

Analysis of Section 305: Modification to Nontraditional Defense Contractor Definitions

Key Points

Section 305 of the Forged Act introduces significant changes to the definition of a Nontraditional Defense Contractor (NDC), expanding it beyond entities lacking recent traditional defense contract experience to include companies demonstrating rapid revenue growth, substantial reinvestment in research and development, or significant recent venture capital funding. This modification is intended to broaden the Department of Defense's (DoD) access to innovative companies, particularly those in the commercial technology sector, and facilitate the use of more flexible acquisition mechanisms. However, this expansion also presents potential challenges related to contractor experience, due diligence, and integration, necessitating proactive mitigation strategies and careful performance monitoring. The revised definition will directly impact various DoD personnel and may face opposition from traditional defense contractors and other stakeholders. Successful implementation will require additional resources, specialized training, and potentially updated systems. The effectiveness of this change will need to be measured through various metrics, and alternative approaches to engaging with non-traditional innovators should also be considered.

History of the recommendation

Analysis of the evolution of defense acquisition policy indicates a persistent need within the Department of Defense to accelerate the adoption of cutting-edge technologies and engage with a wider array of innovative companies. This imperative has become increasingly critical given the rapid advancements in commercial technology sectors relevant to national security. The current modification to the Nontraditional Defense Contractor definition, as outlined in Section 305 of the Forged Act, likely represents a continuation of ongoing efforts to refine the mechanisms for engaging with these non-traditional sources of innovation.

Prior legislative efforts and reports from bodies such as the Defense Science Board have likely explored various strategies to better integrate non-traditional entities into the defense industrial base. Section 305 can be viewed as a further iteration in this process, specifically targeting companies that exhibit strong growth potential or have attracted significant private investment. Examination of congressional records related to the Forged Act may reveal the specific rationale and legislative intent behind the inclusion of Section 305. Committee reports and floor debates could shed light on

why revenue growth, R&D investment, and venture capital funding were chosen as key indicators of a company's "nontraditional" status and its potential to contribute valuable innovation to the defense sector.

Organizations like the Defense Innovation Unit (DIU) have likely played a role in advocating for a broader definition of NDCs, drawing on their direct experience working with commercial technology companies and recognizing the limitations of the previous definition in capturing the full spectrum of relevant innovators. Their insights into the characteristics of successful commercial technology firms likely informed the development of the new criteria. The inclusion of specific financial and investment-based criteria in the revised definition suggests a recognition that traditional metrics of prior defense contracting experience might inadvertently exclude highly innovative and agile companies, particularly those operating in rapidly evolving technological landscapes. The focus on these metrics aims to identify companies demonstrating dynamism and investor confidence, regardless of their history with the DoD. Furthermore, the establishment of specific thresholds for revenue growth, R&D reinvestment, and venture capital funding likely reflects an attempt to strike a balance between identifying high-potential companies and ensuring that the criteria are achievable for a meaningful number of non-traditional entities. The detailed reasoning behind these particular percentages would warrant further investigation to fully understand their intended scope and impact.

Desired Effect of the recommendation

The primary desired effect of modifying the Nontraditional Defense Contractor definition through Section 305 is to enhance the Department of Defense's ability to engage with dynamic technology firms [Desired Effect 1]. By expanding the definition to include companies demonstrating rapid revenue growth, significant investment in research and development, or recent substantial venture capital funding, the DoD aims to lower the barriers for these innovative entities to participate in defense-related projects. Reports from organizations like the Defense Technical Information Center (DTIC) may underscore the DoD's continuous need for access to emerging technologies predominantly developed in the commercial sector.

A related desired effect is to increase the speed and agility of the acquisition process [Desired Effect 2]. By enabling a larger number of companies to qualify for streamlined acquisition pathways such as Other Transactions (OTs), the DoD anticipates a reduction in the delays often associated with traditional contracting methods. OTs offer more flexible terms and conditions, making them more appealing to companies that may be unfamiliar with or hesitant to navigate the complexities of

standard government contracting procedures. This flexibility is expected to facilitate faster procurement and fielding of new technologies.

Furthermore, the expanded definition is intended to foster greater innovation and competition within the defense industrial base [Desired Effect 3]. A larger pool of eligible non-traditional contractors has the potential to drive down costs and incentivize the development of more innovative solutions through increased competition for defense contracts. Government Accountability Office (GAO) reports have frequently highlighted the benefits of competition in defense acquisition, and this modification can be seen as a strategic move to inject more competitive dynamics into the process.

Another anticipated benefit is the diversification of the defense industrial base [Desired Effect 4]. By engaging with companies from diverse commercial sectors, the DoD seeks to reduce its reliance on a relatively limited number of traditional defense contractors. This diversification can lead to a more resilient industrial base and provide access to a broader range of technological capabilities and innovative approaches. Historical analyses of the defense industrial base might illustrate the ongoing efforts to modernize and diversify its participants.

Finally, the inclusion of companies that have recently secured significant venture capital funding aims to attract private sector investment into the development of technologies relevant to national security [Desired Effect 5]. Venture capital investment often serves as a strong indicator of a company's growth potential and the perceived value of its technology. By signaling a greater willingness to partner with such companies, the DoD hopes to encourage more private capital to flow into dual-use technologies with both commercial and military applications.

Potential Negative impacts of the recommendations

One potential negative impact of broadening the Nontraditional Defense Contractor definition is an increased risk associated with contractor inexperience in the specific requirements and regulations of defense contracting [Potential Negative impact 1]. Companies meeting the new financial criteria might lack familiarity with stringent security protocols, government accounting standards, and the intricacies of military specifications. This could potentially lead to performance issues, project delays, or cost overruns. While these companies may exhibit financial success in the commercial sector, their understanding of the unique demands of defense contracting might be limited.

Another potential negative outcome involves challenges in conducting thorough due diligence and ensuring accountability [Potential Negative impact 2]. The rapid growth and non-traditional nature of these companies could complicate the DoD's ability to comprehensively assess their capabilities, financial stability, and long-term viability as defense contractors. Traditional due diligence processes may need to be adapted to effectively evaluate companies with limited or no prior defense contracting history and potentially volatile growth patterns. Ensuring accountability and compliance with government regulations might also prove more challenging for these new entrants.

There is also a potential risk of attracting companies with a short-term focus and opportunistic behavior [Potential Negative impact 3]. The emphasis on recent financial performance and funding could incentivize the formation of companies primarily to capitalize on defense contracting opportunities, without a genuine long-term commitment to the defense sector or the development of sustainable defense capabilities. Such companies might prioritize short-term gains or achieving the next round of funding over the long-term needs of the DoD.

Furthermore, the new criteria could potentially disadvantage smaller, established niche technology providers [Potential Negative impact 4]. These companies might possess highly specialized and valuable technologies relevant to defense but may not meet the rapid growth or venture capital funding requirements of the revised definition. This could inadvertently narrow the pool of potential non-traditional partners by focusing on specific financial characteristics rather than the depth and relevance of their technological expertise.

Finally, integrating technologies and solutions from companies with non-traditional backgrounds into the complex ecosystem of existing defense systems and processes could present significant difficulties [Potential Negative impact 5]. These companies might employ different development methodologies, security standards, and integration philosophies compared to traditional defense contractors, potentially leading to interoperability issues or requiring substantial adaptation efforts. Ensuring seamless integration will necessitate careful planning, coordination, and potentially significant investment in bridging technological and procedural gaps.

Mitigations the organization will take to diminish the negative impacts

To mitigate the potential negative impact of increased contractor inexperience, the DoD should develop and implement tailored onboarding programs and educational resources specifically for non-traditional defense contractors [Mitigation of Negative Impact 1]. These programs could familiarize them with defense-specific regulations,

requirements, security protocols, and contracting processes. Mentorship programs pairing new entrants with experienced defense contractors could also prove beneficial in bridging the knowledge gap.

To address the challenges in due diligence and accountability, the DoD should enhance its due diligence processes to include specific assessments of the technical capabilities, financial stability, and long-term commitment of companies meeting the new NDC criteria [Mitigation of Negative Impact 2]. This could involve leveraging third-party expertise, developing specialized risk assessment frameworks, and incorporating performance-based metrics into contracts.

To mitigate the risk of short-term focus and opportunistic behavior, the DoD should implement robust oversight and performance monitoring mechanisms for contracts awarded to newly defined NDCs [Mitigation of Negative Impact 3]. This could include establishing clear milestones, conducting regular progress reviews, and employing stringent performance metrics. A phased approach to contract awards, starting with smaller initial contracts to assess capabilities before committing to larger-scale projects, could also help mitigate this risk.

To avoid disadvantaging smaller, established niche technology providers, the DoD should ensure that acquisition strategies continue to include set-asides or specific pathways for small businesses and niche technology providers that may not meet the new NDC growth criteria but offer valuable specialized capabilities [Mitigation of Negative Impact 4]. This could involve maintaining existing definitions or creating new categories within the "nontraditional" umbrella to ensure inclusivity and access to opportunities.

Finally, to address the difficulties in integrating non-traditional technologies and processes, the DoD should establish dedicated integration teams and develop clear standards, protocols, and technical assistance programs to facilitate the integration of technologies and solutions from non-traditional contractors into existing defense systems [Mitigation of Negative Impact 5]. Creating innovation labs or technology transition offices focused on this specific challenge could also prove effective.

DoD Personnel Most Affected

Contracting Officers will be significantly affected by the revised definition of an NDC [DoD Personnel Most Affected]. They will be responsible for interpreting and applying the new criteria when soliciting bids and awarding contracts. This will require them to develop expertise in evaluating non-traditional business models and financial metrics,

potentially increasing their workload as they engage with a larger pool of potential contractors. They may also face complexities in navigating different contracting authorities and negotiating contract terms with entities unfamiliar with traditional defense contracting.

Program Managers will also experience a significant impact as they oversee projects involving these newly defined NDCs. They will need to manage contractors with potentially varying levels of experience in defense contracting and ensure the successful integration of their technologies into existing systems. This may require adapting communication and collaboration strategies to different organizational cultures and potentially providing more guidance and support to less experienced contractors, leading to increased complexity in project management.

Technology Scouts and Innovation Officers, particularly those within organizations like the Defense Innovation Unit (DIU), will be at the forefront of identifying and engaging with companies that now qualify as NDCs under the expanded definition. This will result in a significantly larger and more diverse pool of potential partners to identify and assess, requiring these personnel to develop a broader understanding of various commercial technology sectors and business models.

Legal Counsel within the DoD will play a crucial role in interpreting the legal implications of the revised definition and providing guidance on its application in contracting and other agreements. They may face increased demand for legal interpretations of the new criteria and potential complexities in applying existing legal frameworks to these new types of contractors.

Auditors and Compliance Officers will be responsible for ensuring that contracts awarded under the new definition comply with relevant regulations and that taxpayer funds are being used appropriately. They may need to adapt their audit methodologies to assess the financial and operational practices of companies with different business models and levels of experience in government contracting.

Stakeholders opposed and rationale for Opposition

Traditional Defense Contractors are likely to be among the stakeholders who may oppose the expanded definition of Nontraditional Defense Contractors. They may view this change as increasing competition for defense contracts, potentially eroding their market share and profitability. Their rationale for opposition could stem from the perception that the new criteria prioritize financial metrics over proven experience and reliability in defense contracting, potentially leading to a shift in contract awards

towards less experienced companies. They may also have concerns about the long-term commitment and sustainability of these new entrants in the defense sector.

Some Government Oversight Bodies, such as elements within the Government Accountability Office (GAO) or Inspectors General offices, might also express opposition. Their concerns could center on the potential for increased risk of fraud, waste, and abuse associated with contracting with companies that have limited experience with government regulations and oversight. They may question the rigor and appropriateness of the new eligibility criteria and express concerns about financial accountability and the adequacy of oversight mechanisms for companies with non-traditional business models.

Small, Established Niche Technology Providers who may not meet the new growth or funding criteria could also oppose the revised definition. They might perceive that the new criteria favor larger, faster-growing companies over smaller, more focused entities with deep expertise in specific areas, potentially limiting their access to defense contracts despite possessing highly specialized and valuable technologies relevant to defense.

Potentially, Unions Representing Workers at Traditional Defense Contractors might also oppose the change. If the shift towards non-traditional contractors leads to a decrease in contract awards for traditional defense firms, unions may have concerns about potential job losses and the erosion of the established defense industrial base workforce. Their rationale would be rooted in the fear of job displacement and a weakening of the traditional defense industrial base workforce due to increased competition from non-traditional sources.

Additional Resources

Successful implementation of the revised Nontraditional Defense Contractor definition will likely require several additional resources within the Department of Defense. Increased funding will likely be necessary to support the implementation efforts, including resources for training DoD personnel on the new definition and how to effectively engage with non-traditional contractors. Additional funding may also be needed to enhance due diligence capabilities, develop new oversight mechanisms tailored to these types of companies, and potentially establish dedicated offices or teams to manage relationships with them.

Comprehensive and specialized training programs will be essential for DoD personnel, particularly contracting officers, program managers, and technology scouts, to fully

understand the nuances of the new NDC definition. This training should cover how to evaluate non-traditional business models and financial metrics, as well as how to navigate the complexities of contracting with these entities.

The DoD may also need to hire or assign personnel with specific expertise in areas such as venture capital, high-growth technology companies, intellectual property, and non-traditional acquisition methods to effectively engage with and manage relationships with the newly defined NDCs. Their specialized knowledge will be crucial in assessing the capabilities and potential risks associated with these companies.

Existing acquisition systems and processes might need to be updated or new tools developed to better track and manage information related to non-traditional contractors, assess their capabilities, and monitor their performance. This could include enhancing data analytics capabilities and potentially developing dedicated platforms for engaging with non-traditional innovators.

Finally, the development of clear guidance documents, best practices, and standardized procedures for implementing the revised NDC definition will be crucial for ensuring consistent and effective application across the DoD. This could involve creating a dedicated center of excellence or establishing interagency working groups focused on non-traditional acquisition.

Measures of Success

The success and effectiveness of the modified Nontraditional Defense Contractor definition can be measured through several key indicators. One important metric will be the increase in the number of new NDCs engaged by the DoD, specifically tracking companies that qualify under the revised criteria and successfully enter into contracts, Other Transactions, or other agreements.

Another measure of success will be the acceleration of technology adoption, assessing the time it takes for new technologies developed by these newly defined NDCs to transition from initial engagement to operational use within the DoD. This will indicate whether the revised definition is indeed facilitating faster access to innovative solutions.

The success rate and total value of Other Transaction agreements awarded to companies qualifying as NDCs solely based on the new financial or funding criteria will also be a critical metric. This will demonstrate the extent to which the revised definition is enabling the use of more flexible acquisition pathways with the intended

target audience.

Innovation metrics, such as the number of patents filed, the development of novel solutions to critical defense challenges, or the introduction of disruptive technologies by these new NDCs, can also be used to assess the impact of the revised definition on the overall level of innovation within the defense sector.

The cost and schedule performance of projects where newly defined NDCs are the prime contractors or key subcontractors should be tracked and compared to projects involving traditional defense contractors to assess the efficiency and effectiveness of these new partnerships.

The extent to which the revised definition leads to a more diverse range of companies contributing to the defense industrial base, including companies from sectors not traditionally associated with defense contracting, will also be an important measure of success.

Finally, regularly soliciting feedback from DoD personnel, such as contracting officers, program managers, and technology scouts, on their experiences working with newly defined NDCs can provide valuable qualitative data and identify areas for improvement in the implementation process.

Alternative approaches

Several alternative approaches could potentially achieve similar outcomes of engaging non-traditional innovators with the DoD, perhaps more effectively or efficiently than the broad modification outlined in Section 305 [Alternative approaches]. One alternative is to implement enhanced outreach and technology scouting programs. Instead of broadly redefining NDCs, the DoD could invest more in proactively identifying and engaging with companies possessing specific critical technologies, regardless of their revenue growth or funding status. This could involve dedicated teams focused on specific technology areas or increased participation in industry conferences and events. This approach could offer a more targeted way to access desired capabilities without the potential downsides of a broad definitional change.

Another alternative is to significantly expand the use of prize challenges and innovation platforms. These mechanisms can attract a wider range of non-traditional innovators to address specific defense needs without requiring them to become traditional contractors or meet specific financial criteria. Prize challenges and hackathons can lower the barrier to entry for participation in defense innovation and

attract a diverse set of problem-solvers.

Creating specialized funding mechanisms for early-stage technology companies could also be a more targeted approach. Expanding programs like the Small Business Innovation Research (SBIR) or Small Business Technology Transfer (STTR) specifically tailored to the needs of early-stage companies could provide financial support and incentivize their engagement with the DoD without altering the fundamental definition of an NDC. Targeted funding can directly support innovation and incentivize participation from companies that might not yet meet the growth or funding criteria of the revised NDC definition.

Instead of relying heavily on the OT authority, the DoD could focus on streamlining its traditional Federal Acquisition Regulation (FAR)-based acquisition processes to make them more accessible and attractive to non-traditional companies. This could involve reducing bureaucratic hurdles, simplifying requirements, and shortening procurement timelines. Addressing the underlying complexities and inefficiencies of traditional acquisition might be a more fundamental solution to attracting non-traditional innovators.

Finally, fostering the formation of public-private partnerships and consortia focused on specific technology areas could facilitate collaboration between traditional defense contractors, non-traditional innovators, and academic institutions. This collaborative approach can leverage the strengths of different types of organizations and create a more integrated innovation ecosystem, promoting technology transfer and the development of innovative solutions.

Section Specific Question 1:

- **Specific Changes to the NDC Definition:** Section 305 of the Forged Act amends Section 3014 of Title 10, United States Code, to modify the definition of a "Nontraditional Defense Contractor." Previously, an NDC was defined as an entity that is not currently performing and has not performed, for at least the one-year period preceding the solicitation, any contract or subcontract subject to full coverage under the cost accounting standards prescribed pursuant to section 1502 of title 41. The amendment introduces two additional pathways for an entity to qualify as an NDC. Now, an entity is also considered an NDC if it:
 - **(1)** Certifies that, for the ultimate parent company's three audited annual financial statements preceding the solicitation, it has achieved more than 30 percent year-over-year revenue growth.
 - **(2)** Certifies that it has reinvested back into the business more than 10 percent of its revenue through non-reimbursable research and development

for the ultimate parent company's three audited annual financial statements preceding the solicitation.

- **(3)** Certifies that it has raised funding through third-party sources in exchange for equity amounting to a minimum of 5 percent of the value of the company's total outstanding shares within the last two years.
- **Impact on Eligibility for Acquisition Authorities (like OTs):** These changes are specifically designed to broaden the scope of what constitutes a Nontraditional Defense Contractor, thereby increasing the number of companies eligible to utilize certain acquisition authorities that are specifically intended for engagement with such entities. The most notable of these is the use of Other Transactions (OTs) under 10 U.S.C. § 4021. OTs offer significantly more flexibility in terms and conditions compared to traditional Federal Acquisition Regulation (FAR)-based contracts, making them a more attractive option for companies that may be unfamiliar with or unwilling to accept the standard requirements of government contracting. By meeting any one of the newly established criteria—achieving high revenue growth, demonstrating substantial R&D reinvestment, or securing significant recent venture funding—a company can now qualify as an NDC. This qualification then opens the door to potentially accessing these more flexible acquisition pathways, facilitating greater collaboration between the DoD and a wider range of innovative commercial entities for the development and procurement of cutting-edge technologies and solutions.

Section Specific Question 2: This section requires further clarification. Please provide the specific question you would like addressed in this section.

Summary

Section 305 of the Forged Act marks a significant evolution in the Department of Defense's approach to engaging with non-traditional innovators. By incorporating financial performance and investment metrics into the definition of a Nontraditional Defense Contractor, the provision aims to expand the DoD's access to a wider array of dynamic and innovative companies, particularly those in the commercial technology sector. This expansion is primarily intended to accelerate the adoption of cutting-edge technologies and diversify the defense industrial base through increased utilization of flexible acquisition mechanisms like Other Transactions. However, the implementation of this revised definition also presents potential challenges related to contractor experience, due diligence processes, and the integration of non-traditional technologies. To mitigate these risks, the DoD will need to implement tailored onboarding and oversight strategies, invest in specialized training and resources for its personnel, and carefully monitor the outcomes of this change. While the revised

definition offers a promising avenue for enhancing defense innovation, alternative approaches to engaging with non-traditional innovators should also be considered as part of a comprehensive strategy. Ultimately, the success of Section 305 will depend on the DoD's ability to effectively leverage the expanded definition to foster meaningful partnerships with innovative companies while safeguarding against potential risks and ensuring the responsible use of taxpayer resources.