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Congress of the United States
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RECYCLED PAPER

Mr. Shay Assad
Director, Defense Procurement
3060 Defense Pentagon
Room 3B855
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Dear Mr. Assad:

On September 24, 2009, Deputy Secretary Lynn and Under Secretary Carter briefed Members of Congress about the Draft Request for Proposals for the KC-X Tanker (Solicitation #FA8625-10-R-6600). At that time, they invited comments from interested Members of Congress. I would like to take this opportunity to submit my serious concerns about four flawed elements of this proposed solicitation document. As you know, I have been directly involved in the tanker procurement issue for the past eight years, and I am well-aware of the egregious mistakes that were made by the Department in the solicitation process that was halted after a GAO found serious problems in 2008.

With those mistakes in mind, it was encouraging that Secretary Lynn and Secretary Carter expressed their view that the acquisition process would be fair, open and transparent. A crucial element of a fair competition that favors the warfighter and the taxpayer is the need for realistic and unbiased criteria in the decision-making process, visible immediately in the Department's initial Request for Proposals.

In the first three concerns outlined below, I am indicating to you where I believe the Department has specified both unrealistic requirements and criteria that specifically—and inexplicably—demonstrate a clear bias for the EADS/NG tanker proposal. Unless these flaws in this draft RFP are corrected at the start, I firmly believe the Department risks the same disastrous outcome that doomed the previous source selection. With the serious delays that have already impacted this critical tanker replacement program, I do not believe this is a risk the Department or the nation should take at this time.

In addition, despite the Department's view that it would be more convenient to completely ignore the official position of the United States Government with regard to the illegal subsidies provided to the EADS A-330 airframe—and the recent concurrence of the WTO panel in that determination—I believe the issue must still be factored into the analysis in order to assure a fair judgment of the cost of the subsidized European contender in this procurement. Therefore I

would specifically ask that the Department correct these flaws and omissions prior to the issuance of a Final Request for Proposals:

Use Realistic Cost of Fuel in Life-Cycle Cost. As drafted, the RFP will calculate the life-cycle cost of fuel consumption of proposed tanker aircraft over a period from 2010 through 2079. For the purposes of this calculation, the spreadsheet in the draft RFP (Section L, Attachment 3) employs a yearly inflation index for the cost of fuel, and a projection of 489 flying hours per aircraft per year. Regrettably neither the cost of fuel nor the number of flying hours is realistic.

The life-cycle cost of fuel is unrealistic on three counts: 1) The inflation indices are unrealistically low and inconsistent with respected sources; 2) the cost of fuel does not reflect the real burdened cost of the fuel that is delivered to an aircraft; and 3) the number of flying hours being used is unrealistically low. The combined effect of these flaws will grossly distort the projected cost of fuel consumption and could lead the Department to select an aircraft that will cost taxpayers a great deal more than is necessary for decades to come.

As drafted, beginning in 2015 the fuel cost inflation indices in the draft RFP project that the cost of fuel will increase by approximately 2.3 percent per year up to the year 2060. Remarkably, from 2060 on, the indices suggest that the cost of fuel will not increase at all through 2079, the end of the period of analysis. This inflation profile is not supported by either common sense or other authoritative sources. The Department of Energy's Energy Information Administration (EIA) forecasts that the cost of jet fuel will increase by 3.5 percent per year over the next 20 years. When compounded over a period of 20 years, the lower inflation rate yields a cost of fuel that is only 60 percent of the EIA estimate. This disparity would be greatly amplified when the calculation runs for 69 years. In raising this issue, I point out that the Government Accountability Office (GAO) recognized EIA's fuel cost forecasts for their accuracy (GAO-07-688R).

With respect to the RFP's inflation indices that forecast zero growth in the cost of jet fuel for the years from 2060 to 2079, this defies common sense. World consumption of oil shows no sign of diminishing (EIA forecasts 1.4 percent growth per year for the next 20 years) and it is implausible that major new sources of petroleum will come into production. A rationale that assumes no increases in the price of jet fuel over any future 20 year period simply is neither credible nor realistic.

A further point concerning life-cycle fuel cost is that the costs proposed in the draft RFP do not account for the "burdened" cost of fuel that represents the true cost of the fuel (including storage and transportation) that is delivered to and used by the tanker aircraft. That is, the real cost of fuel consumed by DOD's systems is not just what the Department pays for the fuel when it is purchased; it includes additional costs to make it available at the points where it is delivered to the platforms that use the fuel. Congress addressed this important factor in the FY2009 Defense Authorization Act (Public Law 110-417). Section 332 of that legislation requires DOD to "develop and implement a methodology to enable the implementation of a fuel efficiency key performance parameter for the modification of existing or development of new fuel consuming systems." The KC-X Tanker solicitation is a major acquisition program where fuel consumption of the system that DOD selects will have a very significant impact on the cost to the taxpayer,

yet the Department appears to be ignoring the will of Congress to reflect all of the real fuel costs in its requirements.

Concerning the projection of 489 hours of flight time per aircraft per year, Secretary Carter explained that this is based on the average flight time of the KC-135 fleet over the past 5 years. He characterized this figure as being “analytically relevant.” However, given the emphasis that the draft RFP puts on the KC-X as a multi-role aircraft that can perform airlift (cargo and passengers) or aeromedical missions, I expect and hope that the Air Force will make use of these capabilities once it has them. Thus, I believe it is unrealistic to expect that the recent use of the KC-135 fleet, which has been almost exclusively for refueling, is the most analytically relevant baseline. In addition, because these aircraft will be new, not requiring the aggressive level of maintenance and time-in-depot that 50-year old aircraft require, it is not logical to predict that these tankers will be utilized in precisely the way the older planes were. A good faith estimate of future use of the KC-X due to its expanded availability and its alternative capabilities should be reflected in the projected flight hours for this analysis.

Use Realistic Military Construction (MILCON) Costs. The draft RFP proposes to use 11 bases for the purpose of analyzing MILCON costs associated with tanker aircraft that are offered for this solicitation. Secretary Carter explained that these bases were selected “based on receiver demand, proximity to existing operational and training air refueling tracks, coverage of coasts and the central US, Guard and Reserve Bases, and CONUS and OCONUS bases.”

The bases chosen in the RFP do not reflect the current force lay-down of KC-135 aircraft, misrepresenting the potential MILCON costs involved to upgrade our actual bases, once the KC-X air-frame is chosen. Of the 11 bases selected by the draft RFP, only four are National Guard or Reserve bases - 36 percent of the evaluated group. This is significantly different than the extant KC-135 force lay-down – where over 75 percent of current tanker bases (22 of 29) are either National Guard or Reserve bases. National Guard and Reserve bases are often smaller than their active duty counterparts, and they are sometimes co-located with civilian airfields. These will likely result in additional required facility modifications or limitations on the space available for additional growth to accommodate significant changes in foot-print requirements. These factors indicate that the potential MILCON costs over the life-span of the KC-X are likely to be much, much higher.

Additionally, the structure of this evaluation does not significantly account for MILCON costs resulting from overseas deployments of a routine or recurring nature. The KC-X is intended to replace our medium-size refueling capability. As the Department re-establishes its focus on the broad range of potential threats and missions around the world, I expect that our acquisition processes would ensure that we demand weapons systems that can meet the highest requirements in the austere environments we are likely to encounter in the future.

All these factors lead me to believe that the draft RFP inadequately captures the full potential MILCON costs of each KC-X submission. These costs could easily be in the \$1-\$2 billion range. I ask that you review this element of the evaluation process and modify it to ensure that the source selection be founded on a more realistic and likely sample of bases than those that are proposed in the draft RFP.

Fuel Flow in Refueling Boom. The current KC-X Draft RFP includes a mandatory requirement for the boom to deliver fuel at a maximum rate of at least 1,200 gallons per minute (GPM). This is in contrast to the requirement from the earlier KC-X competition that specified the boom maximum offload rate as a non-mandatory requirement to *“be capable of delivering fuel to all receptacle equipped receivers at rates and standard refueling pressure such that the KC-X is not the limiting factor.”*

I understand that the Air Force has cited the need for 1,200 GPM boom offload rate because certain large receiver aircraft can, at least during a portion of the total refueling time, accept fuel at a faster rate than the 900 GPM offload rate of the KC-135. The Air Force answered a recent draft RFP question regarding the rationale for the 1,200 GPM offload rate as follows:

“The requirement was and still is 1200 GPM. In the previous source selection this was a tradeable requirement and any value less than 1200 GPM could have been offered and received partial credit. The previous SRD required the boom flow rate to “not be the limiting factor” during aerial refueling. To meet this requirement, the maximum boom flow rate must be at least 1200 GPM to meet C-5 receiver capability. The new SRD clarifies this requirement by specifying maximum boom flow rate of at least 1200 GPM.”

If the rationale for the 1,200 GPM offload rate is that the boom offload rate not be the limiting factor during refueling, how do you reconcile this with the fact that there are aircraft such as the C-17 that can receive fuel at faster rates (approaching 1,300 GPM)?

Since the stated rationale for the offload rate is not logically consistent with the facts, I have to question the basis for having chosen this particular value as a requirement. I find it more than curious that the 1,200 GPM figure conveniently coincides with the advertised offload rate of the NG/EADS KC-30 tanker.

The Air Force should revisit this requirement and establish a solid, rational basis for it. Instead of adopting what appears to be an arbitrary requirement, why would the Air Force not employ an approach that is consistent with other RFP requirements by establishing a mandatory requirement consistent with KC-135 capabilities (900 GPM) and a higher fuel offload rate being “non-mandatory”?

Reflect the Real Impact of Unfair Foreign Subsidies. Since 2004, the position of the United States Government has been that for several decades Airbus has systematically benefitted from unfair government subsidies for its commercial aircraft. These subsidies have resulted in lost sales, eroded market share, and reduced employment for American producers of large commercial aircraft (in particular the Boeing Company). In the words of Ambassador Ron Kirk, U.S. Trade representative (Sept 16, 2009), these subsidies “caused adverse effects to the interests of the United States.” On August 28th, the World Trade Organization (WTO) completed its interim ruling on this case and reportedly upheld virtually every point made by the United States in its complaint.

Secretary Lynn and Secretary Carter briefed us that the draft RFP for the KC-X Tanker could not reflect the unfair subsidies because the WTO report is "interim." However, this attitude belies the real character to the WTO's finding. Rarely does an interim ruling of the WTO change in any substantive way between an interim and final ruling. In the words of Ambassador Kirk, "the report itself is not a first step, but rather a critical step in *finalizing* this dispute. Furthermore, I point out that the reality of the situation is that the position of the United States Government is that reliance on unfair subsidies has been a longstanding practice for Airbus.

Among the unfair subsidies that Airbus received is \$5 billion in "Launch Aid" for the A-330 aircraft that is the basis for one of the tanker aircraft that will be proposed. This subsidy has enabled Airbus to finance the development of this aircraft at a significantly lower cost than would have been the case if it had obtained financing in the commercial marketplace where the real time value of money is taken into account.

In the face of a situation where the position of the U.S. government is that the commercial aircraft on which one bidder's aircraft is based has received unfair government subsidies, and that position now has been upheld by the WTO, the draft RFP proposes to include only a "hold harmless" provision that shields the taxpayer from future penalties that might be imposed. This provision does nothing to establish a fair competition where it is known that one offeror will be able to price its aircraft with the distorting effect of illegal government subsidies. In order to be fair, the RFP must be modified to neutralize the advantage that government subsidies give to one bidder.

In summary, I strongly urge the Department of Defense to inject more realism into critical elements of the RFP for the KC-X Tanker. As it stands, the draft RFP needs to be significantly improved in order to realistically reflect the life-cycle costs of fuel consumption and military construction. It also needs to reflect the reality of the distorting effects of unfair government subsidies that one bidder's aircraft has received. By incorporating the realism that I am calling for into these key portions of the RFP, the Department of Defense will close significant shortfalls in its quest to conduct a fair competition that delivers the best result for the warfighter and taxpayer.

Sincerely,



NORM DICKS
Member of Congress

Copy to:

Mr. William J. Lynn, Deputy Secretary of Defense

Dr. Ashton B. Carter, Under Secretary of Defense for Acquisition, Technology and Logistics