legitimate question moving forward what your legal options are.

MR. LYNN: I don't want to go beyond the statement that we -- we do have legal options that have been pursued on -- in these kinds of situations in the past; they could be pursued again. We are hoping that we don't have to. We are hoping that we have a robust competition in this process.

Q At the end of the day, at the end of the evaluation period, can you go over how the decision-making process is going to happen, how that's going to work?

DR. CARTER: Well, that's, I think, what you were explaining, with the source-selection authority and -- why don't -- why don't you --

SEC. DONLEY: The source-selection authority is the one who receives the two bids, applies the methodology, takes the price they give, adjusts the price for warfighting effectiveness and cost of ownership, compares those two prices.

If they're more than 1 percent apart, you got a winner. If they're less than 1 percent apart, then you consider those extra, additional items in the trade space and make the award on that basis.

And you'll be able to backtrack all of that when an award is made.

Q And that's all Air Force, the source selection?

SEC. DONLEY: The source selection authority --

DR. CARTER: The source-selection authority is a single individual --

Q Right.

DR. CARTER: -- who is responsible for making the decision. He is an -- he is advised by an advisory council, which we showed you -- about 11 folks, I think -- who are senior folks that advise him on sort of their assessment of the evaluation products produced by the teams. As I mentioned, there are 14 teams. They'll take the proposals, divide them up into 14 areas, and they'll review 14 separate pieces, side by side. And the advisory council will review all that material, and advise the source-selection authority.

Q And the advisory council is all Air Force, or it's Air Force and joint --

DR. CARTER: It's mixed.

Q You mentioned real quick earlier how this program's going to be a pilot for weapons systems --

MR. LYNN: Flagship, I think I said.

Q Flagship for weapons -- acquisition reform. Do you plan to wait until this program is done before launching any other new acquisition initiatives, to see how it goes, get your feedback?

MR. LYNN: No. I mean, we're already undertaking others. The small-diameter bomb has some characteristics; littoral combat ship does.

I don't know, Ash, if you want to --

DR. CARTER: On CAP-4 . No, you see, in all the programs that we're starting, programs we're restructuring, we are implementing these same principles.

Q Mr. Lynn, if this is a flagship for acquisition, what's the nine years of trying to get to this point today? And how would you characterize the effort thus far? If this is going to be your flagship, kind of look back a second. Is this a fiasco, or -- or what?

MR. LYNN: Well, I'm not going to criticize the -- I mean, obviously, this has been -- you know, has had a couple of false starts, for different reasons.

We think that -- when I said flagship, I think that what I'm referring to is not the history of the tanker program. I'm talking about the characteristics of this acquisition: the fixed-price nature of the acquisition, the inclusion of life-cycle costs and the mandatory nature of the requirements and setting the requirements up front.

Those are all changes to prior approaches that we think reflect reform. When I say flagship, that's what I mean. I'm not kind of comparing this to prior.

MR. WHITMAN: We've been going for about an hour now, and some of you need to get to file. And so we are going to bring it to a close right now. If you would like a copy of the slides that were presented today --(inaudible) -- has them off to the side here.

Thank you very much.