[H.A.S.C. No. 112–142]

SEQUESTRATION IMPLEMENTATION OPTIONS AND THE EFFECTS ON NATIONAL DEFENSE: INDUSTRY PERSPECTIVES

COMMITTEE ON ARMED SERVICES
HOUSE OF REPRESENTATIVES

ONE HUNDRED TWELFTH CONGRESS

SECOND SESSION

HEARING HELD
JULY 18, 2012

U.S. GOVERNMENT PRINTING OFFICE

75–666 WASHINGTON : 2012

For sale by the Superintendent of Documents, U.S. Government Printing Office,
http://bookstore.gpo.gov. For more information, contact the GPO Customer Contact Center,
U.S. Government Printing Office. Phone 202–512–1800, or 866–512–1800 (toll-free). E-mail, gpo@custhelp.com.

HOUSE COMMITTEE ON ARMED SERVICES

ONE HUNDRED TWELFTH CONGRESS

HOWARD P. "BUCK" MCKEON, California, *Chairman*

ROSCOE G. BARTLETT, Maryland
MAC THORNBERRY, Texas
WALTER B. JONES, North Carolina
W. TODD AKIN, Missouri
J. RANDY FORBES, Virginia
JEFF MILLER, Florida
JOE WILSON, South Carolina
FRANK A. LOBIONDO, New Jersey
MICHAEL TURNER, Ohio
JOHN KLINE, Minnesota
MIKE ROGERS, Alabama
TRENT FRANKS, Arizona
BILL SHUSTER, Pennsylvania
K. MICHAEL CONAWAY, Texas
DOUG LAMBORN, Colorado
ROB WITTMAN, Virginia
DUNCAN HUNTER, California
JOHN C. FLEMING, M.D., Louisiana
MIKE COFFMAN, Colorado
TOM ROONEY, Florida
TODD RUSSELL PLATTS, Pennsylvania
SCOTT RIGELL, Virginia
CHRIS GIBSON, New York
VICKY HARTZLER, Missouri
JOE HECK, Nevada
BOBBY SCHILLING, Illinois
JON RUNYAN, New Jersey
AUSTIN SCOTT, Georgia
TIM GRIFFIN, Arkansas
STEVEN PALAZZO, Mississippi
ALLEN B. WEST, Florida
MARTHA ROBY, Alabama
MO BROOKS, Alabama
TODD YOUNG, Indiana

ADAM SMITH, Washington
SILVESTRE REYES, Texas
LORETTA SANCHEZ, California
MIKE MCINTYRE, North Carolina
ROBERT A. BRADY, Pennsylvania
ROBERT ANDREWS, New Jersey
SUSAN A. DAVIS, California
JAMES R. LANGEVIN, Rhode Island
RICK LARSEN, Washington
JIM COOPER, Tennessee
MADELEINE Z. BORDALLO, Guam
JOE COURTNEY, Connecticut
DAVE LOEBSACK, Iowa
NIKI TSONGAS, Massachusetts
CHELLIE PINGREE, Maine
LARRY KISSELL, North Carolina
MARTIN HEINRICH, New Mexico
BILL OWENS, New York
JOHN R. GARAMENDI, California
MARK S. CRITZ, Pennsylvania
TIM RYAN, Ohio
C.A. DUTCH RUPPERSBERGER, Maryland
HANK JOHNSON, Georgia
BETTY SUTTON, Ohio
COLLEEN HANABUSA, Hawaii
KATHLEEN C. HOCHUL, New York
JACKIE SPEIER, California
RON BARBER, Arizona

ROBERT L. SIMMONS II, *Staff Director*
JACK SCHULER, *Professional Staff Member*
WILLIAM (SPENCER) JOHNSON, *Professional Staff Member*
LAUREN HAUHN, *Research Assistant*

CONTENTS

CHRONOLOGICAL LIST OF HEARINGS

2012

WEDNESDAY, JULY 18, 2012

SEQUESTRATION IMPLEMENTATION OPTIONS AND THE EFFECTS ON NATIONAL DEFENSE: INDUSTRY PERSPECTIVES

STATEMENTS PRESENTED BY MEMBERS OF CONGRESS

WITNESSES

APPENDIX

SEQUESTRATION IMPLEMENTATION OPTIONS AND THE EFFECTS ON NATIONAL DEFENSE: INDUSTRY PERSPECTIVES

HOUSE OF REPRESENTATIVES,
COMMITTEE ON ARMED SERVICES,
Washington, DC, Wednesday, July 18, 2012.

The committee met, pursuant to call, at 10:22 a.m. in room 2118, Rayburn House Office Building, Hon. Howard P. "Buck" McKeon (chairman of the committee) presiding.

OPENING STATEMENT OF HON. HOWARD P. "BUCK" MCKEON, A REPRESENTATIVE FROM CALIFORNIA, CHAIRMAN, COMMITTEE ON ARMED SERVICES

The CHAIRMAN. The hearing will come to order. Good morning, ladies and gentlemen. The House Armed Services Committee meets today to receive testimony from our industry partners on the challenges of planning for sequestration. Since we began this hearing series back in September of last year, we have held seven hearings and one briefing on sequestration, the bulk of which have delved into the impact of sequestration on our military capabilities and national defense.

Today we are holding our second hearing that is focused on the economic impact of sequestration, this time focused on the implications for the defense industrial base that enables and supports our warfighters. Joining us today are Mr. Bob Stevens, Chairman and CEO [Chief Executive Officer] of Lockheed Martin; Mr. Sean O'Keefe, Chairman and CEO of EADS North America; Mr. David Hess, President of Pratt & Whitney; and Ms. Della Williams, President and CEO of Williams–Pyro. In addition to their own companies' perspectives, I should note that Mr. O'Keefe also chairs the National Defense Industrial Association and Mr. Hess chairs the Aerospace Industries Association. Ms. Williams is on the board of the National Association of Manufacturers.

Barring a new agreement between Congress and the White House on deficit reduction, over a trillion dollars in automatic cuts, known as sequestration, will take effect. Although the House has passed a measure that would achieve the necessary deficit reduction to avoid sequestration for a year, the Senate has yet to consider legislation, and the President's budget submission, which sought $1.2 trillion in alternative deficit reduction through increased tax revenue, was defeated in a bipartisan and bicameral manner.

This impasse and lack of a clear way forward has created a chaotic and uncertain budget environment for industry and defense planners. While the cuts are scheduled for implementation January

2nd, companies are required to assess and plan according to the law, and sequestration is the law right now.

We have all heard the growing number of estimates. Secretary Panetta has warned sequestration would be catastrophic to our military and result in the loss of one-and-a-half million jobs and a 1-percent increase in the unemployment rate. This would send 200,000 of our men and women in uniform from the frontline to the unemployment line. It would, as the Secretary has said, result in the smallest ground force since 1940, the smallest number of ships since 1915, and the smallest Air Force in its history.

The National Association of Manufacturers warned that dramatic cuts in defense spending under the Budget Control Act of 2011 will have a significant negative impact on U.S. jobs and economic growth. The manufacturers' forecast and one by Dr. Stephen Fuller, on behalf of the Aerospace Industries Association, have estimated private sector job losses at over a million.

Faced with the prospect of being forced to lay off workers, renegotiate contracts, disrupt production, and give bad news to the shareholders, industry leaders have been attempting to get more guidance from the Administration on how they will interpret and implement the law. To date, the guidance has been piecemeal. For example, last fall the Pentagon stated that war funding would not be sequestered. Then in May the OMB [Office of Management and Budget] overruled the Department and declared that while veterans' benefits would be exempt, funding for the troops on the frontline would not be exempt. In June 2012, Secretary Panetta met with various defense industries executives to discuss the impact of sequestration on their operations and to gauge the current state of the industry in general. In addition, press reports indicate that the Director of the Office of Management and Budget met separately with heads of several major defense companies.

Unfortunately, it doesn't sound like industry learned much from those meetings. Reports indicate OMB made it clear that it does not plan to issue implementation guidance until at least November, less than 2 months before sequestration is scheduled to take effect. My fear is that the guidance will come much too late. Industry faces a host of planning challenges and requirements to be met this summer, not the least of which is the WARN [Worker Adjustment and Retraining Notification] Act, which requires most employers to provide notification at least 60 calendar days in advance of mass layoffs and plant closings. In some States the requirement is 90 days. That means, as we will hear today, defense companies are currently grappling with whether to send pink slips by November 3rd to their employees.

In addition to the issue of jobs, I worry that the cavernous silence from the President will lead many to exit the industry or to walk away from capital investments that are in the best interests of our troops. As I have said many times before, the men and women on the front lines have our backs. Who is going to have theirs if we allow the impending threat of sequestration to shutter the American industrial machine that enables them to fight, win, and return home safely?

This overdue guidance from the Administration on how they intend to interpret the law and implement sequester mechanically is critical to employers, not to mention Congress, and I look forward to our follow-on panel with the Director of the OMB on August 1st.

We all believe there is strong, bipartisan agreement that sequester is bad policy and should be replaced. My hope is this hearing will provide additional incentives for the Administration to provide more information to employers and for all parties to resolve this impasse, and I look forward to your insights today.

Mr. Smith.

[The prepared statement of Mr. McKeon can be found in the Appendix on page 47.]

STATEMENT OF HON. ADAM SMITH, A REPRESENTATIVE FROM WASHINGTON, RANKING MEMBER, COMMITTEE ON ARMED SERVICES

Mr. SMITH. Thank you, Mr. Chairman. I thank our witnesses for being here to discuss this very important subject and to give their perspectives on it. As some of our leading employers in the defense industry, their perspectives are critically important as we go forward, both in terms of the industrial base issues and in terms of the impact on our broader national security, and I completely agree with the chairman that sequestration is not a good idea. It would be bad for our economy, bad for defense. I always hasten to point out not just defense, it is, you know, a sort of mindless across-the-board cut in all discretionary spending. So education, transportation, infrastructure, on down the line—it would have a devastating impact, and part of the problem in addition to that is that the Budget Control Act was not particularly well drafted. I have heard dozens of different opinions about what it means and what exact effect it would have, what is exempt, what isn't exempt, how would you implement it. Nobody knows for sure until we actually do it. That is part of what the Administration is wrestling with.

So I don't think there is any dispute that it is bad. I have not heard the White House dispute that. Secretary Panetta, in particular, has been very forceful on explaining how awful sequestration will be. The problem is, it is not like you can really come up with a plan that is going to make it anything other than awful. The burden, the real burden of this committee, this House, and the Senate, and the President is to get rid of it one way or the other, to make sure that it doesn't happen. If it happens, it will have a very profound and negative impact. And it is also worth pointing out and I think the chairman has done an excellent job of this, this is a problem right now. We tend to look at it and say, well, sequestration kicks in on January 1st and people begin to imagine that that is the deadline. But all of you and thousands of other employers are making decisions right now based on what they reasonably project will happen in the next fiscal year, and those decisions are leading to people hiring less people and in some cases laying them off in anticipation that cuts will come one way or the other. So it definitely needs to be avoided.

But we also need to look at the larger problem in terms of what got us into this and why we are having such a devil of a time getting out of it. There seems to be this opinion that while this is a terrible, terrible thing and it is just sort of fundamental incompetence that is preventing us from dealing with it, it is really not.

It is more denial about the fiscal situation we are in. Let's go back to the fact that we are only here because of the refusal of the majority of people in the House to raise the debt ceiling. This deal was done as the only way to raise the debt ceiling and stop the United States of America from defaulting on its obligations for the first time. It was only that sort of blind notion that somehow not raising the debt ceiling was a solution to our fiscal problems that forced us into this awful, awful decision, an awful decision which I didn't support, mainly because it put all of the burden on the discretionary budget.

We unquestionably have a budget problem, we have a $1.2 trillion deficit, actually 1.3 last year, a 38-percent deficit, and it needs to be addressed. Thus far we have put all of the burden of that on the backs of 38 percent of the budget, which is the discretionary spending budget, and we have refused to talk about revenue. So the solution going forward, the thing that will help us come together and come up with the deficit control steps necessary to avoid sequestration is, number one, admit that we are not balancing the budget anytime soon. We would all love to have a balanced budget, but there isn't an economist out there that won't tell you doing that in the near term would be devastating to the economy. We are going to have structural deficits for a while. Our role is to get those deficits under control so that they are manageable, but we can't hold hostage steps that will do that to the notion that we have to have a balanced budget right now or even in the next 3, 4, 5, 6 years. So admit that. And then, second, everything has to be on the table. We are going to need more revenue. We have cut taxes across the board over the course of the last 10 or 12 years. If we are truly, truly committed to providing for the men and women who serve us and providing for our national security, then we absolutely have to be willing to raise the revenue to pay for that. That is a critical, critical piece of it. And, yes, we also have to look at the other 62 percent of the budget, the mandatory spending, and find savings there as well. So that sort of a sort of realistic discussion is needed. Right now there seems to be this desire for a balanced budget. Also a desire to not raise revenue and a desire not to cut any spending that is important. Those numbers don't add up.

So I hope this committee can begin to be part of the process of starting a realistic debate that can avoid the truly awful outcome that would come with sequestration and the awful outcome that is coming every day, every day that we delay in making it clear that we are not going to do sequestration.

So I think this hearing is very appropriate. I thank the chairman for having it. I look forward to the testimony and the discussion. Thank you.

[The prepared statement of Mr. Smith can be found in the Appendix on page 49.]

The CHAIRMAN. Thank you, Mr. Smith. And thank you again, each of you, for being here today. This is probably one of the most important hearings I can remember attending, and we really appreciate your willingness to be here. Your—Mr. Stevens, if you will begin, please.

STATEMENT OF ROBERT J. STEVENS, CHAIRMAN AND CHIEF EXECUTIVE OFFICER, LOCKHEED MARTIN

Mr. STEVENS. Thank you, Mr. Chairman. Good morning. Chairman McKeon, Ranking Member Smith, distinguished Members of the committee, I thank you very much for this opportunity to express our industry perspectives on the impact of sequestration. With your permission, I will submit a prepared statement for the record and offer now a brief summary.

The CHAIRMAN. With no objection, so ordered. And that would go for each of you.

Mr. STEVENS. Thank you, sir. As Chairman and Chief Executive Officer of Lockheed Martin, I am enormously proud to represent 120,000 hard-working, patriotic women and men who are the foundation of our business. We are a global security company operating in 50 States and 75 countries. Our workforce includes 61,000 scientists and engineers and 26,000 military veterans. Year in and year out our company consistently hires the largest number of graduating engineers from U.S. universities compared to any other company. We receive more than a million résumés each year from highly talented people who have a strong desire to deliver the next generation of technology that will help keep our Nation safe and secure and ensure the United States leads the world.

Lockheed Martin is also the largest provider of information technology services to the Federal Government, and we have a business presence in virtually every Federal department or agency, including the Social Security Administration, the National Institutes of Health, the Veterans Administration, the Department of Homeland Security, and the Federal Aviation Administration, just to name a few. So the men and women of our company play an important role in America's future, and we all take that responsibility seriously.

Sequestration jeopardizes that future. From a national security perspective, Defense Secretary Leon Panetta has spoken in the strongest possible terms against sequestration. He said this process will have catastrophic consequences for our Nation's defense, and he described it as a meat ax. It is. Sequestration's automatic trigger and across-the-board cuts were developed independent of any correlation with national security strategy, force structure, technology needs or operational reality, and those cuts will be detrimental.

From an industry perspective, our near-term horizon is completely obscured by a fog of uncertainty. With just 167 days remaining until it takes effect, we have little insight as to how sequestration will be implemented and no insight into which programs will be curtailed, which sites will be closed, which technologies will be discontinued, which contracts will be reformed, and which suppliers, particularly small businesses who are so vital to our supply chain, will be shut down or severely crippled. Most tragically, we fear we will be unable to provide the equipment and support needed by our military forces, and we are unable to reliably estimate how many employees are going to lose their jobs and how many families are going to be disrupted.

It might be flattering to believe that our industry is so robust and so durable that it could absorb the impact of sequestration without breaking stride, but that is a fiction. The impact on our industry would be devastating, with a significant disruption in ongoing programs and initiatives leading to facility closures and personnel reductions that would severely disrupt advanced manufacturing operations, erode engineering expertise, and accelerate the loss of skills and knowledge. In short, it will undermine our aerospace and defense industrial base, which I believe is one of the crown jewels of the American economy and is strategically vital to our country.

Beyond defense, I think the broader consequences of sequestration also are not well understood. The abruptness and across-the-board nature of the cuts will hit hard virtually all domestic discretionary accounts as well, and since most of our domestic departments and agencies don't have substantial capital acquisition accounts like the Department of Defense, that means the cuts will come from people, through significant work furloughs and personnel reductions that will likely constrain agencies from providing essential support and services and fulfilling their missions.

In short, sequestration constitutes blunt-force trauma. It is likely to tear the fabric of our industry, adversely affect our national security, and impair our domestic agencies.

Mr. Chairman, I don't profess to have the wisdom or expertise to give counsel to this committee or to Congress on the precise path forward to resolve all the fiscal challenges that our Nation is facing, but I have spent decades of my professional working life in the national security arena, and I have never been as concerned over the risk to the health of our industry and our Government enterprise.

Sequestration has been described many times to me as a doomsday device, as a threat that was designed never to happen, but the effects of sequestration are being felt right now throughout our industry. Every month that goes by without a solution is a month of additional uncertainty, deferred investment, lost talent, and ultimately increased costs.

Respectfully, I urge you to take action to stop the sequestration process and ask that you do so soon. Thank you, sir.

[The prepared statement of Mr. Stevens can be found in the Appendix on page 51.]

The CHAIRMAN. Thank you very much.

Mr. O'Keefe.

STATEMENT OF SEAN O'KEEFE, CHAIRMAN AND CHIEF EXECUTIVE OFFICER, EADS NORTH AMERICA, AND CHAIRMAN, NATIONAL DEFENSE INDUSTRIAL ASSOCIATION

Mr. O'KEEFE. Thank you, Mr. Chairman, Members of the committee, I appreciate the opportunity to appear here today on behalf of the 90,000 members of the National Defense Industrial Association, which I serve as chair, in addition to representing EADS, which is the world's largest aerospace and defense company.

I am particularly cursed by a memory of how this particular provision of public finance was first introduced into the Federal process as a mechanism to enforcing some measure of discipline, given my prior public service experience. Gramm-Rudman-Hollings, when it was enacted in the mid-1980s, was intended particularly to be indiscriminate by its precision to be exacting. Across the board by precisely the same amounts, the logic was, 25 years ago when it was enacted was that the method was a substitute for rational judgment and choice of priorities because the process had failed to reach consensus on what those priorities would be, and so therefore an exacting precise amount with an indiscriminate application was enacted. The logic was also that this method was devoid of any priority selection and that nothing would be more affected and so therefore there were no priorities. If everything is the same priority, there are no priorities of any substance. And finally, the logic was this resource management mechanism was so stupid that the threat of it would be a prompt all by itself to public leaders to avoid it at any cost.

That was the logic, quaint as it sounds, 25 years ago. But it has been adopted a year and a half ago or a year ago, excuse me, as a mechanism now of enforcement following the debt limit extension provisions that were then subsequently enacted in order to force this again. The consequences of this are serious. Bob Stevens has talked through a variety of very particular reference that would be applicable, but the percentage that is to be applied, while it ranges anywhere in the single digits to very low double digits, may sound like that is not going to be much of an impact masks the real consequence of this. The most severe is the administrative disruption that will likely cost almost as much as what this mechanism is designed to save. So by however much is sequestered, taken across the board without priority, without particular application to any sense of its value one way or the other in which body armor contracts are valued at exactly the same value as cutting grass at military bases, that the consequence of that may sound like it is going to be exacting in its precision, but indeed the administrative effort to implement it will be much more disruptive than anything else. It is going to force inefficiencies, as it has in the past in much smaller applications of this provision, and that has been demonstrated and documented in terms of its extent. It is going to implement and force any number of contract penalties. It will terminate a variety of different programs because there are some efforts to select within the amounts that are identified by the very wonkish-sounding program, project, and activity definitions, and even those definitions I think as Congressman Smith highlighted are still in dispute and argument over exactly how they would be applied. So that will extend this even further. Unit costs will certainly increase as there is a change in quantities by contract. The cost of capital for smaller second- and third-tier suppliers will almost certainly go up as financing expenses just to meet the cash flow requirements as progress payments are disrupted, and then once that is settled, Prompt Pay Act penalties will then be applied as well. Bob Stevens spoke to the, as well as the chairman spoke to the WARN Act provisions, that is going to be an across-the-board disruptive effort, and indeed that has already started in some cases by notification to many of you and your colleagues as well as Governors in 50 States that indeed this provision may, in fact, have to be implemented. So it has already begun.

The impact on second- and third-tier suppliers, of which the National Defense Industrial Association, most of its members represent or are a part of that, is going to be very, very significant in that regard, and the disruption in that particular market is going to be one that may not sound like, again, the percentage sounds like a very big deal. But just take, for example, some of the suppliers to my company, EADS, which does purchases $15 billion worth of commercial and other activities in the United States every year on an annual basis. Seventy percent of what we do is commercial, 30 percent is related to public contracts. And yet many of the suppliers are much the same for aerospace articles that apply in some circumstances to defense equipment and in other cases of which again we do roughly 30 percent, the other bulk of it is towards the commercial side of the equation. The cost of doing business for many of the second- and third-tier providers is going to go up significantly because some of those providers will elect to either exit one element of the market, defense in particular or public spending in particular, and as a consequence the options for competition to maintain cost competitiveness is going to become much stiffer in the $15 billion a year that my company invests every year to purchase goods and services in the United States. Some of those subtier providers will exit the market, and when they do there will be less choice and the cost of doing business will go up.

In the defense market that is particularly true since those same products, identical in many respects in a commercial or military sale, costs in a public market at least on the order of 20 percent more to do business. Those suppliers who are providing in both markets will exit the public defense market faster than any other, just to shed that 20 percent overhead that it costs to do business there. And so as a consequence, it becomes an easy choice or one that they are driven to in order just to survive in many cases. And that is an opportunity at the same time to examine what that cost of doing business is uniquely to the public sector. If every article or most require roughly the same comparability of its application in a commercial or defense context, why does it cost that much more just to sell to the public? And that has an opportunity for reexamination.

The Defense Business Board has advocated what is now called a regulatory holiday. During the 1990s in the post-Cold War period the Administration at that time referred to this as a procurement holiday. Let's just stop buying things, we have got enough of an inventory, no need to buy more. Well, the same could be applied in these particular cases, in which 20 percent of the cost that is applied just to do business with the public could be reexamined on a case-by-case basis. But to demonstrate why it ought to stay there as opposed to be just accepted and therefore be justified on each occasion, they have come up with—the business board has come up, the Defense Business Board has come up with a very creative method to do that, and that is to be advanced as one method in the alternative to looking at a mindless across-the-board application of no-priority, everything-is-a-priority kind of reduction. And that is an overhead that I would encourage as an opportunity to really look at what those expenses could be to yield a lower cost and ultimately the kind of savings that are to be accrued.

Lost in all this, though, and maybe this is the most important element, is that while there will be, there is no doubt, almost to equal proportion a reduction in this area of the domestic discretionary appropriations, as again Congressman Smith described, it nonetheless is going to resonate in a different way. We are looking at dominantly public servants or delivery of public services that require personnel, and as a result how the Federal Government goes about the process of determining how those reductions will be made is something yet to be heard from. So while there may be a prospect of fewer TSA [Transportation Security Administration] agents at the airports on any given day or flight disruptions as a consequence of the FAA [Federal Aviation Administration] air traffic controllers not being asked to report for duty that day, and there will be fewer research grants because the NIH [National Institutes of Health] or the National Science Foundation is withholding the grant that was required through a university for some research activity. All those are severe impacts. But by comparison to the impact that will be particularly on the Armed Forces of the United States, men and women in service who voluntarily are there in order to defend us, that impact is going to be particularly profound on them and their families. And it is worthy, therefore, of consideration of what that consequence will be that is far greater than anything we are talking about here this morning on the industry.

The CHAIRMAN. Mr. O'Keefe, are you close to——

Mr. O'KEEFE. I am done. I simply would want to add, I commend the committee for seeking some resolution to this issue, and I very much appreciate the opportunity to testify. Thank you.

[The prepared statement of Mr. O'Keefe can be found in the Appendix on page 68.]

The CHAIRMAN. Thank you very much.

Mr. Hess.

STATEMENT OF DAVID P. HESS, PRESIDENT, PRATT & WHITNEY, AND CHAIRMAN, AEROSPACE INDUSTRIES ASSOCIATION

Mr. HESS. Chairman McKeon, Ranking Member Smith, and Members of the committee——

The CHAIRMAN. Is your mike on?

Mr. HESS. I believe it is, sir. Is that better?

The CHAIRMAN. You have to get it right close.

Mr. HESS. Thank you, sir.

Chairman McKeon, Ranking Member Smith, and other Members of the committee, I appreciate the opportunity to testify before you today regarding the serious matter of the potential for sequestration and the implications it has to our defense industry.

As you know, I wear two hats currently. One is the President of a $13 billion company that employs more than 36,000 employees worldwide, and second as the Chairman of the Aerospace Industries Association, which represents 300 aerospace companies across the United States which collectively account for about 90 percent of the revenues for the entire—for the aerospace and defense industry. I commend the committee on assembling such a representative group of witnesses to provide diverse answers based on the different challenges faced by each of us in the coming months.

As chairman of AIA [Aerospace Industries Association], it has been my privilege to visit Capitol Hill on numerous occasions to outline what we see with regard to sequestration, the potential to affect over one million highly skilled, highly compensated aerospace and defense-related jobs. AIA's second-to-none advocacy campaign has been spreading throughout the country with grassroots rallies highlighting the importance of fixing sequestration versus suffering its consequences.

As an industry, we are already seeing the impacts of potential sequestration budget cuts today. Companies are limiting hiring and halting investments largely due to the uncertainty about how sequestration cuts would be applied. At our UTC [United Technologies] sister division, Sikorsky, the leadership has already indicated that given this environment, if they had to choose right now between investing an internal R&D [Research & Development] dollar between a commercial and defense program, they would choose commercial programs because of the uncertainty in the defense budget, and that is considering there is a fair amount of uncertainty in the commercial environment right now. Equally concerning are the impacts of sequestration on the domestic side as it relates to Homeland Security, border security, air traffic control, TSA, and other agencies. The sequestration threats facing other Government agencies' contracts and workforce affects our member companies' ability to do business safely and effectively. In the near term some clarity from the Office of Management and Budget about how sequestration cuts would be implemented would be helpful in terms of avoiding some of these impacts.

Regardless of how the cuts are implemented, the consequences for the industry would be dire. The Defense Industrial Base Task Force commissioned by Secretary of Defense Panetta has reported that sequestration level cuts would result in the closure of production lines, a layoff of skilled workers, severe curtailment of research and development investments, and a reduced ability to respond to the emergent needs of the U.S. military.

However, today I am here as the President of Pratt & Whitney to offer my view on how sequestration will affect us directly and share with you how the effects Secretary Panetta mentioned are becoming a reality for us.

At Pratt & Whitney we build jet engines for both the commercial and military marketplace. As you know, our future military base market consists primarily of the F135 engine for the F–35 Joint Strike Fighter. While we are also proud of our engine chosen to power the next generation KC–46 aerial refueling tanker for the U.S. Air Force, these engines will not really add to our production business until 2016 or later. With the end of the production run of the F–22 engine this year and potentially the end of the production run for our engine for the C–17 next year, the F135 engine is our future for our military business.

Already the decline in defense spending is negatively affecting the F–35 production ramp and subsequently affecting our engine production. As you know, $487 billion in defense budget cuts already announced has pushed out 179 F–35 Joint Strike Fighter aircraft between 2012 and 2020. Original projections just a few years ago had us building over a hundred F135 engines per year. This year we will build just over 50, so about half of that number. Next year our F135 production will actually decrease, and if sequestration were to take effect, that number would decline dramatically. It is not just new engine deliveries that are impacted at Pratt. Spare parts are the key to keeping our manufacturing base healthy and sustainable, but as a result of the announced $487 billion defense budget cuts, flight hours have already been cut back, and sequestration would result in still further reductions. This undercuts demand for our spare parts and overhaul work. For my company this situation poses both a workforce and a supply base problem. As the F–22 program winds down, I am currently transitioning many of these workers to the F135 production, but this is extremely difficult given the near-term production decline I described earlier. With sequestration it will be even more difficult to retain those highly skilled employees, and quite simply my workforce is aging, specialized, and highly compensated. If and when we do ramp back up production, the learning curve for new employees is steep and will affect production quality and training, all of which adds time and costs.

Pratt & Whitney is somewhat unique because from a production standpoint a jet engine is a jet engine, whether it goes in a military aircraft or a commercial aircraft. This allows us to absorb some of the disruptions better than small companies in the supply base. For a short time I may be able to move employees between military and commercial programs, assuming I have an increase in demand for the commercial area. I can, if forced to, take some risks if there is to be a reward at the end of the day, but this is like putting a proverbial Band-Aid on a bullet wound.

In terms of our supply base they, too, are currently struggling with volume. Many of them are small businesses, making specialized parts for military engines that simply cannot survive another production decline or disruption. We continue to hear from our suppliers that if further cuts take place, we would be—they would be forced to lay off employees, curtail investment, and pursue other businesses.

One large supplier has told us, quite frankly, they don't believe the DOD [Department of Defense] will ever produce the number of engines in the Joint Strike Fighter program. This uncertainty makes suppliers less willing to enter long-term agreements and drives our costs up today.

If sequestration were to go in effect, no amount of juggling is going to preserve my workforce or help me maintain our supply base. A step down in the current production ramp for the F–35 means some people will lose their jobs. It also means reduced volume for suppliers, and that means costs go up. More importantly, it puts a good program in a very tenuous position, a program that we cannot afford to lose.

To reiterate, Mr. Chairman, we at Pratt & Whitney are better able than smaller companies to deal with short-term implications of sequestration, but make no mistake, it is dangerous to the warfighter, for us as a business, for our supply chain companies, and for us as a Nation.

Again, I appreciate your perseverance on this important topic and for your allowing me to be here today. Thank you, sir.

[The prepared statement of Mr. Hess can be found in the Appendix on page 85.]

The CHAIRMAN. Thank you.
Ms. Williams.

STATEMENT OF DELLA WILLIAMS, PRESIDENT AND CHIEF EXECUTIVE OFFICER, WILLIAMS–PYRO

Ms. WILLIAMS. Thank you. Mr. Chairman, Ranking Member Smith, and Members of the committee, thank you for the opportunity to testify on sequestration implementation options and the effects on national defense industry perspectives. My name is Della Williams, and I am the President and CEO of Williams–Pyro in Fort Worth, Texas.

Williams–Pyro is a woman-owned small business that designs and manufactures innovative products, including custom cables, connectors, adapters, automated test equipment, and intelligent power management systems. Our products have improved the safety of flight line maintainers, reduced aircraft downtime, boosted the buying power of the defense and procurement dollar. We currently have 89 employees who continue to amaze me every day. I have been here since day one.

As a manufacturer and part of the defense industry chain, defense supply chain, I very much appreciate your focus on defense industry and the impact of the impending cuts in defense spending set to begin on January 1, 2013. While I wish I were here under better circumstances, and the impending threat of these wholesale budget cuts is of deep concern to me, my goal today is to put a face and a name to what is rather cavalierly discussed in the press as sequestration.

Most people would associate defense cuts with big Tier I defense contractors which are represented by several of my colleagues here today. Supporting every one of these large integrators on dozens of programs are thousands of Tier II and Tier III suppliers, most small and medium-sized businesses who design and manufacture what seems like small parts. Moreover, the defense supply chain companies collectively employ millions of hard-working people who each support spouses and children and communities.

So these cuts will not just impact a few companies, these cuts will flow down the supply chain and through the broader economy. They will impact companies like mine and threaten the jobs of thousands of skilled workers who work at them. In fact, a report released last month by the National Association of Manufacturers concludes that by 2014 the cuts in defense spending enacted last year combined with the cuts set for January 1, 2013, will result in the loss of more than one million jobs, increasing the unemployment rate by almost 1 percent. Just in Texas alone this means a loss of more than 100,000 jobs. If small business, and I would submit even further manufacturing, is an engine of economic growth, why are we making decisions that will inevitably stall that engine? The budgetary issues the Federal Government is facing are the same ones that I, as a small manufacturer and a taxpayer, deal with every day in my own business.

Analysts say the defense industry is faced with several choices, either exit the market, double down on defense by buying your competitors or weather the storm. At Williams–Pyro, however, we have chosen to invest in product development. These are major investments for a small business, but we are committed to developing products that will meet the military's operational and procurement requirements. I believe that this dedication to providing innovative products for the defense industry helps to illustrate the potential impact sequestration will have on my business and many others.

Sequestration, as is being discussed, will create a mass exodus of talent and skills to other industries. Williams–Pyro presently has almost 90 employees, including machinists, assemblers, and R&D engineers experienced in mechanical, electrical, software, firmware, hardware, and manufacturing. These jobs are in jeopardy.

What is being billed as a stopgap budget fix will have lasting effects on our defense capabilities for years to come. The switch will just not get flipped back on to reverse that trend. Moreover, the deep personnel and program cuts will threaten our national security. Indeed, the United States could lose our technological and strategic advantage and never get it back.

In conclusion, I urge Members of Congress to go back and sharpen your pencils. Sequestration is cosmetic surgery with a chainsaw. Working together we can solve this, but we need to do it smartly and strategically while keeping the economy moving and defending this great land.

Thank you again for inviting me to appear before you to talk about this very important issue. I would be pleased to answer any questions you might have. Thank you.

[The prepared statement of Ms. Williams can be found in the Appendix on page 90.]

The CHAIRMAN. Thank you very much. I think we on this committee probably all understand more than perhaps the rest of Congress how serious these impacts will be on our military and on our industrial base, but you have laid out even further these problems. I have a series of questions that probably could be answered very briefly. I would encourage you to do that so that we get these things on the record, which will help us as we go forward.

Based on your testimony, it appears to me that you believe if sequestration goes into effect January 2nd there will be job losses. Can you each confirm at this time that layoffs are reasonably foreseeable?

Mr. STEVENS. Yes, sir.

Mr. O'KEEFE. Yes, sir.

Mr. HESS. Yes, sir.

Ms. WILLIAMS. Yes, sir.

The CHAIRMAN. Thank you very much.

Do you believe that you are obligated by either the spirit of the letter of the Worker Adjustment and Retraining Notification, known as the WARN Act, to give conditional notices to your employees that may be laid off as a result of sequestration in advance of making a final determination regarding which specific employees will be let go?

Mr. STEVENS. Sir, given the uncertainty in this environment today, yes, we do.

The CHAIRMAN. May I—I would like that answer from each of you, but you have a specific history regarding the presidential helicopter that is very important. Could you just expand on that a little bit as to your history there?

Mr. STEVENS. I can, sir. With respect to the termination of the VH–71 helicopter where we knew there would be layoffs at a particular site in Owego, New York, but we didn't know which employees would be laid off, we did not issue WARN notices at the time of that termination, opting rather to do internal planning to see if we could replace the worker in another assignment either in that location or another location, look at dimensions of the business we might have to provide some flexibility here. That process took about 45 days. In the subsequent evaluation of the termination claim that is typical in a termination for convenience environment, we have an opinion from the Defense Contract Audit Agency that said we should have acted more timely and that the costs associated with that 45 days may well not be allowable and viewed, I believe, in their draft opinion that our actions were unreasonable, that we waited an unreasonably long period of time.

So experiences like that inform us in an odd way of the compelling requirement to take timely action and not allow the ambiguity of the situation to accrue against the interests of the company even though in that case our preference was in our judgment to act prudently and see if we could move the employees around.

The CHAIRMAN. And you are still in litigation on that issue, as I understand it?

Mr. STEVENS. It is a negotiation over the termination, yes, sir. It has not been concluded yet.

The CHAIRMAN. Thank you. Mr. O'Keefe.

Mr. O'KEEFE. Yes, sir, no, I concur entirely with your question that yes, indeed, we will be as a matter of the spirit of the law compelled to do something in that regard, yes.

The CHAIRMAN. Mr. Hess.

Mr. HESS. We would certainly abide by the requirements of the WARN Act. Now we have certain advantages in our business that Mr. Stevens doesn't have, Mr. Stevens' business, roughly 80 percent of it is defense. At Pratt & Whitney roughly 25 percent of our business is defense, so depending on what is happening in the other elements of the business, the commercial environment, we might have the potential, the opportunity to redeploy people, but it is far from certain, and certainly when you are looking at budget cuts of the order of magnitude that sequestration would involve, potentially another 10 to 14 percent on top of the 10-percent budget reduction that is already being implemented today, certainly there would be scenarios where we would be looking at proportional head count reductions.

The CHAIRMAN. Thank you. Ms. Williams.

Ms. WILLIAMS. I don't believe we are covered under the WARN Act because we are less than 100 employees. However, if that changes, absolutely. And even if it doesn't change, if we don't get some contracts soon, and I don't see how we will be able to get, keep our employees, and this sequestration is going to cut drastically in our contracts.

The CHAIRMAN. Thank you.

Barring additional guidance from the Office of Management and Budget and the Department of Defense on the application of sequestration, do you believe that conditional notices will have to be issued this fall prior to January 2 to comply with the WARN Act? How many employees do you estimate will receive those conditional notices? And if you will not have to issue conditional notices this fall, what extenuating factors affect your decision?

Mr. STEVENS. Yes, sir. I think that we will be compelled to issue notices. There is an ongoing discussion about how many WARN notices will need to be issued and exactly when. There is so much uncertainty in this environment. I think that will be a capstone comment that I know the committee wrestles with all the time in your deliberations. But we do know several things. We do know sequestration is the law. We know that law takes effect January 2. We believe any reasonable modeling around that law will require significant reductions in force with double-digit reductions in the budget.

In the past, when we have had budget reductions, we look internally at a strategic assessment of our company because if we just cut the cloth uniformly, it would be terribly uneconomical and inefficient, and those costs would flow back in the future. That restructuring likely means we will have plant closings. Plant closings and significant reductions in force will trigger the WARN Act.

The question then becomes, when? Our best judgment, as we have tried to put pencil to paper with all this uncertainty about planning, is that agencies will actually move closer to January 2 because the act requires a $55 billion reduction in fiscal 2013. But the act takes effect after the first quarter. So the $55 billion has to be reduced over 9 months, not a year. Every day it is delayed after January 2 makes the magnitude of the reduction to accumulate $55 billion in the year more. If 3 more months go by, the equivalent of $110 billion would have to be taken out of the agency, which would be more and more disruptive.

So I think as people come to terms with their responsibilities in that sequestration is the law and we must prepare for it, there will be an impetus to move closer to January 2. We need to be prepared to enable agencies to make those determinations. Because of that preparedness, we will set back 60 days or, in the case of New York, 90 days from that. The question is, which employees would be terminated? We don't really know. We would have to broaden the notification under WARN appropriately. We are very hungry for more guidance, very hungry for more information so we can narrow this and behave responsibly.

The CHAIRMAN. And yet when we held one of our hearings in September, and we asked the Assistant Secretary, Dr. Carter, what they were doing to prepare, his comment was rather flippant, "We don't have to do anything to prepare. We just take the budget out, take the percentage off of every line item. So it takes no planning." I just think that is totally irresponsible.

Mr. O'Keefe.

Mr. O'KEEFE. Again, I think as much as you have heard from others here, absent any specific guidance on how this should be applied, we will be compelled as a matter of compliance with the spirit of the law following through on the WARN Act provisions.

Now we have already begun that process. Again, we have notified many Members of Congress that represent constituencies and districts in which we operate in as well as the Governors of those States that this provision will have applicability. We are assessing at what point we have to make that determination. And as much as you just heard from Bob Stevens, we are going to have to make that choice. As we see the time unfold here, absent any guidance, that is going to have to be sooner or later. And again, the determination from the Office of Management and Budget and DOD would prescribe that.

But much as what you heard as well from Dave Hess, 70 percent of what we do is commercial related. We are going to have options and alternatives. But there are going to be very specific contracts and programs that will be affected that are Federal contracts across the board. And once we get those more specifically targeted, that will be the focus on where the WARN Act applications and notifications will have to occur.

The CHAIRMAN. Thank you.

Mr. Hess.

Mr. HESS. We will certainly abide by the regulations in the WARN Act. But as you have heard from my colleagues, given the amount of uncertainty in terms of how these budget reductions play out, also given the opportunity maybe to redeploy people to other parts of the business, it is not clear to us today that we would trip the thresholds involving implementation of the WARN Act. With respect to your question about conditional notification, we are still considering that possibility.

The CHAIRMAN. Thank you.

I understand you are not affected by this. But please explain whether any of the exemptions to the 60-day notice WARN Act requirements are applicable in this situation. For example, could your company claim that layoffs resulting from sequestration were sudden, dramatic, and unexpected?

Mr. STEVENS. We don't believe so.

Mr. O'KEEFE. No. They are well forecasted and anticipated. We knew months in advance and you could see it coming.

Mr. HESS. I would agree with my colleagues. The law on the books today says that sequestration will occur on January 2, not conditional or contingent on anything; that it is the law of the land, and we are obligated to plan on it.

The CHAIRMAN. Even though some in the Administration say, it is not going to happen, don't worry about it, you feel you are bound by the law?

Mr. HESS. We have a fiduciary responsibility to our boards, to our shareholders and our employees to plan based on the laws that are on the books today.

The CHAIRMAN. And my final question, aside from issuing notices to your current employees, how has the possibility of sequestration impacted your current hiring practices or that of your industry partners?

Mr. STEVENS. Well, sir, we have slowed down on I think the very simple and logical premise that if we are going to engage in significant reductions in the workforce in January, it is imprudent to bring people on for 6 months.

What struck me as more interesting and maybe more telling about the future, we recruit heavily on college campuses. We do get a million résumés a year from very talented young people. And I know you interact and the Members of the committee interact with these young people all the time. And it really gives you optimism about the future of America when you have the ability to see the talent, the energy, and the vision possessed by these young graduates. For the very first time in my tenure as CEO, they have started to ask whether they want to come into the industry or specifically with our company, even though they love the technology and they love the mission. Because they question, if I join you now, will I have a job next year? These are very smart kids. We want them because they are smart young people. And they are smart enough to realize that this uncertainty may cause them to look at other options for their career.

We want the best and brightest talent in the defense industry so we can continue to innovate the products and services that our women and men in the Armed Forces rely on to keep themselves safe.

The CHAIRMAN. Mr. O'Keefe.

Mr. O'KEEFE. Mr. Chairman, I would say that we have slowed down hiring as a consequence indirectly of sequestration. What is occurring now is requests for proposals, a range of different contractual activities. We are all shifting to the right in the Federal activity. It has all been delayed. So as a consequence, that really refocuses your attention. We are not going to hire folks in anticipation of what we think is going to be market opportunities coming down the road that we think we can compete for successfully. We have slowed that down significantly.

The CHAIRMAN. So even though you have been told that it is probably not going to happen, don't worry about it, the department is already slowing down in anticipation of it happening?

Mr. O'KEEFE. Absolutely. There is no question.

The CHAIRMAN. Thank you.

Mr. Hess.

Mr. HESS. Clearly the threat of sequestration is tempering our decisions today with respect to hiring and capital investments. And quite honestly, we have seen companies in the past that have made decisions to invest and are suffering the consequences today. For example, in the Joint Strike Fighter program, I mentioned the fact that the volumes that we are looking at today—production volumes—are about half of what they were forecasted to be. Companies that had invested based on the prospects of a much higher volume are now struggling. In fact, some of them—we have examples, small businesses, like Williams, that have gone chapter 11 or chapter 7 because they can't support the cash flow. They made decisions based on forecasted growth. They haven't occurred. Sequestration would only exacerbate that.

The CHAIRMAN. Ms. Williams.

Ms. WILLIAMS. I feel that I owe an obligation to my employees to explain this as well as I can to them. I mean, they get very nervous about this word "sequestration." They were like, what does this mean? But I owe it to them so that they know what might be happening and whether they should go look for another job. And believe me, I don't want to lose those people because they are longtime employees. But this consumes about 50 percent of our business, a little over 50 percent. And I think my hands are going to be tied if all of this happens.

The CHAIRMAN. Thank you very much.

Mr. Smith.

Mr. SMITH. Thank you. First of all, just out of curiosity, have any of you been told that it is not going to happen, don't worry about it?

Mr. STEVENS. In my case, sir, there is lots of discussion when we engage in a dialogue about what we should prepare for. And there are suggestions that a remedy will be developed.

Mr. SMITH. Sure.

Mr. STEVENS. I would say and I think your comments earlier certainly reflected this, sir, that there are lots of opinions, and there are a lot of points of view. But we hold ourselves to a set of standards that I know you and the committee expect business leaders to hold themselves to.

Mr. SMITH. I understand that. I have further questions.

The chair has said a couple of times the Administration's position is, it is not going to happen, don't worry about it. I don't think that is accurate.

Mr. STEVENS. We are preparing for the implementation of sequestration.

Mr. SMITH. Right. The Administration is aware of the fact that this is the law. And until we change it, it is potential. They don't want it to happen. Nobody on this committee or in this room wants it to happen. The problem isn't so much a matter of preparation. The problem is that the law is, regrettably, on the books and coming. And we have to find a way to change it.

And toward that end—and I do have a question at the end of this. But I think what we have learned here is that Government spending kind of matters. You can't just blindly cut it and assume that there is no problem, which is sort of what led us to this horrible deal and the Budget Control Act last time was, well, you don't raise the debt ceiling. It is no big deal. That will get us to a balanced budget. That will work.

Government spending matters. So does private sector, so does keeping taxes low, I will grant you all of that. But we can't simply blindly say, whatever you cut from Government, it will be fine because they are not really doing anything that important anyway. And it is that attitude that led us to where we are sitting here, the notion that you didn't have to raise the debt ceiling and then if you put in place mandatory cuts, it really isn't that big a deal. So I hope that lesson will be learned.

And as we go forward, looking at our budget situation with a $1.3 trillion deficit, as I mentioned, even if, let's say, tomorrow we just say, never mind, we are not going to do sequestration, I am curious, as all of you look at the next 10 years—the defense budget doubled since 2002. It was a boom time for defense contractors. No matter what happens—sequestration or no sequestration—we have got a pretty tight fiscal situation for the next 10 years. How are you looking at that? How are you anticipating the impact of simply the reality of, you know, revenue being in one place and spending being in another and the need to reconcile that and the reality that the defense budget right now is 20 percent of our budget? How are you planning for that over the course of the next 10 years?

Mr. STEVENS. Well, the way we are focusing our business now is to accommodate the reductions already in the Budget Control Act of $487 billion that Defense Secretary Panetta has spoken about, that is embedded in our national security strategy. A number of our programs have been capped, terminated, canceled. We have slowed down those programs. Our workforce is 18 percent smaller today than it was 3 years ago. We are hitting the brakes there. We have taken out 1.5 million square feet of facilities. We will take out another 2.9 million square feet before the end of 2014. We have cut our capital investments. We have cut our research and development, sizing the cloth of the business to meet the market reality.

We are also looking to work with the Administration and the leadership in the Pentagon at international work because our Nation has asked others to step up as security cooperation partners. As good security cooperation partners, if we have interoperable systems, we are able to do more effectively well together. They burden-share some of the expense. And any incremental work flowing into our businesses stabilizes our businesses, stabilizes the workforce. And it lowers the cost of every bit of equipment that the U.S. buys for U.S. purposes. So that is how we focus the strategy and the business.

Mr. SMITH. But if I could—Mr. O'Keefe, you can take a stab at this one. How worried are you that, looking at the budget realities, that that reduction number is going to wind up above the $487 billion that is currently projected? And also, if I could piggyback on that question, there are a number of studies coming out now that the Pentagon's plans to, quote, "reduce debt spending over the course of the next 10 years" don't really quite add up. What they say gets them savings doesn't. The programs they have started actually are going to wind up costing more than that. So do you think it could be more than what has currently been talked about?

Mr. STEVENS. I think it is possible. We have watched the reductions associated with the Budget Control Act. If there are reductions, we will do the best that we can to accommodate our business. We have done it historically. And we will continue to do our very level best to size the business so that we can deliver against these commitments.

I think the greater concern we have is that the resources that are available for national security align with a strategy for national security as an objective set of outcomes.

Thank you, sir.

Mr. SMITH. Does anybody else want to comment on any of those?

Mr. O'KEEFE. I will just pick up on that last point. And that has yet to be mentioned. This is the first time we have seen in the course of better than 40 years in which every change and reduction in national security spending in that span of time has been precipitated by a change in strategy to accommodate or to recognize a different threat level. This hasn't happened in this case. This is purely exclusively driven by the financial realities of——

Mr. SMITH. If I may—exclusively—I mean, we just took 175,000 troops out of Iraq. We are drawing down in Afghanistan. There are national security changes that have precipitated some of it. I think it is certainly the budget part of it. But I wouldn't say it is exclusive. There have been, just like in those previous cases, changes in our national security needs, at least based on Iraq and Afghanistan.

Mr. O'KEEFE. To this point, certainly there has been accommodation to that. But I think you would also suggest, as you have in your opening statements as well, that much of what we are seeing going forward here is going to be a consequence of the fiscal uncertainty and less about the threat.

So it is very difficult, it is near impossible, from where we sit, to anticipate exactly what kind of market changes that will involve. And I think very realistically, there is a pairing back of expectations of what the market will look like in the future and what demand will look like. And what we are already seeing is a gravitation toward—from second- and third-tier suppliers towards different activities that are far more commercially oriented.

Mr. SMITH. And the last thing, I imagine it would help if the Government had more revenue so it wasn't forced into as bad of a budget situation. Would any of you disagree with that assessment?

Mr. O'KEEFE. I think the choice of exactly what spending and revenue balance is, is more dominantly of your portfolio. So, as a consequence, I would defer to you on the answer to that one, sir.

Mr. SMITH. That is true.

I yield back. Thank you.

The CHAIRMAN. Thank you.

Mr. Bartlett.

Mr. BARTLETT. Thank you.

Twenty years ago, I sat in the most junior seat on this committee and was frequently frustrated particularly in important hearings like this that time is going to run out before I came up in the queue.

Sensitive to that frustration, I would like to yield my time to the most junior Member of our committee here at gavel fall today, and that is Mr. West.

Mr. WEST. Thank you, Mr. Bartlett.

And thank you, Mr. Chairman and Mr. Ranking Member.

I would like to try to get a little bit more specific. I would like to know from each of you what are your four major weapons systems programs or developments that you have the most concern about being affected by sequestration and, of course, the corresponding workforce concerns as well. So if you could give us that idea of kind of your top four.

Mr. STEVENS. I want to be responsive to your question, sir. When you align the top four with sequestration, one of the challenges we have is, our understanding of sequestration is across the board.

Mr. WEST. Yes. But irregardless of sequestration, what are the top four that you think would cause you concerns if they were affected by sequestration?

Mr. STEVENS. Undoubtedly, the Joint Strike Fighter program. Undoubtedly programs in missile defense. And there is a portfolio associated with missile defense. Without question, programs like the Littoral Combat Ship, which are accelerating capabilities. And then we have an array of what I would describe as classified or intelligence-oriented programs, all of which is, as I understand the environment, would not be immune so the support service we provide to the intelligence community would be adversely impacted.

Mr. WEST. How about workforce effects from those four programs? Just an estimation.

Mr. STEVENS. Our best estimate, which I will admit is sufficiently crude, that I am a little embarrassed to offer it, across the board, 10,000 people. But we have done it on the back of the envelope where we have made up most of the assumptions of 120,000 people, in the neighborhood of 10,000. That neighborhood could be more or less, depending upon, will there be accounts that are excluded? As the chairman and ranking member said, there is still yet information to be determined. We will shape our outcome there, I think 10,000 across the board is about the best answer I can offer.

Mr. WEST. Thank you.

Mr. O'KEEFE. Well, sir, the three that I would highlight in particular are, first and foremost, the UH–72 Lakota helicopter, the program that is frequently recognized by every audit service and the Defense Department overall as on time, on budget for over 225 aircraft thus far without any exception to that whatsoever. That could be compromised. As the changes in production rates alter, that will almost certainly motivate cost increases per unit. And that would be the first time in the entire experience of that program that we would see a cost increase or a failure on delivery. I really would hate to see that record of absolute achievement compromised or blemished even for a moment.

The second is one which, as Bob Stevens described, is the Littoral Combat Ship. We have a very strong interest in a lot of the systems that are engaged there, for radar and a variety of other activities, all of which will turn on whether or not the number of vessels commissioned for production and contracted will be engaged. That is going to be an uncertainty for a period of time which, therefore, takes whole units and defers them until such time as there is certainty.

And the third would be for the United States Coast Guard, often recognized as a very strong support element of the defense establishment and national security overall. We produce most of their helicopters and a good number of their cargo aircraft, all of which by contract at this point have a prospect of being deferred, given the very small maneuverability that particular agency has towards capital accounts. We don't know what that would be.

So, all in sum, trying to estimate the numbers of people would be nearly impossible to figure out what would be involved here, until we see what those exemptions are as well as which programs in specific may ultimately have to deal with that, if they are all going to be applied across the board evenly.

Mr. HESS. For Pratt & Whitney, we are already seeing significant engine delivery reductions in our legacy engine programs. Certainly our sole source engine on the F–22, now that that program has been terminated, engine deliveries for that program will cease this year. We are finishing up some spare engine deliveries.

Similarly, for the C–17 and the F–16 where we deliver military engines both of those program delivery rates are declining as well as they shift largely to international sales. We are counting on the ramp-up and the increase in the Joint Strike Fighter program that Bob talked about with our sole source engine there to offset those declines and really kind of stabilize our operation and enable us to maintain our industrial base. But again, as we see that program continue to be delayed, the last reductions that support the $487 billion in reductions took 179 airplanes out of the schedule in the next 5 years. So that is 179 engines for us. So that has impacted our delivery rates. And we were also counting on the ramp-up in the Air Force tanker program. But deliveries there don't start until 2016 and beyond. So really, Joint Strike Fighter and to a lesser degree the tanker would be the important programs for us.

Ms. WILLIAMS. The weapons systems test equipment that we manufacture for all aircraft that we do currently for F–16, F–15, F–18, the A–10 program and the F–35 and some on the F–22. But this concerns me because we go to the Air Force bases, and recently we saw 1969 technology still being used.

Do you remember 1969? Rabbit ears and transistors and diodes.

Mr. WEST. I was only 8 years old.

The CHAIRMAN. The gentleman's time has expired.

Mr. WEST. Thank you, Mr. Chairman.

My time has expired.

The CHAIRMAN. Thank you. Mr. Andrews.

Mr. ANDREWS. Thank you, Mr. Chairman.

Thank you, ladies and gentlemen for your testimony this morning.

I agree with you completely that I favor repeal of the sequester as soon as we can possibly do it for many of the reasons you very well articulated here this morning.

But I also acknowledge the responsibility to understand the comments that Admiral Mullen gave us when he was chair of the Joint Chiefs of Staff, in which he recognized that a country that borrows 40 percent of its operating funds can no longer be a strong country. Inevitably, the national debt is a national security issue.

The way we got into this mess is that for five decades, people on this side of the aisle and people on that side of the aisle have gone through the following exercise: Whenever anybody brought up a reduction in spending, we had hearings about how bad that was and who it would hurt. And whenever anyone brought up an increase in revenues, we had hearings about how bad that was and who it would hurt.

So we made a series of decisions that you would never make in your fiduciary responsibility. We made a series of stovepipe decisions about those spending programs and those revenue increases in isolation. That is how you create a $17 trillion debt.

How you get out of it is to do things that people do not like. I think most of you would agree that since nearly half of our budget—I guess more than half of our budget soon is Social Security, Medicare, and Medicaid, that we have to do something about restraining the growth of those programs in an equitable way. I agree. That is why I am one of the fewer than three dozen people who voted for the Simpson-Bowles budget proposal Mr. Cooper put on the House floor in March. I will stipulate that most of you I think would agree with that.

Let me ask you another question. It has become an article of almost religious faith around here for some Members that any revenue increase at any time on anyone should be taken off the table. Who here agrees with that proposition?

Mr. HESS. Let me speak. I don't think you will hear any of us here today arguing against the need for fiscal responsibility. I mean, we all have our jobs to do running the companies that we run. But I would say—and I can look honestly at my colleagues here and know that we are first and foremost Americans. And as Bob talked about, we are all making decisions today to deal with the 10-percent budget reduction that has already been enacted and being planned on and implemented now. We are making decisions in terms of head count reductions. We are right-sizing our companies. We are closing facilities, consolidating our footprint, making the tough decisions, and taking the tough actions to deal with the need for fiscal responsibility. We, I think, are supportive of that and understand that.

Mr. ANDREWS. But, Mr. Hess, if I may, the specific question I asked was, who here would advise Congress to rule out under all circumstances any revenue increase on anyone at any time? Would any of you make that recommendation to us?

Mr. HESS. I would say that I don't think any of us are sitting here today presuming that we have the wisdom to recommend a solution here.

Mr. ANDREWS. No. I don't think it is a matter of wisdom. I think you have a lot of wisdom. Do you have an opinion though? You are an American citizen. You are a leader of a major institution. Do you or do you not think it is wise for Congress to rule out all revenues on all people at all times forever? Do you think that is a wise course?

Mr. HESS. I think everything has got to be on the table at this point. This is a personal opinion. I am not speaking for the employees for United Technologies or for UTC.

Mr. ANDREWS. I think you are right, Mr. Hess, and I agree with you.

How about the rest of you? What do you think of that.

Mr. STEVENS. I know when we face challenges in our business—and I don't intend to imply that the challenges that we face come close to the magnitude of the challenges you face on this committee or Congress faces at large—it really makes ours look pale—we tried to put into the recipe every possible ingredient that might lend itself to the formation not just of a solution but, in a perfect world, a flexible array of solutions.

Mr. ANDREWS. A balanced solution.

Mr. STEVENS. Comprehensive, integrated, thorough that allows us the flexibility to run the business.

Philosophically, I think you will see that in our actions. I think we are held accountable for that kind of behavior from our board and our shareholders. I think our employees expect it.

Mr. ANDREWS. I appreciate that. Since my time is running, I will just give you this context: Social Security was truly imperiled in the early 1980s. And a President named Ronald Reagan stepped forward and, on two occasions, agreed to raise more revenue for it. It is the reason Social Security still exists today. And I think that our friends on the other side would be wise to follow President Reagan's example in this time of national emergency.

I yield back.

The CHAIRMAN. Oh, that we had President Reagan.

Mr. Forbes.

Mr. FORBES. Thank you, Mr. Chairman.

Gentlemen and lady, thank you for being here.

Mr. Chairman, I want to first thank you, not just for holding this hearing but for being across the country, alerting the public to the dangers of sequestration long before anybody else was doing it and also for actually putting a solution on the table. We are not going to change this by press conferences. Unfortunately, the House, as you mentioned, has passed a solution. It may not be the perfect one. But at least they have passed a solution. The second thing I have to do is take issue with something the ranking member said at the beginning because I just believe it to be blatantly inaccurate.

We did not get here because a majority of Members of the House of Representatives or a majority of individuals across the country realized the insanity of continuing to allow an irresponsible and uncontrolled massive increase and the smothering debt our Nation is mounting. We got here very easily—a picture is worth a thousand words.

If you look, this Administration decided that they would spend $825 billion on a stimulus package, $347 billion of interest. And if you look at these charts, if they look identical, it is identical because what actually happened was they decided to spend in 1 year on a stimulus package almost the entire amount they are now taking out of defense for 10 years. And even though this package has no measurable significant increase in jobs, we know this is going to cost us between 1.5 million and 2 million jobs.

So I think it is important, we want to know how we got here. But this committee is not the Ways and Means Committee. We are not here to talk about tax increases and anything else. We are not even a "jobs creation" committee. What we are here for is looking at the national defense of this country. And that is what you guys do, and you do it very, very well.

My big concern is, as I go back to the 1990s and look at all the cuts that are taking place, and I am concerned about the $487 billion we have already taken, much less the $500 billion that is coming. It is my understanding that we started that decade with 50 major defense firms, and we ended up with six prime contractors. We started that decade and at the end of it, our major surface combatant shipbuilders and our fixed-wing aircraft developers fell from eight to three. Our tactical missile producers fell from 13 to 3. And the number of track to combat vehicle developers fell from three to two. Today there are just two companies, Boeing and Lockheed Martin, that build U.S. fighter aircraft. My question for you is, What impact do you think sequestration may have that might be similar to the 1990s in terms of weeding out our industrial base and the impact it may have on that over a long-term period of time?

Mr. STEVENS. Yes, sir. Well, having lived through the 1990s, I think the consolidation you described was an effort to size supply to the likely demand that has to equilibrate somehow. In a consolidated environment, that we are in today, another round of significant reductions on the demand side of this will adversely affect supply. The question will be, should we try another round of consolidation in the industrial base? Right now that is viewed as unfavorable and undesirable so as not to limit competition. But there has to be a healthy relationship between the demand for the products and services that we have and our ability to supply them. So the supply chain in some form or fashion will equilibrate over time. It will either be graceful and focused and have a good architecture or it won't be. But it will size and shape itself differently to meet the level of demand that exists.

Mr. O'KEEFE. I think that the shakeout in the market we are seeing right now in second- and third-tier suppliers is already a manifestation of that point. We are seeing either companies consolidate, be bought by larger primes, as I have seen in the last few years, or they have just simply exited the public market and have consolidated much more toward the vagaries of some of the commercial trends that occur but at the same time much more reliable than what we are seeing as forecast for the next decade in the public spending market. So I think that is already occurring. It is happening right now.

Mr. HESS. I guess I would have to agree with you. I think we are getting to a very critical point with respect to the industrial base. And quite honestly, it is not just the big companies that you reference, people like Lockheed and Boeing. But honestly, where we see a greater concern is with the smaller companies, such as represented by Ms. Williams today, where we are down to one company that maybe has a unique skill set or technology or capability that is at the point where they are considering exiting the business. It is not worth their trouble. They will go pursue commercial or other markets. And that is quite honestly where we are really starting to see some concern.

Ms. WILLIAMS. I would agree with the gentleman here, that this is going to affect us greatly.

Mr. FORBES. Mr. Chairman, thank you.

I yield back.

The CHAIRMAN. Thank you very much.

Mrs. Davis.

Mrs. DAVIS. Thank you, Mr. Chairman. And thank you all for being here.

I just want to say, as someone representing San Diego that I want to thank you for your work on behalf of your employees and certainly their families. And I really relate to what you are saying about people being affected.

But as we know, it is not just in the defense industry that we see tremendous effect on families today, uncertainty. And I know that you have to be concerned about that. How young people are educated today is critically important to our national security. So that is a concern as well.

I want to just identify myself with some of the comments and the questions of my colleague Mr. Andrews because I think we do want to see this in a balanced way. And I call upon you—and I hope that you are considering that you obviously need to be very strong advocates, which you are, for the industry that you represent. But I would hope that you would extend that, as we work into these very, very difficult issues that we are facing. And I wonder if I could count on you to do that, to include those kinds of comments as well and the need that we have to balance out and put everything on the table, as you suggested. I hope that we can count on you to do that. Thank you.

What I wanted to ask you about is, as you think about and you are asking, let's be strategic about this. I don't support sequestration. As we said, nobody here does in terms of those kind of across-the-board cuts. But the reality is you have had to deal with cuts and different ways of really analyzing the work that you do in the Budget Control Act and some of that extends to additional changes that may be made in the industry.

Are you in a position today to suggest to us, are there some reforms in contracting that you think are critically important to make? We know that multiyear contracts—perhaps that can spread out some of the sacrifices, if you will that, that might be made in terms of looking at the strategy that is put in place, the targeted kinds of cuts. And I know that, Ms. Williams, you spoke about that as well.

What is it that we should and could be looking at that is—I really don't want to say a next generation of reform but something that perhaps you talk about but we don't necessarily acknowledge as part of this whole discussion?

Mr. STEVENS. Thank you. I will try first, ma'am. And I will say this probably won't sound inventive or innovative in any way because it is interesting about acquisition reform. The fundamentals that seem to keep resurfacing are the same observations we have across the industry. I will tell you first is stability. Whether that stability is the funding environment or the requirements environment or industry's ability to hire, train, get the right people in the right place at the right time, do those fundamentals, those fundamentals drive this process substantially.

Secondly, if we could look at shortening the cycle times. Cycle times in the industry are getting longer and longer and longer from the formation of a proposal, the early test phases; it is getting longer. And time is money. Anything we can do to streamline, simplify, and shorten that process, certainly would accrue to a portfolio of efficiency initiatives that I think would result in good savings.

Mr. O'KEEFE. I would simply offer that the recommendations of the Defense Business Board that reports to the Secretary of Defense, take them up on their suggestion: What they are proposing is simply suspend a regulatory environment in which every regulation then has to justify the reasons for its application, as is being sought to be applied. Otherwise, suspend it; just dispense with it.

That is an approach that will sort out this question—not our recommendations, one that the Business Board made to the Secretary of Defense in that regard. It is not an unreasonable proposition. It is a documented proposition that it costs for precisely the same articles at least 20 percent more to sell to the public than it does in any other commercial activity. So sorting out what causes that 20 percent is one matter that the Defense Business Board has recommended. I would take them up on their suggestion and do it.

Mrs. DAVIS. What do you think keeps us from doing that now?

Mr. O'KEEFE. I don't know. Resolve. Commitment. Suggestion, whatever. And it has just been put forward. But it is one that would be worthy I think of inquiring of the Defense Department and of the Office of Management and Budget. What is errant about the logic that this group has recommended forward to be implemented, which doesn't suspend regulations? It simply says, justify in every term why it needs to be there or else it is dismissed. It is a fairly reasonable proposition, one we would love to contribute in on every effort because of the additional cost of doing business.

Mrs. DAVIS. Thank you, Mr. Chairman.

The CHAIRMAN. The gentlelady's time has expired.

Mr. Wilson.

Mr. WILSON. Thank you, Mr. Chairman. And thank you for your leadership. You have proposed legislation that would address sequestration. In fact, Chairman McKeon has led three times in the House. We voted to address sequestration. But sadly, the President has threatened a veto. The Senate has not taken up the legislation. But the more the American people learn about the consequence—I want to thank all of you for bringing this issue up——

Also, I am really grateful that Bloomberg Government has done a study of every State which indicates defense spending. A State near and dear to me—and this is available to the American people—is Virginia. My mother was born in Richmond. I am a very proud graduate of Washington Lee University of Lexington. And I have a son who is Active Duty Navy at Norfolk. So we cover the State. And it is very revealing, particularly in Northern Virginia, as you look at the consequence of defense spending, it is just not Northern Virginia. It is by community. And there are communities which have over $1 billion which could be affected by sequestration, which include McLean, Sterling, Arlington, Falls Church, Alexandria, Fort Belvoir, Quantico. Each one, over $1 billion. Northern Virginia would be such a State affected—or a district, communities affected. Jobs. Military families truly are put at risk. As we approach this—it has already been addressed—but there has been some confusion about the WARN Act. The notices of layoffs. 60 days, 90 days. State law. What is it? And with a minimum of 60 days, when would persons anticipate to receive the notice of layoff? If each of you could give your point of view.

Mr. STEVENS. I am certainly no attorney or WARN Act specialist. But I seem to surround myself with a lot of attorneys who claim to be WARN Act specialists, particularly as we look at sequestration. Our sense is, 60 days from January 2 with timely notification puts the notice, end of October/early November for 60-day notification States. New York is a 90-day notification State. I think we would set that back obviously 30 days in time. It would be the end of September/early October.

Mr. O'KEEFE. As I testified a little bit earlier, we have already begun to notify Members of Congress that represent districts in which we operate and do business as well as Governors of those respective States that we may be compelled to do this once we—in the absence of guidance from the Office of Management and Budget or the Defense Department. Now that will have to occur some time prior to that 60-day notification stage. And exactly when is going to be very much contract-dependent, depending on what advice or the guidance we receive from the Administration.

Mr. HESS. I think Mr. Stevens clearly defined the requirements of the WARN Act. And again, we are certainly prepared to comply with the law. Again, given the uncertainty and how sequestration will play out, it is not clear to us that UTC would trigger the WARN Act thresholds. But it certainly is a concern that we have.

Ms. WILLIAMS. As I said earlier, I don't think this applies to me because I am less than 100 people. But I still want to give my employees an update and bring them up to speed on this because they don't understand what is happening.

Mr. WILSON. And it is an extraordinary coincidence, each of you have identified a date prior to November 6, which is Election Day. So this is something the American people need to know.

Ms. Williams, has your company stopped or slowed down capital investment in an effort to conserve funds in anticipation of sequestration?

Ms. WILLIAMS. What we have done previously is—the way we got a lot of our business was that we would make prototypes. And that is how we developed all these years. But recently, as I was talking earlier, we went to an Air Force base, saw the 1969 technology. We personally invested lots of dollars in order to bring this up to current technology. We have done that. We are not through by any means. But we have done that. What concerns me is, will I be able to continue to finish that project? And if this happens, I will lose those engineers.

Mr. WILSON. Well, I just want you to know, I particularly appreciate it. I represent the communities of Fort Jackson, Fort Gordon. I currently represent Parris Island. I want the best for our troops, for their health and safety. We do have the best in the world, but it really is dependent on your efforts. And I want to thank you for your prototype efforts and however we can help.

Ms. WILLIAMS. Thank you, sir.

The CHAIRMAN. Thank you.

Mr. Courtney.

Mr. COURTNEY. Thank you, Mr. Chairman. Thank you for holding this hearing and the witnesses for your really important testimony here today.

I want to also note, Mr. O'Keefe, your comments regarding the sort of genealogy of sequestration, talking about the Gramm-Rudman Act I think is very helpful because, frankly, it is a concept which is now sort of lost in the midst of time a little bit. And I think it is important for people to remember that—again, it was a measure that was used at a time of structural deficit. And one of the sponsors of it, then-Congressman Gramm, was quoted at the time saying, it was never the objective of Gramm-Rudman to trigger sequester. The objective of Gramm-Rudman was to have the threat of a sequester force compromise and action. And obviously those are the critical two words that I think is our burden to satisfy here, as Members, which is, A, to compromise and, B, to act.

And if you finish the story in terms of Gramm-Rudman, it was a bumpy ride to get to the point where we started to actually deal with the structural deficit that existed at that time. It was really not until President George Herbert Walker Bush negotiated the compromise at Andrews Air Force Base that moved off some sort of sacred cows to get to a measure, but it adopted the PAYGO rules which, again, put real discipline into the proceedings of Congress and the budget that President Clinton passed in 1993, which changed the tax rates that finally intersected spending and revenue to a point where for the first time in our lives, we actually had the Government's public finances in balance. And by the way, we created 22 million jobs during that time period.

When I view the Budget Control Act, which, again, I joined the majority of people in this committee supporting passage, that is certainly the path that I think we voted for or should have been thinking we were voting for, that compromise in action was what we were looking for, not a chainsaw going through the Government. So it is going to require people to move off of pledges and some sacred positions to really fix the problem.

And again, we have a historical precedent. We can do this. Our country did it. And again, your testimony—all of you here today—again, reinforces the fact that the stakes are huge if we don't.

One issue, which you have mentioned, a number of you, is the question of, again, having that horizon, that stability, which really provides the basis for you to move forward and plan and invest. Coming from a district where the construction of nuclear submarines takes roughly 4 to 5 years, obviously a 1-year horizon is not enough in terms of really trying to, you know, get to that sweet spot of efficiency and quality. One of the measures that we have been voting on here is just a 1-year fix to sequestration. And I was wondering if you could just sort of comment whether or not that, in your mind, really fixes the problem or just delays it and just, again, leaves the challenge of trying to do intelligent planning sort of out there for just a short period of time.

Mr. STEVENS. Well, we are a long-cycle business. Our products last 20, 30, 40 years. Right now, we don't have 6 months' visibility, which is unprecedentedly short. And we are doing our planning for our business cycle in detail right now, 1-year, 3-year, 5-year. I do think—the best suggestion I can give, recognizing how complex and difficult the actions will be associated with this suggestion is a complete, a comprehensive, a balanced and an integrated a durable approach is I think the very best solution. When we look at the challenges in our company, we think a lot about growth. The growth of our business—and I think you could extrapolate the growth of our country—is through competitiveness. That means getting the best talent, investing in that talent, getting the best innovation and investing in that. That investment cycle is absolutely determined by how much visibility and how much certainty or uncertainty is in the environment. Right now, there is crushing uncertainty that is limiting all of that. So the more comprehensive a solution that can be put together, the longer duration of that would clear the deck chairs considerably and I think open up degrees of freedom for businesses to take actions that would lead to that kind of growth that we are looking for in our business.

Mr. O'KEEFE. I would simply offer to add to that, the history that you describe—I think most accurately—is to the extent that this particular mechanism is useful for the purpose of prompting process reform and adherence within the determination of public policy and public finance choices, that is terrific. To the extent, though, that it also serves to create unrest in the marketplace, a complete, you know, lack of confidence and any stability down-phase because of the prospect of this sort of Damocles, as it was called historically at its point of origin, to the extent that it could be triggered, if that creates the kind of market disruption that is seen to the point of I think reaction a year ago. That does nothing to add or contribute to the stability either. So this is a double-edged sword. There is no question. It is in some respects perhaps a Hobson's choice that is uniquely a challenge that you confront. As Members of Congress who have to wrestle with this question, I don't envy you at all.

The CHAIRMAN. Thank you. The gentleman's time has expired.

Mr. Wittman.

Mr. WITTMAN. Thank you, Mr. Chairman.

Ladies and gentlemen, thank you so much for joining us today. We appreciate your perspective. It has been very telling as to what may be looming out there if sequestration takes place.

I want to summarize some of the comments that you all have made. I think they are very telling. Some of the adjectives you used, uncertainty, instability, unrest. Obviously as that relates to what you all have pointed to as your greatest asset—that is, your intellectual capital, your human capital—that affects that significantly. I would argue that both in our uniformed services and the U.S. supporters of those uniformed services is those intellectual capacity assets that are most valuable and that if we lose those or if those are weakened, that we weakens us in the future. Even if we don't get to sequestration, even if it is put off, as you are quoting us today, that uncertainty is building. That affects your workforce. That affects your capacity, your capability. Those things are concerning to me.

What I do want to look at though is to try to define, if we do get to this sort of Damocles, as it has been termed, of sequestration, what effect will it have on your current contracts? Will those contracts have to be terminated for default? And if so, what does that mean for your employees, for your partners, for your suppliers? I think that has a significant effect. What would happen with the restructuring of those contracts? I want to make sure we understand not only the uncertainty that is leading up to that but what happens if—and what does that mean for you all—and you talked about long term. Obviously, the contractual agreements there are what is going to affect you in the long term. So I would like to get your perspective on what that scenario might hold.

Mr. STEVENS. Well, we certainly think it will affect a lot of contracts, broad-based, thousands perhaps. I don't believe these terminations would be for default because it is not a for-cause termination. It would be a convenience termination, if the contract were terminated. Contracts can be reformed without being terminated, which I rather suspect will be the majority of the cases. We probably won't stop buying everything. We will just buy fewer or less.

And that would require folks like us to go into the supply chain and reschedule all the work that is being done to accommodate a lower profile of resources available to put under contract. It is our sense that our suppliers will look at that environment, look at that action, and call that a business disruption and will, as a result of that business disruption, formulate a claim, a request for equitable adjustment or some consideration under the contract.

So one of the areas we are still trying to explore in greater depth is, if $55 billion is needed, that is a net number. There is likely to be some business interruption or disruption claims flowing back. Do the cuts actually have to be deeper than $55 billion to achieve a net $55 billion outcome? All of that will unfold very broadly, probably all at once when we get agency guidance about either terminations or reformations of contracts. And it will require a huge amount of administrative and auditing effort to prepare these claims to submit them and to deal with this administrative environment.

Mr. WITTMAN. Mr. O'Keefe.

Mr. O'KEEFE. I agree entirely with the representation as well as the process that Bob Stevens has walked through. I think that is a certainty. Other than to simply add, this is going to be a full employment act for auditors. And if you are an attorney, this is going to be a great opportunity to do all kinds of things in the future because everything now is going to be subject to adjustment in these cases of review at the levels he is talking about. It is just about impossible to estimate what the consequence of that will be at this juncture.

Mr. WITTMAN. Mr. Hess.

Mr. HESS. I think your question is a very good one and one that hasn't really been considered. There is clearly going to be a cost to sequestration that hasn't been considered here. And I think Bob described it well. But clearly, if you look at the volume of contracts that would have to be repriced and requests for equitable consideration, it is a huge task both for the contractor as well as for the Department of Defense to administer all of that. We don't know quite honestly how it would be accomplished.

Mr. WITTMAN. Ms. Williams.

Ms. WILLIAMS. The effect I think that it is going to have on us—I have already had five contracts put on hold. They have not been stopped. In fact, I have been even asked by the contractor, when could you finish this? Well, when you give me the funds to finish it. You know, it is that simple. And they are not forthcoming. And when you ask them where the funds are, when we could expect it, you can't. So we are virtually shut down on those five contracts right now.

The CHAIRMAN. The gentleman's time has expired.

Mr. Johnson.

Mr. JOHNSON. Thank you, Mr. Chairman.

I have got to tell you, I had to pinch myself as I prepared for this hearing today. I thought I might be dreaming. House Republicans are holding hearings that talk about how cuts to Government spending are going to hurt jobs and the economy. It is really amazing.

Now no one thinks sequestration is a good idea. The meat-ax approach to defense cuts is irrational, and it is obviously bad policy. And it was designed by my colleagues on the other side of the aisle, the Republicans, to be so bad that we would make tough decisions about raising revenues and cutting spending so that we could avoid it.

Nevertheless, here we are playing brinkmanship again. The same folks who self-righteously opposed President Obama's $700 billion stimulus package, the same folks who sneered and said Government never created a single job in America and never would, they are now wringing their hands because the impact on jobs of about $50 billion in defense cuts in 2013—of course, it is $500 billion over 10 years, but $50 billion next year.

Now there is an easy way out of this: Make tough choices and tough compromises to raise revenues, cut spending, and meet our budget targets. The President is willing to do that. The Democrats in the House are willing to do that.

What is the Republican solution? The Ryan budget: Cut employment and training programs, cut food stamps, cut health care for children, the sick and the poor, cut foreclosure prevention, cut taxes for the rich, and lard up the defense budget with an East Coast missile shield, nuclear facilities that no one wants, and billions of dollars of waste, far in excess of caps under the Budget Control Act.

With all due respect to our witnesses today, you won't see House Republicans calling community leaders, church leaders, the owners of mom-and-pop businesses or struggling homeowners to testify on the impact of all of these cuts to help the poor and the jobless and the sick.

Now to our witnesses today, each of you are highly talented, highly sought-after executives. And I imagine that you are pretty well compensated for the value that you add to your companies, and I deeply respect that. As you have made clear, you are also rightly concerned about the impact of sequestration on your businesses, your employees, and our country's national defense.

My first question is, would each of you be willing to forgo the 4 to 5 percent of your annual income that you save under the Bush tax cuts in order to avoid sequestration? Yes or no? Mr. Stevens?

Mr. STEVENS. I am afraid I am not going to be able to give you a yes or no answer to your question, sir, and I offer that to you respectfully.

Mr. JOHNSON. Okay.

Mr. STEVENS. I have never——

Mr. JOHNSON. Good enough, good enough right there. Mr. O'Keefe?

Mr. O'KEEFE. Mr. Chairman, I think the choices over revenue and spending is entirely the prerogative of the Government, the Administration, and Congress.

Mr. JOHNSON. Would you be willing to forgo your savings if the Bush tax cuts were made permanent in lieu of sequestration? Would you rather have your 4 or 5 percent and undergo sequestration or would you—you know, what is your position?

Mr. O'KEEFE. My opinion of the priorities are far less significant than yours.

Mr. JOHNSON. Okay.

Mr. O'KEEFE. You are empowered——

Mr. JOHNSON. Well, you are not going to give me an answer on that?

Mr. O'KEEFE. No, sir. I think that is a prerogative, it really is important for you to make those choices.

Mr. JOHNSON. All right. I have got you. How you about, Mr. Hess?

Mr. HESS. I would echo Mr. Stevens' response.

Mr. JOHNSON. All right. And Ms. Williams?

Ms. WILLIAMS. I would do the same.

Mr. JOHNSON. Okay. Well, nobody wants to give up their 4 or 5 percent that they would save if the Bush tax cuts were made permanent. That is exactly the sentiment that is being represented by the Republicans here in Congress. They will not impose any taxes, any tax increase on those who can afford to bear it because of the Grover Norquist pledge, and my time has expired.

The CHAIRMAN. The gentleman's time has expired. Just a little update on history as to how we got here. We had last year the opportunity to vote for the Budget Reconciliation Act or shut down the Government. At the time a compromise was worked out with the Administration, the Senate, and the House, and Budget Reconciliation Act was passed and signed by the President. So all three parties were involved.

Since then we have passed in the House a solution for this that pays for the first year of the sequestration. There had been a lot of talk about we will not support tax increases and the Democrats want tax increases. We have taken action in the House. The Senate has done nothing but talk. All they have to do, according to the Constitution, is pass a bill in the Senate. Then we would go to conference, and then we have real negotiation. Then we will have real talk because plans have been laid out and passed. But the Senate has refused to take action, and the President has not given the leadership and the direction to get us past this point. So that is just correcting the history.

Mr. Scott.

Mr. SCOTT. Thank you, Mr. Chairman, and ma'am and gentlemen, thank you for being here today. We do have fundamental differences, certainly. The Democrats believe that higher tax rates lead to higher tax revenues. I fall into a different camp. I believe that businesses embed the costs of their taxes into the products that they sell, and the higher the tax rate is, the more a product costs, and therefore the less of that product they get to sell and therefore giving an advantage to our industries' overseas competitors. If you listened to the President's initial speech a couple of years ago, he talked about the fact that we needed to actually reduce the corporate income tax rate. We as Republicans embraced him on that, and then he turned around and withdrew and never gave us a specific proposal.

But 18 months ago I was a small business owner, Ms. Williams, and so I will tell you what I found in my small business was that my percentage of fixed costs were much higher than larger competitors. I didn't have the ability to play with variable costs the way the larger competitors do. Do you think that—and so the last dollar's worth of revenue meant much more to me as far as the end profit at the business and therefore the amount that I paid income taxes on. Do you think that is—have you found that to be true in your industry?

Ms. WILLIAMS. Yes, sir, that is true, very much so.

Mr. SCOTT. And that is where I am very concerned with kind of this anti-profit mentality that some have in Washington right now, that while our large industries, and I certainly want all of our large industries that operate ethically to be profitable, but my real fear with the economy today is what we are doing to our small businesses and the suppliers to the large guys, and if you lose 8 percent of your revenue, Mr. Stevens, I think the impact on Ms. Williams of an 8-percent revenue loss would be much greater on her business and her employees therefore.

So I want to go, though, if I could to you, Mr. Stevens, because you talked about back-of-the-envelope math, and you have got approximately an 8-percent operating margin in your business if I am correct; is that right?

Mr. STEVENS. It is closer to 10. But yes, sir.

Mr. SCOTT. Closer to 10. And your profit margin on that is somewhere in the 6 percent range, just above 6 percent if I am not mistaken.

Mr. STEVENS. Yes.

Mr. SCOTT. And when you talk about your back-of-the-envelope math, you take that 8 percent, and you have got approximately 120,000 employees, you multiply that 8 percent, which would be your approximate 10 percent, which is kind of the number we are assuming will be your cut to revenue, 80 percent of your revenue is Government business, so that is an 8 percent loss, which happens to correlate, quite honestly, pretty close with your operating margin, and it also correlates pretty closely with what you say your reduction in employees will be because if the company is not profitable, nobody gets a paycheck. Is that a fair statement?

Mr. STEVENS. Certainly we perform against a set of objectives every year where profitability is an important objective for every business. You extinguish your ability to perform if you don't generate a profit, that would be correct.

Mr. SCOTT. So this is my question for those of you with publicly held companies. What are your SEC [Securities and Exchange Commission] obligations with regard to sequestration? How has the impending threat of sequestration affected your reporting to your shareholders and the fact that this is currently the law, there are no plans to rescind this law other than what the House has done, and what, again, obligations do the three of you have to your shareholders to discuss sequestration?

Mr. STEVENS. As a result of being a publicly traded company, but I would say it is true of every high integrity business person we know, we have duties of loyalty, of transparency in our disclosures, of not acting in a way that is imprudent with respect to the business, not taking unnecessary risks, but importantly conveying with honesty and accuracy within our best professional judgment the status of the business and the risks associated to the business certainly to the equity investors in the company. We have a collateral responsibility to the bondholders, the credit rating agencies, certainly to our customers and our suppliers because they are our partners in this enterprise. So we have been disclosing under our SEC disclosures in 10–Qs and other correspondences the nature of sequestration, including the discussion of the WARN Act, and we will continue to do that.

Mr. SCOTT. Mr. Stevens, I am very short on time. If we could get to Mr. O'Keefe and Mr. Hess.

Mr. O'KEEFE. That is precisely the same debate we are underway with right now in looking at what our various obligations are.

Mr. HESS. Again, we clearly plan to adhere to the requirements of the WARN Act, and we are looking at the possible impacts and doing some scenario planning now. Absolutely we have a fiduciary responsibility to our shareholders and our boards to do exactly that.

The CHAIRMAN. The gentleman's time has expired. Mr. Ryan.

Mr. RYAN. Thank you, Mr. Chairman. Back when I was younger I used to coach like 9th grade football or 9th grade basketball, 7th and 8th grade, and there is a stunning dynamic when you get into coaching and you are coaching kids. You could be a coach and see a coach, and they could be the most objective person in the world in analyzing their players and their talent. Then their kid is on the team, and they lose all objectivity, right? They think their kid is a little better than they probably are, so their kid starts and all of this other stuff. We all know that happens in the midst of Little League season. And I feel like my friends on the other side, and it is just stunning to watch this hearing, completely have a blind spot when it comes to Government spending for the military. Now, I represent Akron, Ohio, so I have Lockheed facilities, we have lots of defense, we have got a lot of Tier II, Tier III. I get it. This is Government spending, and it is creating jobs, and the scenario that we are talking about right now is that a cut in Government spending is going to cost jobs, and that is why we are here, and we don't want to see that happen. And to have my colleague from South Carolina talk about, you know, the jobs in Virginia that are going to be lost or the WARN notices, the WARN notice was put into law by an Ohio Senator, Senator Metzenbaum, because of factories being closed down in the 1980s. So we know that, you know, what could potentially happen here in my district and in our State, and I just find it stunning that we can sit here and have a conversation about job loss because of these reductions, but turn around in the same breath and say that the stimulus package had absolutely no effect, didn't save any jobs when numbers and every economist basically will tell us otherwise.

We need your help because there is a narrative in this country right now that every dollar that the Government spends is a waste of money, should be privatized, outsourced, done by the private sector, so on, so forth. Transportation, education. And I just—and I am not here to lecture anybody, but I just find it stunning because I am on the Budget Committee, too, and I have to listen to—you know, I just try to imagine if you were energy companies, if you were alternative energy companies, if you were a solar panel company, if you were a windmill company, and there was Government funding, saying we need to reduce our dependency on foreign oil, so we want to contract with energy companies and put up windmills so we can reduce our dependency and get out of all these entanglements all over the world, you guys would be crucified right now, crucified. And I am with you. I think this is a bad idea. I think I like the chainsaw, you know, for cosmetic surgery analogy. This is terrible what is going to happen, and it is stupid. But we need your help to say, hey, all Government funding isn't bad, you can't just be concerned with your one little slice of the pie because you are getting bombarded by a narrative, quite frankly, that has been created by the other side, and we have all got to deal with this problem, I get it, but it is overwhelming, and now we are all swimming upstream trying to say, well, wait a minute, this funding is very necessary because it has got all these jobs and here is the Tier II and Tier III supply chain that is going to be affected by this. And if a guy like me from Youngstown, Ohio, comes out and says, well, maybe we need some Government funding for security in our neighborhoods and we need to fund the COPS [Community Oriented Policing Services] program or we need to fund fire grants, I would be crucified. I am a liberal tree hugger, Government doesn't have a responsibility to do that stuff. Security is security. And it is just important for us, we have got to get past this because this is ridiculous. This is the end result of 20 or 30 years of bashing the Government, and here we are, sequestration is all coming right to a head right now.

So I just want to ask one question of all of you if you can quickly give me an answer or one of you can speak for the group because the time is short. We are going to have to go out and borrow money to make sure that this sequestration doesn't go online. We have got to borrow it. So I don't want it to go online, I don't think it is a good idea. Help me make the argument to my constituents that it is okay for us to go out and borrow money to make sure that these cuts don't happen. Can you help me make that argument why it is valuable at this point in a deep financial crisis that we are in? Why it is important for us to go out and maybe borrow it this time until the economy recovers? Can any of you help me make that argument in Ohio?

The CHAIRMAN. The gentleman's time has expired. He made some beautiful, eloquent arguments, but you will have to answer those for the record if you would.

Mr. RYAN. Could I get those for the record, Mr. Chairman?

The CHAIRMAN. I would be happy to ask the witnesses if they will provide that for the record.

Mr. RYAN. Thank you.

[The information referred to can be found in the Appendix on page 141.]

The CHAIRMAN. Also for the record, this committee is the Armed Services Committee. We have the responsibility to look after the defense of this Nation which is in our Constitution. We have the responsibility to provide for that defense of the Nation. So there is a difference between that and providing for COPS.

Mr. RYAN. Will the gentleman yield?

The CHAIRMAN. I would be happy to.

Mr. RYAN. We also have a responsibility to provide for the general welfare.

The CHAIRMAN. We do.

Mr. RYAN. I think when you look at the gentlemen that Mr. Stevens was talking about, the young people that he wants to hire, something——

The CHAIRMAN. Reclaiming my time.

Mr. RYAN [continuing]. Would tell me that those are——

The CHAIRMAN. This is not the general welfare committee, this is the Armed Services Committee. We have the responsibility to provide——

Mr. RYAN. But I would just add, Mr. Chairman, we have an obligation to make sure that Mr. Stevens keeps getting those bright, intelligent people that he wants to hire——

The CHAIRMAN. Reclaiming my time.

Mr. RYAN. Something tells me that they got a Pell grant, they went through public education.

The CHAIRMAN. Reclaiming my time. We could go on, I am sure, Mr. Ryan, for a long time.

Mr. RYAN. I am happy to, Mr. Chairman.

The CHAIRMAN. But we do not have the time at this moment. And we will now turn the time to Mr. Garamendi, 5 minutes.

Mr. GARAMENDI. I almost want to give you time to answer the question, but it probably won't——

The CHAIRMAN. Do you want to use your time for that?

Mr. GARAMENDI. No. We are going to have a written response perhaps.

Gentlemen and ma'am, you are leaders in America. You really are. You are the titans of industry, big and small, and you have awesome responsibilities not just to your shareholders but to your workers and really to this Nation. That responsibility is very direct in the military and the defense of this Nation, as the chairman just pointed out. But your responsibilities, because of your position, go far beyond that. It really goes to leading and providing leadership. We have had some discussion from Mr. Johnson and now Mr. Ryan, and I think it is really important. I don't want sequestration. I voted not to have sequestration. But the real question underlying all of that is about the deficit and about the financing of our Government, and it is either going to be cuts, you have argued against cuts in the defense industry, okay. And my question is then what do we cut and/or, and/or do we raise revenue? And I want you to answer this question as a leader in America that each of you are.

Mr. Stevens, what do we do? Do we make cuts in other areas? And if so, what? Do we raise revenue? If so, where?

Mr. STEVENS. The very best answer I can give you, and I am flattered that you regard me as a leader. I take my leadership responsibilities seriously, my board holds me accountable, investors, employees, members of the communities in which we live and work. We look to you, sir, respectfully, the Members of this committee and Congress, as leaders, you are our leaders. We have a portfolio of responsibilities in our company. That is my domain. I truly do look to you and others to wrestle——

Mr. GARAMENDI. Let me ask——

Mr. STEVENS [continuing]. With these incredibly complicated circumstances.

Mr. GARAMENDI. Excuse me for interrupting. Does your company contribute to political contributions, to political action groups, and do those action groups express your opinion?

Mr. STEVENS. We do contribute to them, yes, sir.

Mr. GARAMENDI. For example, do you contribute to the Chamber of Commerce, the U.S. Chamber of Commerce?

Mr. STEVENS. We do.

Mr. GARAMENDI. Okay, do you agree with their view that there should be no taxes, no tax increases?

Mr. STEVENS. We contribute to organizations that we think in the main express the view that we have, which I believe is the focus of the committee's attention today on a strong national security, and my role here today is to communicate in my best effort the disastrous effects of a sequestration that will disable our ability to contribute to the national security, sir.

Mr. GARAMENDI. I am going to just forgo the rest unless you would like to answer my question. The reality is you have twice, three times now you have been asked the question, and then I would just ask you to take up your leadership role beyond the narrow focus of your own company. You are leaders.

Mr. O'Keefe, you were the leader of a major university, a very successful university. You have a different role today, but you have not given up your leadership role in this Nation. You were Secretary of the Navy. We have a very, very, very difficult, very difficult situation, one that requires each of you, all four of you and other leaders around this Nation to really come to grips with the reality and put aside all the political rhetoric, much of which you have heard here, and help us. Yes, I do have a responsibility, I am more than willing to take up that responsibility and have. But you also have a responsibility. And I would ask you to ponder, if you would, that responsibility to speak out on this issue. If you don't want cuts in the military, then where do we cut? Social Security? Medicare? Employment opportunities? Education? If we don't want to cut there, then what revenues do you want to increase and where do we do that? Or do we not do it at all?

I am going to let it go at that. I don't want to put you on the hot seat anymore, but I really would ask you to take up your larger responsibility as very, very influential men and women. Thank you very much.

Mr. O'KEEFE. Congressman and Mr. Chairman, if I could respond for just one moment, I very much appreciate the spirit and context of your commentary, and that is primarily what you have offered here. And certainly I think we all accept the leadership responsibilities we bear, and that is why we are here. We were invited and requested to speak to a mechanism of how to achieve these kinds of targeted reductions, not what the alternatives are. Those are really complex challenges that again you have observed the importance of really having an opinion as citizens, and that is an entirely separate point. In terms of institutional challenges, what you face is the challenge of, again, revenue and spending objectives and how that gets sorted out, there are methods to do it, and this is one we are simply advising is more destructive than others, not where it is applied. It is across-the-board on domestic and defense, all discretionary spending, just as observed in the very opening comments.

Thank you.

The CHAIRMAN. The gentleman's time has expired.

Mr. WILSON. Mr. Chairman?

The CHAIRMAN. Mr.——

Mr. WILSON. Mr. Chairman? As we conclude, we have just received sad news of a terrorist attack on a bus in Burgas, Bulgaria, and I want to express my sympathy for the tourists from Israel and our NATO [North Atlantic Treaty Organization] ally Bulgaria.

The CHAIRMAN. Thank you. Mr. Smith.

Mr. SMITH. Thank you. I want to follow up on that point because we have heard a number of times from all of you that, you know, when we get down to the tough question of how to actually avoid this that basically that is on us, that is up to us as if, you know, everybody else in the country has no role whatsoever to play in public policy decisions.

Let me tell you, that attitude that you expressed right there is the number one biggest problem in solving the problem, is the notion that you have no responsibility in solving the problem. The only responsibility you have is to explain to us how bad it is going to be in one given area because that is exactly what public policy has come down to in this country, everybody protects their own piece. And I will say this, you are in no way unique in that regard. Everybody who comes back here is concerned about what happens to Medicare and Social Security or they are concerned about this tax going up or they are concerned about defense being cut or concerned about something else, and then when we come down to how to add it up they say, oh, no, we can't, that is not us, we can't have anything to do with that. So what happens is we divide and destroy, and every little piece of our country protects themselves and makes no argument whatsoever beyond that because that is easy. It is much easier to say don't cut this, don't raise that tax. The hard part of governing—and in a representative democracy theoretically we all have some responsibility for governing—is making choices, and everybody does exactly what you did today. You flat refuse to say anything about making those choices and dump it all on us. Meanwhile, not only do you flat refuse to say anything about it, but you also take steps that systematically kick our legs out from under us as we try to deal with it. Mr. Garamendi pointed out some of that. But even if it isn't taxes, if nobody, but nobody is advocating for the types of cuts or the types of tax increases that are necessary to deal with our deficit, then you are never going to be able to build the political support necessary to get this Nation to support those steps. It is just not going to happen, and everybody conveniently hides behind that. And I know why. Because it is brutal. And ultimately I will say this: We have a far, far greater responsibility, there is no question. But that will always play out because we are the only ones that ultimately have to vote and will ultimately be held accountable for that decision. That greater responsibility is baked in, and there is no way for us to duck it one way or the other. But to the extent that group after group, individual after individual comes up here and says don't cut this, don't raise that tax and balance the budget, and then refuses to move the needle at all on a solution to that problem, refuses to take a leadership role in moving the debate in the direction of getting the country to acknowledge that choices have to be made, we are dead. There is just no way we can get public opinion. That is why you can take public opinion polls, I have this Pew research poll, and I will close with this, from February 2011 that best sums up the problem. It asked people if they were concerned about the deficit. Eighty percent said we ought to basically balance the budget. And then it listed every single area that the Federal Government spends money and asked if you would like to see the amount of spending there kept the same, cut or increased. Over two-thirds of the people on every single category save foreign aid, which still managed to get 50 percent, so 99 percent of where we spend our money, two-thirds said increase it or keep it the same. Those exact same people who expressed profound concern about the size of the deficit, and then of course they asked them if they wanted to raise taxes, and they all said no. Now where do these opinions come from? How do people form these opinions? They form these opinions because all they ever hear is people advocating for spending and tax cuts. They never hear anybody advocating for the ability to make that work. So that is why we get a little vexed when people like you come up here and say you are going to kill our industry if you fix this. Okay, well, we get that, but the reason that you are in the position you are in is because of the problems with our deficit, okay? Because they are very real and necessary problems. So if you didn't say, okay, well, what do we do to get out of it? Oh, we have got nothing to say on that, except of course for all the ads we run to say don't cut—don't raise taxes or in some cases don't increase spending. So what you are doing isn't helping. Certainly not solely responsible. There are many others, all of us in many ways, you know, in Congress many times advocate for things that don't add up either, but we have got to get past this, look, I am only here to talk about my area, don't talk to me about the rest because it is a budget, it all adds up and we have to make those decisions, and we need help in getting the public to support those decisions because if they don't, it won't happen.

The CHAIRMAN. My good friend and I sometimes disagree.

Mr. O'KEEFE. Mr. Chairman——

The CHAIRMAN. This is one of those, one of those times. None of us was forced to run for this job. Each of us chose to run for the House of Representatives, we understand that we have the responsibility to make the final decisions. These people are here today at our request to talk about the guidance that they need to implement the laws that we have passed. I have not heard them say, don't cut defense. That—maybe we should have another hearing on that, but I haven't heard them say that. What they have said is you already implemented $487.0 billion, we are implementing that, we are taking care of how we can manage that. You have given, you have passed a law that is going to cut another $500 [billion] to $600 billion out of defense. We are just wanting to know how, as business people, do you expect us to comply with the law that was passed and carry out those instructions to the best of our ability? That is what this hearing was for. That is what they have advocated, that is what they have talked about.

You know, I come from a small business background, and it wasn't anything like building ships or planes or boats. We sold western wear, pretty simple little business, family business. But even at that level we went to a market in January to buy products that we were going to sell for the first half of the year, and we would go to the different booths, and we would buy shirts and boots and hats and jeans and the things that we needed for our customers, and they would be shipped in a timely manner so we would have inventory in February and March and April and May, and customers would come in, and they would expect we would have the size and the things that they needed. Meanwhile, our suppliers, after we gave them orders in January, they would go to their suppliers, and they would buy the things they needed to make the jeans and the hats and the boots and shirts, and it was done in an orderly method because we didn't have the Government involved. They are trying to run their business in an orderly manner, and they want to know what they need to do in January and February and March so that our warfighters that are over in Afghanistan right now going outside the wire every day, putting their lives on the line will have the things they need to protect themselves and to carry out their mission at the direction of our Commander in Chief. And I applaud them for the job that they do, I applaud all of our workforce that is invested in that and gets up every day, goes to work at the best of their ability trying to carry out their mission to see that those warfighters over there return home safely, and that is the responsibility of this committee, and we will continue to carry out that responsibility. There are other committees, I also sit on the Education Committee, and I can go across to the Education Committee and I can talk about things, but while I am here as chairman of this committee, we will carry out that mission of looking out for our warfighters who are putting their lives on the line.

Thank you very much for being here today. I have one other final question I would like you to submit for the record. We have OMB coming up here the 1st of August to testify. You have all talked about things that you would like to see, but I would specifically ask, can you please describe, except for Ms. Williams who doesn't have to deal with the WARN Act, guidance from the OMB and the Department so that we can give them these questions beforehand necessary for you to begin making decisions related to the onset of sequestration. If you could get that to us at the earliest possible so that we can get it to them so that our hearing on August 1st will be productive.

[The information referred to can be found in the Appendix on page 141.]

The CHAIRMAN. Thank you very much, and this hearing stands adjourned.

[Whereupon, at 12:40 p.m., the committee was adjourned.]

APPENDIX

JULY 18, 2012

PREPARED STATEMENTS SUBMITTED FOR THE RECORD

JULY 18, 2012

Statement of Hon. Howard P. "Buck" McKeon

Chairman, House Committee on Armed Services

Hearing on

Sequestration Implementation Options and the Effects on National Defense: Industry Perspectives

July 18, 2012

The House Armed Services Committee meets today to receive testimony from our industry partners on the challenges of planning for sequestration. Since we began this hearing series back in September we have held seven hearings and one briefing on sequestration, the bulk of which have delved into the impact of sequestration on our military capabilities and national defense.

Today we are holding our second hearing that is focused on the economic impact of sequestration, this time focused on the implications for the defense industrial base that enables and supports our warfighters. Joining us today are Mr. Bob Stevens, Chairman and CEO of Lockheed Martin; Mr. Sean O'Keefe, Chairman and CEO of EADS North America; Mr. David Hess, President of Pratt & Whitney; and Ms. Della Williams, President and CEO of Williams–Pyro. In addition to their own companies' perspectives, I should note that Mr. O'Keefe also chairs the National Defense Industrial Association and Mr. Hess chairs the Aerospace Industries Association. Ms. Williams is on the Board of the National Association of Manufacturers.

Barring a new agreement between Congress and the White House on deficit reduction, over a trillion dollars in automatic cuts—known as sequestration—will take effect. Although the House has passed a measure that would achieve the necessary deficit reduction to avoid sequestration for a year, the Senate has yet to consider legislation. And the President's Budget submission, which sought $1.2 trillion in alternative deficit reduction through increased tax revenue, was defeated in a bipartisan, bicameral manner.

This impasse, and lack of a clear way forward, has created a chaotic and uncertain budget environment for industry and defense planners. While the cuts are scheduled for implementation January 2nd, companies are required to assess and plan according to the law—and sequestration is the law right now.

We've all heard the growing number of estimates. Secretary Panetta has warned sequestration would be "catastrophic" to our military and result in the loss of 1.5 million jobs and a 1-percent increase in the unemployment rate. This would send 200,000 of our men and women in uniform from the frontline to the unemployment line. It would as the Secretary has said, result in the smallest ground force since 1940, the smallest number of ships since 1915, and the smallest Air Force in its history.

The National Association of Manufacturers warned that "dramatic cuts in defense spending under the Budget Control Act of 2011 will have a significant, negative impact on U.S. jobs and economic growth." The Manufacturers' forecast, and one by Dr. Stephen Fuller on behalf of the Aerospace Industries Association, have estimated private sector job losses at over a million.

Faced with the prospect of being forced to lay off workers, renegotiate contracts, disrupt production, and give bad news to shareholders, industry leaders have been attempting to get more guidance from the Administration on how they will interpret and implement the law. To date the guidance has been piecemeal. For example, last fall the Pentagon stated that war funding would not be sequestered. Then in May, OMB overruled the Department and declared that while Veterans benefits would be exempt, funding for the troops on the front line would not be exempt. In June 2012, Secretary Panetta met with various defense industry executives to discuss the impact of sequestration on their operations and to gauge the current state of the industry in general. In addition, press reports indicate that the Director of the Office of Management and Budget met separately with heads of several major defense companies.

Unfortunately, it doesn't sound like industry learned much from those meetings. Reports indicate OMB made it clear that it does not plan to issue implementation guidance until at least November, less than 2 months before sequestration is scheduled to take effect. My fear is that guidance will come much too late. Industry faces a host of planning challenges and requirements to be met this summer, not the least of which is the WARN Act, which requires most employers to provide notification at least 60 calendar days in advance of mass layoffs and plant closings. In some States, the requirement is 90 days. That means, as we'll hear today, defense companies are currently grappling with whether to send pink slips by November 3rd to their employees.

In addition to the issue of jobs, I worry that the cavernous silence from the President will lead many to exit the industry or to walk away from capital investments that are in the best interest of our troops. As I've said many times before, the men and women on the front lines have our backs. Who is going to have theirs if we allow the impending threat of sequestration to shutter the American industrial machine that enables them to fight, win, and return home?

This overdue guidance from the Administration on how they intend to interpret the law and implement sequester mechanically is critical to employers, not to mention Congress, and I look forward to our follow-on panel with the Director of the OMB on August 1st.

We all believe there is strong bipartisan agreement that sequester is bad policy and should be replaced. My hope is this hearing will provide additional incentives for the Administration to provide more information to employers and for all parties to resolve this impasse. I look forward to your insights today.

Statement of Hon. Adam Smith

Ranking Member, House Committee on Armed Services

Hearing on

Sequestration Implementation Options and the

Effects on National Defense: Industry Perspectives

July 18, 2012

I thank our witnesses for being here to discuss this very important subject and to give their perspectives on it. As some of our leading employers in the defense industry, their perspectives are critically important as we go forward, both in terms of the industrial base issues and in terms of the impact on our broader national security, and I completely agree with the chairman that sequestration is not a good idea. It would be bad for our economy, bad for defense. I always hasten to point out not just defense, it is, you know, a sort of mindless across-the-board cut in all discretionary spending. So education, transportation, infrastructure, on down the line that would have a devastating impact, and part of the problem in addition to that is that the Budget Control Act was not particularly well drafted. I have heard dozens of different opinions about what it means and what exact effect it would have, what is exempt, what isn't exempt, how would you implement it. Nobody knows for sure until we actually do it. That is part of what the Administration is wrestling with.

So I don't think there is any dispute that it is bad. I have not heard the White House dispute that. Secretary Panetta, in particular, has been very forceful on explaining how awful sequestration will be. The problem is, it is not like you can really come up with a plan that is going to make it anything other than awful. The burden, the real burden of this committee, this House, and the Senate, and the President is to get rid of it one way or the other, to make sure that it doesn't happen. If it happens, it will have a very profound and negative impact. And it is also worth pointing out and I think the chairman has done an excellent job of this, this is a problem right now. We tend to look at it and say, well, sequestration kicks in on January 1st and people begin to imagine that that is the deadline. But all of you and thousands of other employers are making decisions right now based on what they reasonably project will happen in the next fiscal year, and those decisions are leading to people hiring less people and in some cases laying them off in anticipation that cuts will come one way or the other. So it definitely needs to be avoided.

But we also need to look at the larger problem in terms of what got us into this and why we are having such a devil of a time getting out of it. There seems to be this opinion that while this is a terrible, terrible thing and it is just sort of fundamental incompetence that is preventing us from dealing with it, it is really not. It is more denial about the fiscal situation we are in. Let's go back to the fact that we are only here because of the refusal of the majority of people in the House to raise the debt ceiling. This deal was done as the only way to raise the debt ceiling and stop the United States of America from defaulting on its obligations for the first time. It was only that sort of blind notion that somehow not raising the debt ceiling was a solution to our fiscal problems that forced us into this awful, awful decision, an awful decision which I didn't support, mainly because it put all of the burden on the discretionary budget.

We unquestionably have a budget problem, we have a $1.2 trillion deficit, actually 1.3 last year, a 38-percent deficit, and it needs to be addressed. Thus far we have put all of the burden of that on the backs of 38 percent of the budget, which is the discretionary spending budget, and we have refused to talk about revenue. So the solution going forward, the thing that will help us come together and come up with the deficit control steps necessary to avoid sequestration is, number one, admit that we are not balancing the budget any time soon. We would all love to have a balanced budget, but there isn't an economist out there that won't tell you doing that in the near term would be devastating to the economy. We are going to have structural deficits for a while. Our role is to get those deficits under control so that they are manageable, but we can't hold hostage steps that will do that to the notion that we have to have a balanced budget right now or even in the next 3, 4, 5, 6 years. So admit that. And then, second, everything has to be on the table. We are going to need more revenue. We have cut taxes across the board over the course of the last 10 or 12 years. If we are truly, truly committed to providing for the men and women who serve us and providing for our national security, then we absolutely have to be willing to raise the revenue to pay for that. That is a critical, critical piece of it. And, yes, we also have to look at the other 62 percent of the budget, the mandatory spending, and find savings there as well. So that sort of realistic discussion is needed. Right now there seems to be this desire for a balanced budget. Also a desire to not raise revenue and a desire not to cut any spending that is important. Those numbers don't add up.

So I hope this committee can begin to be part of the process of starting a realistic debate that can avoid the truly awful outcome that would come with sequestration and the awful outcome that is coming every day, every day that we delay in making it clear that we are not going to do sequestration.

So I think this hearing is very appropriate. I thank the chairman for having it. I look forward to the testimony and the discussion.

STATEMENT OF ROBERT J. STEVENS

CHAIRMAN AND CHIEF EXECUTIVE OFFICER

LOCKHEED MARTIN CORPORATION

BEFORE THE HOUSE ARMED SERVICES COMMITTEE

JULY 18, 2012

Mr. Chairman, Ranking Member Smith and Members of the Committee:

On behalf of the 120,000 men and women of Lockheed Martin that I am so very privileged to represent, thank you for the opportunity to share our views on the impacts of sequestration. We strongly believe this represents the single greatest challenge faced by our company and our industry.

We understand the fiscal pressures our nation faces, and we are 3 years into an aggressive effort to reduce costs and better align ourselves to these budget realities. We have reduced our overhead, cut capital expenses, curtailed research and development, consolidated facilities, and engaged in very painful but necessary reductions in personnel across our company. And we'll continue to do more, because we understand the need to be more affordable, more efficient, and more effective.

To illustrate this commitment, over the past three years alone, we have reduced costs by billions of dollars. We've removed a million and a half square feet from our facilities' footprint, and we will reduce another 2.9 million square feet before the end of 2014. Most painfully, today our workforce is 18 percent smaller than it was just three years ago. That means we have 26,000 fewer employees today, and the pace of our hiring has slowed considerably.

We know that program execution is critical to delivering affordable products and services to our customers ... and we stay focused on that priority every day, because that's how we deliver value to our customers which enables us to return value to our shareholders.

Yet, our ability to continue this orderly process of reducing cost while continuing delivering to our customers the best technology and security capabilities in the world is under direct jeopardy by the arbitrary and uncertain consequences of budget sequestration. Despite assurances by some that sequestration is not likely to happen, it is the law of the land and we have no choice but to do our best in planning for its execution. Accordingly, if sequestration occurs in January of next year, it will result in cuts of about half a trillion dollars each in defense and non-defense accounts over the next nine years. For defense, that's an additional half trillion dollars beyond the Budget Control Act commitments already in place to reduce defense by $487 billion over 10 years beginning this year.

Secretary of Defense Panetta has spoken in the strongest possible terms against sequestration. He said this process will have catastrophic consequences for our national defense and called it a "meat axe". It is. By its very nature, the sequestration process would occur independent of any correlation with strategy, force structure, technology needs or operational reality.

My purpose here today is not to attempt to speak for our government customers. But we certainly closely listen to them as to what they need and why. We know they invest a considerable amount of time examining the global security environment, the technologies and capabilities they will need, and how that flows into recapitalization programs.

In the new national security strategy, the President and the Secretary of Defense have spoken extensively about those requirements. And sequestration doesn't align with any of them. That is one of our great concerns about sequestration. It's not aligned with the national security strategy. It's not aligned with technology evolution. It's not aligned with mission areas.

From an industry perspective, because of the specter of sequestration, the near-term horizon is completely obscured by a fog of uncertainty. With just 167 days remaining until it is triggered, we have little insight as to how sequestration will be implemented ... no insight into which programs will be curtailed, which sites will be closed, which technologies will be discontinued, or which contracts will be reformed. Nor do we know which suppliers – particularly our small business participants, who are so vital to our supply chain – will be shut down or crippled. And most tragically, we can't reliably estimate how many people will be affected. How many dedicated employees are going to lose their jobs? How many family lives are going to be disrupted?

Some may consider it flattering to believe that our industry is so robust and so durable that it could absorb the impact of sequestration without breaking stride. But this is fiction. The impact on industry would be devastating, with a significant disruption to ongoing programs and initiatives, leading to facility closures and personnel reductions that would significantly disrupt advanced manufacturing operations, erode engineering expertise, and accelerate the loss of skills and knowledge. It would also directly undermine a key provision of the new national security strategy, which is to preserve the industrial base, not dismantle it. We fear our industry – which is a crown jewel of the American economy -- will suffer a loss of learning, a depletion of talent, and erosion in quality.

In fact, the very prospect of sequestration is already having a chilling effect on the industry. Our ability to hire the best and brightest is being hurt. We're not making as many discretionary investments. We're not leaning forward. We're reducing our training programs. All because of the uncertainty associated with sequestration's sudden and arbitrary additional cuts in next year's defense budget. It's a huge disruption to our businesses.

Beyond the defense industry, the broader consequences of sequestration, in my opinion, are also not well understood. Contrary to the popular perception, sequestration does not only affect defense accounts. It affects non-defense discretionary accounts as well. And since most of those departments and agencies don't have substantial capital acquisition accounts like the Department of Defense, that means these cuts are likely to fall more heavily on the "people accounts" through significant unpaid furloughs and personnel reductions. This will constrain agencies from providing essential support and services, and severely hurt their ability to properly fulfill their missions.

Unless this law is changed, we're probably going to see a reduction in the number of FBI agents that are on the job, the number of Border Patrol officers who are available, the number of people who process social security claims, the number of air traffic controllers, Coast Guardsmen, TSA agents, and so many more people whose jobs will be cutback. These are very real, direct implications of sequestration that many people don't fully appreciate. Taken together, we agree with the emerging assessment that sequestration would have extremely adverse impacts on our U.S. economy at a critical time.

In terms of how sequestration will actually be implemented, what we know are the basic facts on when it is supposed to take place and the aggregate figures involved. Beyond that knowledge, we don't have authoritative guidance on how sequestration will be implemented or the mechanics of this process. There are many important implementation questions yet to be answered that will affect significantly how the sequestration process unfolds.

We do know, however, that we have responsibilities under the Worker Adjustment and Retraining Notification Act – the WARN Act – that require us to notify workers in advance of plant closings or significant layoffs. Under the law, we must give affected employees 60 days' notice in most states and 90 days' notice in New York.

That establishes a framework where we're compelled to start talking to our employees and our 40,000 suppliers, who want to know, "am I going to have a job in January," and "am I going to have a contract in January?"

And the answer from us today is we're not clear about that. We know it's the law to notify many of them in advance, and we know we'll comply with the law. Our best estimate at this point is that defense sequestration is likely to result in about a 10 percent, across-the-board reduction, at the program, project and activity level for most accounts, which means it could be peanut butter spread set of cuts across most of our contracts. We have seen higher estimates and lower estimates depending on how the Administration chooses to implement the Act. But as responsible business leaders we must do the best we can to prepare for this coming reduction. The law, prudence, good corporate governance, and our integrity require that of us.

But without additional guidance on how or when cuts will be implemented, the modeling that we're undertaking lacks clarity in many cases. Based on the limited information available to us and taking into account the allocation of our business among DOD, other U.S. Government and commercial work that will not likely be impacted, a very rough "seat of the pants" estimate is that we might be required to lay off about 10,000 employees. This number is derived by assuming a 10% across-the-board cut in the DOD budget and an 8% across-the-board cut in non-DOD governmental budgets and reflects the fact that approximately 60% of our business is with the DOD and approximately 20% is with non-DOD governmental entities.

But which 10,000? And when? That is difficult to determine without additional guidance from the Government that allows us to narrow the potential

impacts. We don't know with much precision yet which lines of business, which sites, which contracts, which programs, or which technologies would be affected. But when we do know the details, it is in the Government's interest and frankly our employees' interest that we be prepared to move out immediately and without delay. Since these reductions involve a defined dollar amount for the fiscal year, every day or week of delay in making necessary cost reductions can mean even deeper cuts might be required later in the fiscal year, or production costs will be higher than necessary and there will likely be a dispute as to who will pay for these costs. So our judgment is that we need to be ready to act as closely as possible to "day one" of the Act.

One thing we are reasonably certain about is that reductions of this magnitude are likely to trigger the law – the WARN Act – requiring 60 days or more advanced notification in certain locations before workers can be laid off. But since we don't exactly who will be affected by layoffs, or whether any plant closings will be necessary absent legal or contractual relief, our best judgment is that we may have to notify a substantially higher number of our employees beginning late in the third quarter of this year that they may not have a job if sequestration takes place. We do not look forward to making those notifications. But we have a legal and ethical obligation to tell our employees what we know and what we can share. We'd very much prefer to give them more clarity and more details because they have a right – the law gives them that right – to know that their jobs are potentially at risk.

We may also conditionally notify our suppliers that the contracts we have with them may or may not be impacted by sequestration. Our suppliers are already asking how they should price their work. If they're bidding a job with us and the job goes on for three years in the future and that starts in 2013, should we include the consequences of sequestration to our cost structure in that bid, or should we not? Or should we propose a re-opener provision? It's very murky right now, and we don't think there's going to be uniformity across the industrial base until we get much more refined guidance about how sequestration would be precisely implemented.

Throughout our supply chain, many of our suppliers, through our drive for affordability and alignment with Pentagon expectations, have worked to lower their costs and provide the most affordable prices for our high-technology products. They've done that with an expectation within reasonable boundaries of what the future business environment will look like. If sequestration occurs in January, the expectations upon which that cost and pricing structure have been built will be off the table.

Another question will be, how will the contracts be modified? And when we have a modification of our contracts, are we going to re-phase and reschedule, in our case, up to 40,000 suppliers? Our sense is, those 40,000 companies will assert that is a business disruption and we are going to make a claim for the adverse cost impact of the disruption in that business. This has happened before, even when individual contracts are modified. And then we'll be compelled to assemble this portfolio of requests for equitable adjustments or claims and pass that along, as the prime contractor to our government customers.

We have no guidance on how that number of requests for equitable adjustments and claims will be managed, so it's just not clear to us, and more importantly, it's not clear to our small-business suppliers. That really puts them under an enormous amount of pressure and for some, will put their businesses at risk.

If sequestration happens, we will comply with the law respectfully and as ably as we can. But if sequestration is going to happen, the sooner we get clarifying and implementing guidance, the better.

For the reasons outlined here, we firmly believe that sequestration is wrong for the country, wrong for the industry, wrong for the people of Lockheed Martin. In summary, it's the wrong process through which to try to secure greater reductions in spending. We firmly believe we must not let an automatic budget trigger – a default position – become the dominant force for allocating resources and shaping our nation's security posture.

If sequestration happens, it will be a blunt-force trauma to industry and to America. We're concerned that it will tear the fabric of the supply chain, the industrial base and our national security in significant and irreparable ways. The evidence is compelling.

Multiple credible studies point to the potential for the loss of up to two million jobs as result of sequestration. The new national security strategy, according to Secretary Panetta, will be unachievable. We'll lose the ability to gainfully employ adequate numbers of engineers, scientists, and mathematicians just when we need more of each to maintain our competitiveness as a nation. We think about that every day, because the long-term health and vitality of our economy, of our ability to provide for our security and provide for our citizens, is based entirely on our ability to be competitive in the 21st century.

We have had meaningful discussions with the Administration, the Congress, and others, and we will continue to have those conversations in hopes that a comprehensive and integrated solution can be found to avoid this disaster.

I don't profess to have the wisdom or expertise to give counsel to this Committee or to the Congress on the precise path forward to resolve all the fiscal challenges facing our nation. But I have spent decades of my professional working life in the national security arena and I have never been as concerned over the risk to the health of our industry and our government enterprise. Sequestration has been described many times to me as a "doomsday device" as a threat designed to never happen. But the effects of sequestration are being felt, right now, throughout industry. Every month that goes by without a solution is a month of additional uncertainty, deferred investment, lost talent and ultimately increased cost.

Respectfully, I urge you to take action to stop the sequestration process and ask that you do so soon.

The invitation to testify identified Rule 11, clause 2(g)(5), of the Rules of the U.S. House of Representatives for the 112th Congress which requires nongovernmental witnesses appearing before House committees to include in their written statements a curriculum vitae and a disclosure of federal contracts received.

Attached is my bio, along with a summary disclosure of the value of Lockheed Martin contracts received from the U.S. Government during the prior two years. Lockheed Martin is the single largest federal contractor with over 10,000 contracts.

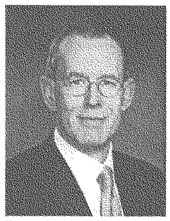
Calendar Year 2011

Department of Defense -	$32,548 Million
NASA -	$1,449 Million
Department of Homeland Security -	$566 Million
Civil/Other US Government/Intelligence -	$5,925 Million
Total U.S. Government Contracts Order Value -	$40,488 Million

Calendar Year 2010

Department of Defense -	$28,869 Million
NASA -	$1,319 Million
Department of Homeland Security -	$488 Million
Civil/Other US Government/Intelligence -	$7,615 Million
Total U.S. Government Contracts Order Value -	$38,291 Million

LOCKHEED MARTIN



Robert J. Stevens
Chairman and Chief Executive Officer
Lockheed Martin Corporation

Robert J. Stevens serves as Chairman and Chief Executive Officer of Lockheed Martin. He has held a variety of increasingly responsible executive positions with the Corporation, including President and Chief Operating Officer, Chief Financial Officer, and head of Strategic Planning through a career that has included experience in program management, finance, manufacturing, and operations.

Mr. Stevens is a Fellow of the American Astronautical Society, the American Institute of Aeronautics and Astronautics (AIAA), the Royal Aeronautical Society, and the International Academy of Astronautics. In addition, in May 2012, AIAA named Mr. Stevens an Honorary Fellow, its highest honor. He serves on the International Advisory Boards of the Atlantic Council and the British-American Business Council and also serves on the Executive Committee of the Aerospace Industries Association's Board of Governors. He is a member of the Council on Foreign Relations, Lead Director of the Monsanto Company, and a member of the Board of Directors of the Congressional Medal of Honor Foundation. Mr. Stevens served on President George W. Bush's Commission to Examine the Future of the United States Aerospace Industry, and in January 2012, he was appointed by President Barack Obama to the Advisory Committee for Trade Policy and Negotiations.

Born in McKeesport, Pennsylvania, Mr. Stevens is a summa cum laude graduate of Slippery Rock University, from which he received the Distinguished Alumni Award. He earned a master's degree in engineering and management from the Polytechnic University of New York and, with a Fairchild Fellowship, earned a master's degree in business from Columbia University. He is a graduate of the Department of Defense Systems Management College Program Management course and also served in the United States Marine Corps. He has been recognized by the National Management Association as Executive of the Year, by Government Computer News as the Industry Executive of the Year, by the Partnership for Public Service with the Private Sector Council Leadership Award, and by the Marine Corps Scholarship Foundation with the Globe and Anchor Award. In 2010, he received the Marine Corps Heritage Foundation's inaugural LeJeune Recognition for Exemplary Leadership, and in 2011 he was recognized by the National Defense Industrial Association with the James Forrestal Industry Leadership Award and inducted into the Washington Business Hall of Fame.

May 2012

DISCLOSURE FORM FOR WITNESSES
CONCERNING FEDERAL CONTRACT AND GRANT INFORMATION

INSTRUCTION TO WITNESSES: Rule 11, clause 2(g)(5), of the Rules of the U.S. House of Representatives for the 112th Congress requires nongovernmental witnesses appearing before House committees to include in their written statements a curriculum vitae and a disclosure of the amount and source of any federal contracts or grants (including subcontracts and subgrants) received during the current and two previous fiscal years either by the witness or by an entity represented by the witness. This form is intended to assist witnesses appearing before the House Armed Services Committee in complying with the House rule.

Witness name: **Robert J. Stevens**

Capacity in which appearing: (check one)

___ Individual

_X_ Representative

If appearing in a representative capacity, name of the company, association or other entity being represented:______________________________

FISCAL YEAR 2011

federal grant(s) / contracts	federal agency	dollar value	subject(s) of contract or grant
SEE ATTACHED			

FISCAL YEAR 2010

federal grant(s) / contracts	federal agency	dollar value	subject(s) of contract or grant
SEE ATTACHED			

FISCAL YEAR 2009

Federal grant(s) / contracts	federal agency	dollar value	subject(s) of contract or grant
SEE ATTACHED			

Federal Contract Information: If you or the entity you represent before the Committee on Armed Services has contracts (including subcontracts) with the federal government, please provide the following information:

Number of contracts (including subcontracts) with the federal government:

SEE ATTACHED

Current fiscal year (2011):______________________;
Fiscal year 2010:______________________;
Fiscal year 2009:______________________.

Federal agencies with which federal contracts are held:

Current fiscal year (2011):______________________;
Fiscal year 2010:______________________;
Fiscal year 2009:______________________.

List of subjects of federal contract(s) (for example, ship construction, aircraft parts manufacturing, software design, force structure consultant, architecture & engineering services, etc.):

Current fiscal year (2011):______________________;
Fiscal year 2010:______________________;
Fiscal year 2009:______________________.

Aggregate dollar value of federal contracts held:

Current fiscal year (2011):______________________;
Fiscal year 2010:______________________;
Fiscal year 2009:______________________.

Federal Grant Information: If you or the entity you represent before the Committee on Armed Services has grants (including subgrants) with the federal government, please provide the following information:

SEE ATTACHED

Number of grants (including subgrants) with the federal government:

Current fiscal year (2011):______________________;
Fiscal year 2010:______________________;
Fiscal year 2009:______________________.

Federal agencies with which federal grants are held:

Current fiscal year (2011):______________________;
Fiscal year 2010:______________________;
Fiscal year 2009:______________________.

List of subjects of federal grants(s) (for example, materials research, sociological study, software design, etc.):

Current fiscal year (2011):______________________;
Fiscal year 2010:______________________;
Fiscal year 2009:______________________.

Aggregate dollar value of federal grants held:

Current fiscal year (2011):______________________;
Fiscal year 2010:______________________;
Fiscal year 2009:______________________.

Calendar Year 2011

Department of Defense -	$32,548 Million
NASA -	$1,449 Million
Department of Homeland Security -	$566 Million
Civil/Other US Government/Intelligence -	$5,925 Million
Total U.S. Government Contracts Order Value -	$40,488 Million

Calendar Year 2010

Department of Defense -	$28,869 Million
NASA -	$1,319 Million
Department of Homeland Security -	$488 Million
Civil/Other US Government/Intelligence -	$7,615 Million
Total U.S. Government Contracts Order Value -	$38,291 Million

Congressional Testimony

Before the House Armed Services Committee

(as presented for the record)

The Impact of Sequestration on the U.S. Aerospace and Defense Industry

By the Honorable Sean O'Keefe

Chairman and CEO, EADS North America, and

Chairman, National Defense Industrial Association

July 18, 2012

Mr. Chairman, Ranking Member Smith and distinguished members of the Committee. Thank you for the invitation to be with you today, and to join my colleagues in the aerospace and defense industry.

My prior public service experience gives me some insight into the challenges which have prompted you to call this hearing. However, it is in my current capacity as Chairman and CEO of EADS North America and Chairman of the National Defense Industrial Association, representing nearly 90,000 corporate and individual members, that I speak with you today.

This hearing is particularly well timed. And I express my appreciation to you, Mr. Chairman, for your foresight and tenacity in tirelessly drawing attention to the impending "perfect fiscal storm" of sequestration.

Many in Washington believe that the disastrous impact of sequestration is a distant threat since it would not be implemented until January 2013. But as you, and your fellow committee members know well, the fiscal challenges of sequestration are already upon us. Industry shares your concerns—and our experience to date validates your alarm.

The question is not how we got in this position, but rather how we steer through the storm. As your defense industrial partners, we recognize that reconciling federal spending to revenues is absolutely essential in securing lasting economic stability and national security. But we fear that the government's reluctance to make difficult choices and apply a well-aimed fiscal razor will mean that the federal budget, and particularly defense, will get the equivalent of a shave with a chain saw.

Cuts will be made – but they will be imprecise and without regard to priority. The mechanistic implementation formula as prescribed in law treats the contract for protective armor and the cost to cut the grass on military bases to be of equal priority. These cuts, and the process used to derive them, also will have a significantly negative impact on hundreds of thousands of men and women in uniform, and millions of employees and their families that our industry supports.

Industry is very familiar with cyclical down-turns and the need to periodically adjust defense spending to meet new fiscal realities. But unlike the "peace dividends" of the past, the next round of cuts will not be driven by positive, external strategic factors like the collapse of the Soviet Union, the fall of the Berlin Wall, or the end of the Vietnam War. Rather, the impending sequestration cuts, if they are allowed to happen, will be driven by our collective inability to make hard choices. In effect, this is a self-inflicted wound.

Every echelon of the defense industry will be impacted. Let me speak specifically for EADS, and its U.S. subsidiary, EADS North America. As you know, EADS is one of the largest aerospace and defense companies in the world with brands you recognize, including Airbus, Eurocopter, Astrium and Cassidian.

As what some refer to as a "non-heritage" defense company, EADS North America has been on a significant growth path in the U.S.: investing in facilities, creating jobs, delivering systems like the UH-72A Lakota and competing for programs like the Air Force refueling tanker, all of which has brought positive return to the American taxpayer and warfighter. In fact just two weeks ago we announced the establishment of an Airbus aircraft manufacturing center in Mobile, Alabama. This $600 million investment will create several thousand construction jobs in the near term, and sustain nearly 1,000 aerospace jobs in the greater Mobile community alone.

In addition to our direct investment and employment, the United States is the largest supplier nation in the world to our corporation. Last year EADS purchased nearly $15 billion in goods and services from American aerospace suppliers. That's more than any other company outside the US. In fact that's more than any country in the world. And our sourcing activities support approximately 250,000 American jobs.

The threat of sequestration raises a number of troubling issues for EADS. All are important, but two jump out:

1. I have already advised the Governors and Congressional delegations in the states and districts where we operate that we are wrestling with how to meet our obligations under the WARN Act. In the absence of definitive guidance from DoD, OMB and the Defense Contract Management Agency, we feel compelled to act in the spirit of this law and in all likelihood will issue WARN notices to those employees engaged in ongoing federal contract activities. It's not something we want to do. But it appears the law requires us to do it. Clearly the intent of the Act is to provide employees with time to prepare for known events that may impact their employment. Without a doubt sequestration could be just that kind of event.
2. We are very concerned about the affect of sequestration on our extended supplier base. EADS buys in the U.S. because of the high quality, innovation

and reliability of our vast American supplier network. We believe sequestration will negatively impact many of these suppliers, including driving some out of the market. Again, in the absence of guidance, we and our suppliers are left to wonder how and if our businesses will be disrupted as a result of sequestration, not only in the defense sector, but commercial activity as well.

The most vulnerable of these aerospace and defense suppliers are the vast number of small to mid-cap businesses that sustain millions of jobs, drive technology and create the innovation that is the hallmark of American aerospace. While larger companies have the capacity to more successfully weather the impending fiscal storm, small businesses do not.

In preparing for my testimony today, the National Defense Industrial Association reached out to a number of our small business members.

Their responses were both illuminating and alarming.

Small business suppliers tell us that they are already preparing to trim payrolls, that they are not creating new jobs because of the anticipation of sequestration and that many are gearing up to leave the federal and defense market space all together.

Here are three examples of our member companies:

1. An eight year old small electronics contract manufacturer, with less than 20 employees and revenues of less than $10M. A five year contract for electronic parts was pulled back by Tier 1 supplier, because of uncertainty of whether that

particular program would survive post-sequestration. The small supplier had a cash flow crunch, forcing them to delay new hires and even downsize slightly.

2. A three year old aerospace parts manufacturer, with less than 25 employees and revenues less than $10M. A two year contract for aircraft parts was placed on hold, because the platform was one of those targeted for cuts for Budget Control Act and sequestration. The small manufacturer pulled back on a proposed capital investment and new hires, instead using the cash to cover payroll while looking for new business.

3. A six year old aerospace components manufacturer, with less than 30 employees and revenues of less than $15M. A three year contract for aircraft components was suspended, because several of the platforms were mentioned as potential sequestration targets. The company shelved a facility expansion plan, put a hold on new hires, and had several employees switch to reduced work hours until the business outlook was more definitive.

These company experiences are particularly disappointing because over the years this Committee has led the effort to bring small businesses into the DoD supply chain. I fear those successes will be significantly curtailed or reversed.

But even in this difficult fiscal environment, I believe there are opportunities and paths we could follow that would produce positive results, leading to more efficient government management of the defense acquisition process, and an equally more efficient industry supporting it.

The first steps in my view would be to set a realistic Defense budget reduction target, repeal the across-the-board sequester, and delegate the creation of a spending reduction plan to the Secretary of Defense. Working with a select group of Congressional national security leaders, the Secretary could produce a difficult, but acceptable, plan to meet necessary budget targets.

Such a plan shouldn't be restricted to just program choices. Rather, it must include an opportunity for "economic stimulus" by removing some of the self-imposed administrative impediments that blunt market activity. The administration has done a decent job of starting to make export control rules less rigid. But more can be done to truncate prolonged reviews by multiple agencies that discourage U.S. industry from seeking overseas markets. At the same time, Congress can help by streamlining current export control laws that negatively impact trade.

This same approach can be applied to domestic programs. The cost of doing business with the government can add more than 20% to the price of goods. This is especially true when it comes to defense. The extensive array of regulations that push up prices and drive out potential competitors could be suspended by executive order. In the mid-1990s, the Clinton administration pursued a "procurement holiday" to reduce defense spending. Introducing a "regulatory holiday" would create immediate and long-term economic benefits.

Under such a regulatory holiday as recommended by the Defense Business Board, all administrative rules and regulations would be suspended, unless reinstated by the Secretary of Defense. I believe we would see broader competition, greater savings and retention of second- and third-tier suppliers—even in the face of budget reductions.

There also are regulatory challenges that could be addressed that impact companies like EADS North America and our ability to offer competitive choices in the U.S. market. For example, many of the new aviation contracts with DoD require FAA certification. While the European Aviation Safety Agency (EASA) standards are considered comparable to the FAA certification standards, there is no DoD process for considering and accepting EASA certified aviation standards. Therefore, the financial and schedule burdens required to convert these comparable aviation standards in order to compete for DoD programs must ultimately be priced into our offers, which increases the cost of doing business with the U.S. government.

Most immediately, the administration must communicate today its sequestration implementation plan to the public, our armed forces and to industry. The current uncertainty has effectively put sequestration and its consequences in motion. In the absence of any guidance, industry is already holding back investments, questioning the fairness of ongoing competitions, doubting the viability of existing contracts and starting to trim capacity.

During my government service I experienced first-hand the challenges of budget reductions. Program managers, analysts and budget officers will burn the midnight oil trying to shelter programs, missions and capabilities from the looming disaster.

Without guidance, I fear their cuts will be random, inwardly focused and not always driven by national security priorities. In addition, the Department will potentially be overwhelmed with renegotiating contracts, dealing with unobligated balances from previous years and addressing unexpected Nunn-McCurdy breaches. Savings for businesses and the government under multi-year procurement contracts could be lost, fixed-price contracts will almost certainly be challenged, as well as many others terminated due to unplanned costs and liabilities.

This is a recipe for endless argument, litigation and gridlock. And it will ultimately drive up costs to the point that they exceed the savings that sequestration was enacted to produce.

But lost in the debate about this budget reduction mechanism is the larger impact of this action. This is not about the bottom line, the corporate balance sheet, share prices and market analyst reports. And it is less about preserving the industrial base, maintaining production capacity, or impacting competitiveness. The impact is on our national security. It's about diminishing the ability of our men and women in uniform who have volunteered to defend us and represent our national interests around the globe. All that we are discussing today is about industry's ability to support them. In the greater context, this is but one element of a wider range of dangerous consequences that this fiscal mechanism will create to erode our national security.

Mr. Chairman and members of the Committee, we in the industry stand ready to support your important efforts. We are prepared to make difficult decisions. But we need guidance, direction and rationality in the process. And we need it now.

Thank you for the opportunity to address the Committee. I look forward to your questions.

EADS
NORTH AMERICA

Sean O'Keefe
Chairman and Chief Executive Officer
EADS North America

Sean O'Keefe was appointed CEO of EADS North America in November 2009 and Chairman of the Board in January 2012. His responsibilities include directing EADS activities in the United States, developing strategic partnerships with U.S. companies, and enhancing the participation of EADS in the U.S. marketplace — including the development, growth, and management of large-scale defense acquisition programs.

Globally, EADS is the parent company of some of the most recognized brands in the international aerospace and defense sector, including Airbus, Eurocopter, Ariane Space, Astrium, Eurofighter and MBDA. The company had annual revenues in 2011 of more than $66 billion and employs some 133,000 people worldwide.

Prior to joining EADS North America, Mr. O'Keefe served as a company officer and Vice President of the General Electric Company in the Technology Infrastructure sector, leading the Washington operations of the GE Aviation business. From 2005 to 2008, he served as Chancellor of the Louisiana State University, the chief executive officer, in Baton Rouge, LA.

On four separate occasions O'Keefe served as a presidential appointee. Prior to leading LSU, he served as the tenth Administrator of the National Aeronautics and Space Administration. Mr. O'Keefe joined President George W. Bush's administration on inauguration day as Deputy Assistant to the President and Deputy Director of the Office of Management and Budget until December 2001, when he was appointed NASA Administrator.

Appointed the 69th Secretary of the Navy in July 1992 by President George H. W. Bush, Mr. O'Keefe previously served as Comptroller and Chief Financial Officer of the Department of Defense from 1989. Before joining then-Defense Secretary Dick Cheney's Pentagon management team in these capacities, he served on the United States Senate Committee on Appropriations staff for eight years and was Staff Director of the Defense Appropriations Subcommittee.

His public service began in 1978 upon his selection as a Presidential Management Intern. Mr. O'Keefe earned his Bachelor of Arts from Loyola University in New Orleans in 1977 and his Master of Public Administration from the Maxwell School of Syracuse University in 1978. He is married to Laura McCarthy O'Keefe, and they have three children - Lindsey, Jonathan, and Kevin.

Industry service
Mr. O'Keefe was appointed in November 2011 as Chairman of the National Defense Industrial Association (NDIA) – America's leading industry association promoting the defense industry and national security. Prior to this appointment, he had served as Vice Chairman of the NDIA's Executive Committee.

Academic service and fellowships
From 1996-2001 Mr. O'Keefe was an endowed chair professor at the Syracuse University Maxwell School of Citizenship and Public Affairs. Concurrently he served as the Director of National Security Studies, a partnership of Syracuse University and Johns Hopkins University for delivery of executive education programs. From 1993-1996 he was Professor of Business Administration and Assistant to the Senior Vice President for Research and Dean of the Graduate School at the Pennsylvania State University.

Mr. O'Keefe is a Fellow of the National Academy of Public Administration, a Fellow of the International Academy of Astronautics, and serves on corporate and non-profit boards of directors. During his academic postings, he was a Visiting Scholar at the Wolfson College of the University of Cambridge in the United Kingdom, a member of the Naval Postgraduate School's civil-military relations seminar team, and conducted seminars for the Strategic Studies Group at Oxford University. He was a member of the 1985 Kennedy School of Government program for national security executives at Harvard University.

Awards and authorship
In 1993, President Bush and Secretary Cheney presented Mr. O'Keefe with the Distinguished Public Service Award. He was the 1999 faculty recipient of the Syracuse University Chancellor's Award for Public Service; recipient of the Department of the Navy's Public Service Award in December 2000; and has been awarded five honorary doctorate degrees from several prestigious educational institutions. In 2003 and 2004, he was recognized and honored by the Irish American Magazine as one of the Top 100 Irish Americans and was named among the magazine's "Stars of the South" in 2006.

O'Keefe was named recipient of the Potomac Institute for Policy Studies' 2005 Navigator Award and received the 2005 Honorary Engineer of the Year Award from the Engineer's Council. He was inducted into the Louisiana Political Hall of Fame in January 2007.

He is the author of several journal articles and contributing author of *Keeping the Edge: Managing Defense for the Future,* released in October 2000. In 1998, he co-authored *The Defense Industry in the Post-Cold War Era: Corporate Strategies and Public Policy Perspectives.*

About EADS North America (www.eadsnorthamerica.com)
EADS North America is the North American operation of EADS, a global leader in aerospace, defense and related services. As a leader in all sectors of defense and homeland security, EADS North America and its parent company, EADS, contribute over $11 billion to the U.S. economy annually and support more than 200,000 American jobs through its network of suppliers and services. Operating in 17 states, EADS North America offers a broad array of advanced solutions to its customers in the commercial, homeland security, aerospace and defense markets.

DISCLOSURE FORM FOR WITNESSES
CONCERNING FEDERAL CONTRACT AND GRANT INFORMATION

INSTRUCTION TO WITNESSES: Rule 11, clause 2(g)(5), of the Rules of the U.S. House of Representatives for the 112th Congress requires nongovernmental witnesses appearing before House committees to include in their written statements a curriculum vitae and a disclosure of the amount and source of any federal contracts or grants (including subcontracts and subgrants) received during the current and two previous fiscal years either by the witness or by an entity represented by the witness. This form is intended to assist witnesses appearing before the House Armed Services Committee in complying with the House rule.

Witness name: Sean O'Keefe

Capacity in which appearing: (check one)

___Individual

_X_ Representative

If appearing in a representative capacity, name of the company, association or other entity being represented: EADS North America, Inc.

FISCAL YEAR 2012

federal grant(s) / contracts	federal agency	dollar value	subject(s) of contract or grant
L12P001513	U.S. Army Aviation and Missile Command (subcontract from SES-I)	$947,387.00	AMPS-M (Missile Warning System) Parts
LP120009663	Army (subcontract from Applied Geo Technologies)	$29,856.00	MQM 175 (Aerial Target) A&B Bore Sight Units
LP120009664	Army (subcontract from Applied Geo Technologies)	$29,857.00	MQM 175 (Aerial Target) A&B Bore Sight Units
F00214	contract is through Air Force, customer is DISA (subcontract from Raytheon)	$1,731,692.00	Ectocryp Black engineering services
HM021010D0002	National Geospatial-Intelligence Agency	$213,000.00	TerraSAR-X imagery
G12PD00079	U.S. Geological Survey	$800,000.00	TerraSAR-X imagery
SRT0005	U.S. Navy (subcontract from Lockheed Martin)	$10,022,559.76	TRS-3D radars for Littoral Combat Ship program
HSCG38-11-D-202053	U.S. Coast Guard	$95,680.48	repair of HH-65 electrical components
HSCG38-10-D-	US Coast Guard	$14,536.00	H-65 Sustaining Engineering

2000013			
HSCG38-10-D-2000016	US Coast Guard	$1,585,865.52	Main Rotor Blades repairs
HSCG38-D-202048	US Coast Guard	$85,701.21	HH65C Bearing Spider PLT repairs
N68335-12-P-0228	US Navy	$39,549.11	Yemen FMS CN-235 Preservation
HSCG23-09-D-010004	US Coast Guard	$19,849.27	IDIQ contract for sustaining engineering support for HC-144A fleet
W58RGZ-06-C-0194	US Army	$296,009,226.73	Light Utility Helicopter (option exercise plus mods)
HSCG23-10-C-2DA020	US Coast Guard	$78,507,936.76	HC-144A Production Contract (option exercise)
N66604-12-D-0051	Navy	$2,624,210	RFDACS Spares
N00383-12-D-012P	Navy	$170,094	JETI Spares Mini Stock Point
Multiple purchase orders	Navy, Army, Marine Corp	~$4,800,000	Misc Electronic and Test System Orders

FISCAL YEAR 2011

federal grant(s) / contracts	federal agency	dollar value	subject(s) of contract or grant
L10P004000	U.S. Army, Aviation and Missile Command (subcontract from SES-I)	$14,701,622.00	AMPS-M (Missile Warning System) sensors and parts
P11P000751	U.S. Army, Aviation and Missile Command (subcontract from SES-I)	$145,697.00	AMPS-M (Missile Warning System) parts
L11P002018	U.S. Army, Aviation and Missile Command (subcontract from SES-I)	$23,722.00	AMPS-M (Missile Warning System) dessicant replacement kits
P11009527	Army (subcontract from Applied Geo Technologies)	$14,293.02	MQM 175 (Aerial Target) A/B Cross Plate kits
E81038	contract is through Air Force, customer is DISA (subcontract from Raytheon)	$300,000.00	Ectocryp Black engineering services
HM021010D0002	National Geospatial-Intelligence Agency	$1,691,841.00	TerraSAR-X imagery
SRT0005	U.S. Navy (subcontract from Lockheed Martin)	$10,219,734.77	TRS-3D radars for Littoral Combat Ship program
SPRMM1-11-P-YD75	Defense Logistics Agency	$100,652.00	TRS-3D Power Supply
SPRMM1-11-P-YD76	Defense Logistics	$100,652.00	TRS-3D Power Supply

	Agency		
SPRMM1-11-P-YD77	Defense Logistics Agency	$25,597.00	TRS-3D Modulator Driver
SPRMM1-11-P-YD78	Defense Logistics Agency	$28,816.00	TRS-3D Grid Modulator
SPRMM1-11-P-YD80	Defense Logistics Agency	$29,975.00	TRS-3D Controller Board
SPRMM1-11-P-YD81	Defense Logistics Agency	$38,377.00	TRS-3D Gear Pump Refinex
SPRMM1-11-P-YD82	Defense Logistics Agency	$25,590.00	TRS-3D Double Coupler 50DB
SPRMM1-11-P-YD83	Defense Logistics Agency	$12,371.00	TRS-3D Power Supply
SPRMM1-11-P-YD84	Defense Logistics Agency	$23,154.00	TRS-3D Grid Bias P.S.
HSCG38-11-D-202053	U.S. Coast Guard	$24,500.63	repair of HH-65 electrical components
W9113M-07-D-0006	Army	$31,499,937.32	Aircraft - CN235
HSCG23-10-C-PX001	Coast Guard	$157,647,996.60	Aircraft - CN235
HSCG38-10-D-2000013	US Coast Guard	$1,210,500.55	H-65 Sustaining Engineering
HSCG38-10-D-2000016	US Coast Guard	1,867,763.41	Main Rotor Blades engineering services
HSCG38-D-202048	US Coast Guard	$127,365.41	HH65C Bearing Spider PLT repairs
HSCG23-09-D-010004	US Coast Guard	$1,835.68	IDIQ contract for sustaining engineering support for HC-144A fleet
W58RGZ-06-C-0194	US Army	$375,534,205.38	Light Utility Helicopter (option exercise plus mods)
N68335-11-D-0017	Navy	1,730,600	TPTI
Multiple purchase orders	Navy, Army, Marine Corp	~18,000,000	Misc Electronic and Test System Orders
HSCG23-10-C-2DA020	US Coast Guard	$41,143,476.38	HC-144A Production Contract

FISCAL YEAR 2010

Federal grant(s) / contracts	federal agency	dollar value	subject(s) of contract or grant
AGT-TMO-IDIQ-07-007	Army (subcontract from Applied Geo Technologies)	$858,776.50	launcher and smoke generation equipment for aerial target system
PO00007861	U.S. Army (subcontract from Griffon Aerospace)	$60,000.00	aerial targets scoring system
WS-LP-0369	U.S. Army (subcontract from Kratos Government Solutions)	$53,196.00	DT 45 (Aerial Target) wings

WS-LP-0431	U.S. Army (subcontract from Kratos Government Solutions)	$46,350.00	DT 35 and DT 45 (Aerial Target) parts
W31D4Q-07-00-D-001	U.S. Army (subcontract from Torch Technologies)	$9,660.00	DT 35 and DT 45 (Aerial Target) Instrumented MAST wing tips
HM021010D0002	National Geospatial-Intelligence Agency	$2,002,240.00	TerraSAR-X imagery
G08C90056	U.S. Geological Survey	$13,290.00	TerraSAR-X imagery
HSCG38-10-D-2000013	US Coast Guard	$877,705.46	H-65 Sustaining Engineering
HSCG38-10-D-2000016	US Coast Guard	$527,002.76	Main Rotor Blades engineering services
HSCG38-D-202048	US Coast Guard	$53,145.16	HH65C Bearing Spider PLT repairs
HSCG23-10-C-2DA020	US Coast Guard	$115,980,650.20	HC-144A Production Contract
HSCG23-10-C-P9X001	US Coast Guard	$157,708,922.32	Merida FMS CN-235 Production
PO 7200007857	US Coast Guard (subcontract from Lockheed Martin)	$31,352,968.32	Yemen FMS CN-235 Production
HSCG38-10-C-011010	US Coast Guard	$1,406,151.23	FSR support for HC-144A fleet
W911QX-11-G9002	US Army	$5,915 378.00	SONEX (detection equipment)
HSCG23-09-D-010004	US Coast Guard	$41,474.26	IDIQ contract for sustaining engineering support for HC-144A fleet
W58RGZ-06-C-0194	US Army	$394,196,322.67	Light Utility Helicopter (option exercise plus mods)
N66604-10-C-0531	Navy	$15,656,992	RFDACS
Multiple purchase orders	Navy, Army, Marine Corp	~$22,000,000	Misc Electronic and Test System Orders

Federal Contract Information: If you or the entity you represent before the Committee on Armed Services has contracts (including subcontracts) with the federal government, please provide the following information:

Number of contracts (including subcontracts) with the federal government:

Current fiscal year (2012):__ ~29______________________________;
Fiscal year 2011:__ ~94______________________________________;
Fiscal year 2010:__ ~77______________________________________.

Federal agencies with which federal contracts are held:

Current fiscal year (2012): National Geospatial-Intelligence Agency, U.S. Geological Survey, U.S. Coast Guard, Army, Navy, DISA/Air Force, Marine Corps;
Fiscal year 2011: National Geospatial-Intelligence Agency, U.S. Coast Guard,

Army, Defense Logistics Agency, DISA/Air Force, Navy, Marine Corps;
Fiscal year 2010: National Geospatial-Intelligence Agency, U.S. Geological Survey, U.S. Coast Guard, Army, Marine Corps.

List of subjects of federal contract(s) (for example, ship construction, aircraft parts manufacturing, software design, force structure consultant, architecture & engineering services, etc.):

Current fiscal year (2012): engineering services, aircraft/helicopter parts, missile warning systems, satellite imagery, radar parts, helicopters, ship radars, cryptologic equipment, aircraft, electronic test equipment, engine test equipment, radio distribution equipment;
Fiscal year 2011: engineering services, satellite imagery, aircraft/helicopter parts, missile warning system, certification and testing, radar parts, helicopters, cryptologic equipment, aircraft, electronic test equipment, engine test equipment, radio distribution equipment;
Fiscal year 2010: aerial target launcher, engineering services, aircraft/helicopter parts, satellite imagery, missile warning systems, helicopters, detection equipment, aircraft, electronic test equipment, engine test equipment, radio distribution equipment.

Aggregate dollar value of federal contracts held:

Current fiscal year (2012): ~$397,727,000.84;
Fiscal year 2011: ~$656,270,275.15;
Fiscal year 2010: ~$742,844,846.88.

Federal Grant Information: If you or the entity you represent before the Committee on Armed Services has grants (including subgrants) with the federal government, please provide the following information:

Number of grants (including subgrants) with the federal government:

Current fiscal year (2012):_N/A________________________________;
Fiscal year 2011:___N/A_____________________________________;
Fiscal year 2010:___N/A_____________________________________.

Federal agencies with which federal grants are held:

Current fiscal year (2012):__N/A________________________________;
Fiscal year 2011:__N/A_____________________________________;
Fiscal year 2010:__N/A_____________________________________.

List of subjects of federal grants(s) (for example, materials research, sociological study, software design, etc.):

Current fiscal year (2012):____N/A______________________________;
Fiscal year 2011:__N/A_____________________________________;
Fiscal year 2010:__N/A_____________________________________.

Aggregate dollar value of federal grants held:

Current fiscal year (2012):_____N/A_____________________________;
Fiscal year 2011:_____N/A__________________________________;
Fiscal year 2010:_____N/A__________________________________.

Testimony of Mr. David Hess
President, Pratt & Whitney
Before the House Armed Services Committee
On Sequestration Implementation and Options and the Effects on National Defense
July 18, 2012

Chairman McKeon, Ranking Member Smith, Members of the Committee, I appreciate the opportunity to testify before you today regarding the serious matter of the potential for sequestration and the implications for the defense industry. As you know, I wear two hats currently – one as the President of a $13 billion company that employs more than 36,000 employees worldwide, and another as Chairman of the Aerospace Industries Association (AIA), which represents over 300 aerospace companies in the United States. I commend the committee for assembling such a fine group of witnesses to provide diverse answers based upon the different challenges each of us face in the coming months.

As Chairman of AIA, it has been my privilege to visit Capitol Hill on numerous occasions to outline what we see with regard to sequestration – the potential to affect over one million highly skilled, highly compensated aerospace and defense related jobs. AIA's "Second to None" advocacy campaign has been spreading throughout the country with grassroots rallies highlighting the importance of fixing sequestration versus suffering its consequences.

As an industry, we are already seeing the impacts of potential sequestration budget cuts today. Companies are limiting hiring and halting investments - largely due to the uncertainty about how sequestration cuts would be applied. At our sister division, Sikorsky, the leadership has already indicated that in this environment, if they had to choose right now how to invest internal R&D dollars between commercial and defense programs, they would choose commercial programs because of the uncertainty with the defense budget. Equally concerning are the impacts of sequestration on the domestic side as it relates to homeland security, border security, air traffic control, TSA and other agencies. The sequestration threats facing other government agencies, contracts, and workforce affect our member companies' ability to do business safely and effectively. In the near term, some clarity from the Office of Management and Budget about how sequestration cuts would be implemented would be helpful in avoiding some of these impacts.

Regardless of how the cuts are implemented, the consequences for the industry will be dire. The Defense Industrial Base Task Force, commissioned by Secretary Panetta, has reported that sequestration level cuts would result in the closure of production lines, the layoff of skilled workers, severe curtailment of research and development investments, and a reduced ability to respond to emergent needs of the U.S. military.

However, today I am here as the President of Pratt & Whitney, to offer my view on how sequestration will affect us directly and share with you how the effects Secretary Panetta mentioned are becoming reality.

At Pratt & Whitney, we build jet engines for both the commercial and military marketplace. As you know, our military base market consists primarily of the F135 engine for the F-35. While we are also proud to have our engine chosen to power the next-generation KC-46 aerial refueling tanker for the U.S. Air Force, these engines will not affect our production business until 2016 at the earliest. With the end of the production run of the F-22 engine this year, and the end of the production of the C-17 engine next, the F135 engine is our future for our military business.

Already, the decline in defense spending is negatively affecting the F-35 production ramp and subsequently affecting our engine production. As you know, the $487B in defense budget cuts already announced has pushed out 179 F-35 aircraft between 2012 and 2020. Original projections from just a few years ago had us building well over 100 F135 engines per year by now. This year, we will build just over 50 F135 engines. Next year, our F135 production will actually decrease, and if sequestration were to take effect, that number would decline significantly.

It's not just new engine deliveries that are impacted at Pratt &Whitney. Spares parts are key to keeping our manufacturing base healthy and sustainable. But as a result of the announced [$487B] DoD budget cuts, flight hours have already been cut back and sequestration could result in still further reductions. This undercuts demand for our spare parts and overhaul work.

For my company, this situation poses both a workforce and a supply base problem. As the F-22 program winds down, I am currently transitioning many of those workers to F135 production – but this is extremely difficult given the near-term production decline I described earlier. With sequestration, it will be even more difficult to retain those highly skilled employees. Quite simply, my workforce is aging, specialized, and highly compensated. If and when we do ramp back up production, the learning curve for new employees is steep and that will affect production, quality, and training – all of which add time and cost.

Pratt & Whitney is somewhat unique, because from a production standpoint a jet engine is a jet engine, whether it goes on a military aircraft or a commercial aircraft. This allows us to absorb some disruptions better than small companies in the supply base. For a short time, I may be able to move employees between military and commercial programs – assuming I have increasing demand in the commercial area. I can, if forced to, take some risk if there is to be a reward at the end of the day. But this is putting the proverbial band-aid on a bullet wound.

In terms of our supply base, they too are currently struggling with volume. Many of them are small businesses making specialized parts for military engines that simply cannot survive another production decline or disruption. We continue to hear from our suppliers that if further cuts take place they would be forced to lay people off, curtail investment and pursue other business.

One large supplier has told us frankly that they don't believe that the DOD will ever procure the number of engines in the current program forecasts. This uncertainty makes suppliers less willing to enter into long-term agreements with us and drives up our costs today.

If sequestration were to go into effect, no amount of juggling is going to preserve my workforce or help me maintain my supply base. A step down in the current production ramp for the F-35 means some of my people will lose their jobs. It also means reduced volume for suppliers and that means costs go up. More importantly, it puts a good program in a very tenuous position – a program that we cannot afford to lose.

To reiterate Mr. Chairman, we at Pratt & Whitney are better able than smaller companies to deal with short-term implications of sequestration. But make no mistake, it is dangerous for the warfighter, for us as a business, for the supply chain companies and for us as a nation. Again, I appreciate your perseverance on this important topic and for your allowing me to be here today.

Pratt & Whitney
A United Technologies Company

David P. Hess
President, Pratt & Whitney

David P. Hess became president of Pratt & Whitney, a division of United Technologies Corp. (NYSE:UTX), on Jan. 1, 2009. He is responsible for the company's global operations in the design, manufacture and service of aircraft engines, space propulsion systems and industrial power systems. With an installed aero engine base of 68,000, an unmatched global service network and strong partnerships in manufacturing and servicing engines, the company had revenues of $13.4 billion in 2011.

Under his leadership, Pratt & Whitney is manufacturing engines with exclusive PurePower® Geared Turbofan™ technology for Airbus, Bombardier, Irkut and Mitsubishi and is the sole provider of the F135 engine for the Lockheed Martin F-35 Lightning II fighter. Hess joined Pratt & Whitney after four years as president of Hamilton Sundstrand, the United Technologies division where he began his professional career in 1979.

He serves as chairman of the Aerospace Industries Association Board of Governors and is a vice chairman of the New England Chapter of the American Cancer Society's CEOs Against Cancer initiative. He also serves on the board of trustees of the National World War II Museum. He is vice chairman of the board of directors for The Discovery Center, a nonprofit group founded by Paul Newman and Joanne Woodward that works with elementary and middle-school students from Connecticut's urban centers and suburban communities on diversity and team-building.

Hess holds a bachelor's degree in physics from Hamilton College and a bachelor's and master's degree in electrical engineering from Rensselaer Polytechnic Institute. He was awarded an MIT Sloan Fellowship in 1989 and earned a master's degree in management in 1990.

February 2012

DISCLOSURE FORM FOR WITNESSES
CONCERNING FEDERAL CONTRACT AND GRANT INFORMATION

INSTRUCTION TO WITNESSES: Rule 11, clause 2(g)(5), of the Rules of the U.S. House of Representatives for the 112th Congress requires nongovernmental witnesses appearing before House committees to include in their written statements a curriculum vitae and a disclosure of the amount and source of any federal contracts or grants (including subcontracts and subgrants) received during the current and two previous fiscal years either by the witness or by an entity represented by the witness. This form is intended to assist witnesses appearing before the House Armed Services Committee in complying with the House rule.

Witness name: David P. Hess

Capacity in which appearing: (check one)

___Individual

X_Representative

If appearing in a representative capacity, name of the company, association or other entity being represented:_Pratt & Whitney, a division of United Technologies Corporation

Individual Contracts and grants for Pratt & Whitney (a division of United Technologies Corporation), are too numerous to list individually. Pratt & Whitney's sales to the U.S. Government in 2009 were $3.66B, representing 30% of total sales. Pratt & Whitney's sales to the U.S. Government in 2010 were $3.60B, representing 38% of total sales. Pratt & Whitney's sales to the U.S. Government in 2011 were $3.32B, representing 25% of total sales.

TESTIMONY OF DELLA WILLIAMS, PRESIDENT AND CEO, WILLIAMS PYRO

BEFORE THE

HOUSE ARMED SERVICES COMMITTEE

JULY 18, 2012

Chairman McKeon, Ranking Member Smith and members of the Committee, thank you for the opportunity to testify at the July 18, 2012, House Armed Services Committee hearing, "Sequestration Implementation Options and the Effects on National Defense: Industry Perspectives."

My name is Della Williams, and I am President and CEO of Williams-Pyro in Fort Worth, Texas. **Williams-Pyro is a woman-owned, small business that designs and manufactures innovative products, including custom cables, connectors, adapters, automated test equipment, and intelligent power management systems. We currently have 89 employees who continue to amaze me every day; and I've been here since Day 1.**

As a manufacturer and part of the defense supply chain, I very much appreciate your focus on the defense industry and the impact of the impending cuts in defense spending set to begin on January 1, 2013. While I wish I were here under better circumstances, the impending threat of these wholesale budget cuts is of deep concern to me. My goal today is to put a face and a name to what is rather cavalierly discussed in the press as "sequestration."

Most people would associate defense cuts with the big Tier I defense contractors, which are represented by several of my colleague here today. Supporting every one of these large integrators on dozens of programs, are thousands of Tier II and Tier III suppliers – most small and medium-sized businesses– who design and manufacture what seems like small parts.

All of those parts combined make up systems that seek out and destroy multiple targets, aircraft that soar to their targets or evacuate civilians in a disaster, and ships that knife through the water to intercede in a conflict or deliver humanitarian aid. Moreover, the defense supply chain companies collectively employ millions of hard-working people who each support spouses and children and communities.

So these cuts will not just impact a few large companies. These cuts will flow down the supply chain and through the broader economy. They will impact companies, like mine and threaten the jobs of thousands of skilled workers. In fact, a report released last month by the National Association of Manufacturers concludes that by 2014, the cuts in defense spending enacted last year combined with the cuts set for January 1, 2013, will result in the loss of more than one million jobs, increasing the unemployment rate by almost one percent.

If small business—and I would submit even further, manufacturing— is an engine for economic growth, why are we making decisions that will inevitably stall that engine?

My company was founded in April 1963—in fact, we celebrate 50 years in business next year. That is a huge milestone for a small, woman-owned company. During that time, our company has proven to be a very innovative organization building our business on designing and manufacturing forward-thinking weapons systems test equipment for the Air Force, Navy, Army and the Marine Corps. Our products have improved the safety of flight line maintainers, reduced aircraft downtime, and boosted the buying power of the defense procurement dollar.

The budgetary issues the federal government is facing are the same ones that I, as a small manufacturer and a taxpayer, deal with every day in my own business. I am proud to say that Williams Pyro has won many awards over the years including the much-coveted Tibbetts Award for Innovation, Small Business of the Year award from Lockheed Martin Global Training & Logistics in 2008 and 2011, Boeing Preferred Supplier, and numerous awards for our 100 percent quality and on-time delivery from the Defense Logistics Agency. Williams Pyro has won these awards by meeting the challenges presented to us.

Analysts say the defense industry is faced with several choices, either exit the market, double down on defense by buying competitors or "weather the storm." At Williams Pyro however, we have chosen to invest in product development. I'd like to share a recent example of our innovation.

A few years ago, my Chief Engineer and I were observing one of our testers at a First Article Test at Nellis AFB and a piece of Government Furnished Equipment was brought out to perform the testing, a unit referred to as the Beer Can. Another manufacturer had developed this device in 1969. Technology of the 1960's was very different from today and included rabbit ears, transistors, diodes, etc. Apropos of the 1960's, the "Beer Can" used a very expensive, and heavy, lithium battery.

While we were there, the technician had to replace the Beer Can three times to find one that worked. Apparently they had numerous problems using and calibrating the device over the years. Since the device was round, and frequently rolled off the wing crashing onto the ground. The batteries also required replacement often and were difficult to find.

After observing what happened, I asked our Chief Engineer to follow up on this when we returned to our facility. I later spoke to the F-16 program manager at the Hill Air Force base about our experience and my concern as a taxpayer that the government was spending a lot of money on an expensive and outdated device. I was surprised to find out from him that the government actually bought 30 percent more of these devices than required because of the problems they encounter with these devices. I secured his commitment that he would look at a replacement device if we could develop one.

When I returned to our facility, we met with our very capable staff of engineers and they developed a digital voltage detector that operates on two off-the-shelf AA batteries. This design offers many superior features and is less costly than what they were using. We developed this "Juice Box," as it is called by the military, with our own R&D money.

Moreover, even amid the talk of the defense cuts, this past year, we have invested over $1 million dollars of our own money to develop a compact, rugged stores management tester that can be used across multiple aircraft platforms, saving additional procurement dollars. This development is still on-going and more money will be required to put it into service. As you can see, these are major investments for a small business, but we are committed to developing products that will meet the military's operational and procurement requirements.

I believe that this dedication to providing innovative products for the defense industry helps to illustrate the potential impact sequestration will have on my business and many others. The same people who have put their hearts, souls and backs into developing the next generation of test equipment I described before, are left wondering if there will be a next generation.

Imagine the talent erosion that is already occurring at thousands of other small and medium sized-businesses in the defense industry, as talented workers leap off what they perceive is a sinking ship. Sequestration, as is being discussed, will create a mass exodus of talent and skill to other industries.

Williams Pyro presently has 89 employees, including machinists, assemblers and R & D engineers experienced in mechanical, electrical, software, firmware, hardware and manufacturing. These jobs are in jeopardy. What is being billed as a stop-gap budget fix will have lasting effects on our defense capabilities for years to come. The switch will not just get flipped back on to reverse that trend.

Moreover, the deep personnel and program cuts will threaten our national security. Indeed, the United States could lose our technological and strategic advantage and never get it back.

In conclusion, I urge members of Congress to go back and sharpen your pencils. Sequestration is cosmetic surgery with a chainsaw. Working together, we can solve this, but we need to do it smartly and strategically, while keeping the economy moving and defending this great land.

Thank you again for inviting me to appear before to talk about this very important issue.

WilliamsPyro

DELLA WILLIAMS

EXECUTIVE BIO

President & Chief Executive Officer — Williams-Pyro, Inc.
President — WPI Firefighters' Fund

Once a one-woman manufacturing company, Della Williams made professional contacts; secured development contracts; handled sales, purchasing, and marketing; and manufactured parts in the shop. This firsthand knowledge of every aspect of the business helped build Williams-Pyro into the successful company it is today. As president and CEO, Ms. Williams has been involved in a variety of professional organizations and legislative efforts.

Serves as

- member of USS Fort Worth Committee
- an Advisory Board Member on the President's Council of the National Association of Manufacturers
- the Chair of the Texas Manufacturing State Advisory Board
- a Member on the DFW TMAC Advisory Board

Member of

- the National Defense Industrial Association and
- the North Texas Women's Business Council

Ms. Williams has also lobbied extensively in Washington, D.C. for continued federal support of the Manufacturing Extension Partnership, an initiative of the U.S. Department of Commerce. Williams-Pyro is celebrating it's 49th year in business in 2012.

Williams-Pyro, 2012

PROFESSIONAL EXPERIENCE

Williams-Pyro, Inc., Fort Worth, TX (1996-Present)
President & Chief Executive Officer
(Co-founder & Vice President of Williams Instruments, Inc. from 1963 to 1998)
(Co-founder & Vice President of Pyro Control, Inc. from 1972 to 1998)

Williams-Pyro is a woman-owned, privately-held small business founded in 1963 that produces more than 200 unique, profitable products, all designed and manufactured in-house. These include:

ElectroLinx™ — cable assemblies, connectors, adapters, ground support and test equipment for the aerospace, defense and energy sectors
StoveTop FireStop® — America's leading automatic residential stove top fire suppressor
Duradero® IECS — Intelligent Energy Control System brings smart micro-grids to the battlefield

SERVICE

WPI Firefighters' Fund, Fort Worth, TX (1999-Present)
President & Founder

In late 1999, Ms. Williams founded a nonprofit 501(c)3 organization called the WPI Firefighters' Fund to help families of firefighters killed or injured in the line of duty. In 2000, the WPI Firefighters' Fund gave $35,000 to firefighters' families in Texas. After September 11, 2001, she worked diligently to raise funds and distribute them quickly to the families of FDNY firefighters who died at the World Trade Center. She made multiple trips to New York and presented donations totaling $489,429.31 to these families. This was the first help any of them had received, and it eased their financial burdens as they awaited their benefits from the city. The fund continues to assist families of fallen firefighters, having disbursed a total of $832,263 since 2001 to families in Idaho, Mississippi, Oklahoma, Texas, New York, and California.

HONORS & AWARDS

- **2011 Tibbetts Award for Excellence in Innovation**
  Small Business Administration (SBA)
- **2011 Great Women of Texas**
  Nominee
- **2009 Small Business of the Year**
  Lockheed Martin, GT&L (LMCO)
- **2007 Best Value Gold Medalist**
  Defense Supply Center Richmond (DSCR)
- **2007 Texas Family Business of the Year Medium business category**
  Hankamer School of Business, Baylor University
- **2006 Mainspring Award**
  Texas Manufacturing Assistance Center
- **2004 Hall of Achievement**
  College of Engineering, University of Texas at Arlington
- **2004 Administrator's Award for Excellence Nominee**
  Small Business Adminstration (SBA)
- **2001 Champion Award**
  Modernization Forum National Conference
- **2001 Women of Influence Finalist**
  Fort Worth Business Press

DISCLOSURE FORM FOR WITNESSES
CONCERNING FEDERAL CONTRACT AND GRANT INFORMATION

INSTRUCTION TO WITNESSES: Rule 11, clause 2(g)(5), of the Rules of the U.S. House of Representatives for the 112th Congress requires nongovernmental witnesses appearing before House committees to include in their written statements a curriculum vitae and a disclosure of the amount and source of any federal contracts or grants (including subcontracts and subgrants) received during the current and two previous fiscal years either by the witness or by an entity represented by the witness. This form is intended to assist witnesses appearing before the House Armed Services Committee in complying with the House rule.

Witness name:_Della H Williams______________________________________

Capacity in which appearing: (check one)

___Individual

_X_Representative

If appearing in a representative capacity, name of the company, association or other entity being represented:___Williams-Pyro, Inc.______________________________

FISCAL YEAR 2011

federal grant(s) / contracts	federal agency	dollar value	subject(s) of contract or grant
W15P7T-11-C-H212	Army	70,000	Heuristic-based Prognostic Power Mgmt
W909MY-10-C-0082	Army	276,471	Intelligent Energy Control System - Mod
N00024-10-C-4141	Navy	300,000	Rapid Electrical Outfitting for Shipbuilding - Ph 2 - Yr 2
FA8222-10-C-0016	USAF	362,000	Method of Locating Unexploded Ordnance - Ph 2 - Yr 2
Dozens of direct (prime) contracts	Multiple agencies	1,572,321	Dozens of contracts to supply components/products to Gov't
Hundreds of subcontracts	Multiple agencies	3,552,664	Over 100 subcontracts to supply components to primes
	TOTAL	6,133,456	

FISCAL YEAR 2010

federal grant(s) / contracts	federal agency	dollar value	subject(s) of contract or grant
W909MY-10-C-0082	Army	2,064,000	Intelligent Energy Control System

N10PC20024	DHS	100,000	Noise Cancellation Smart (VOX) For Firefighters
N00024-10-C-4141	Navy	300,000	Rapid Electrical Outfitting for Shipbuilding - Ph 2 - Yr 1
N00024-10-C-4183	Navy	747,328	Water Impermeable Connector - Ph 2
FA8222-10-C-0016	USAF	188,000	Method of Locating Unexploded Ordnance - Ph 2 - Yr 1
FA9101-10-M-0013	USAF	100,000	Autonomous Distributed Plant Monitoring Network
Dozens of direct (prime) contracts	Multiple agencies	969,215	Dozens of contracts to supply components/products to Gov't
Hundreds of subcontracts	Multiple agencies	2,288,459	Over 100 subcontracts to supply components to primes
	TOTAL	6,707,002	

FISCAL YEAR 2009

Federal grant(s) / contracts	federal agency	dollar value	subject(s) of contract or grant
W909MY-09-C-0003	Army	730,000	Plug and Play Architecture for Tactical Power Grids
W912HZ-09-C-0004	Army	70,000	Acoustic Detection and Verification
N65538-09-M-0034	Navy	100,000	Rapid Electrical Outfitting for Shipbuilding - Ph 1
N65538-09-M-0115	Navy	100,000	Water Impermeable Connector - Ph 1
FA8224-09-C-0044	USAF	100,000	Method of Locating Unexploded Ordnance - Ph 1
FA9201-09-C-0267	USAF	750,000	Wireless Fire Detector
Dozens of direct (prime) contracts	Multiple agencies	1,005,849	Dozens of contracts to supply components/products to Gov't
Hundreds of subcontracts	Multiple agencies	3,581,784	Over 100 subcontracts to supply components to primes
	TOTAL	6,437,633	

Federal Contract Information: If you or the entity you represent before the Committee on Armed Services has contracts (including subcontracts) with the federal government, please provide the following information:

Number of contracts (including subcontracts) with the federal government:

Current fiscal year (2011):__ 157__________________________;
Fiscal year 2010:__________157__________________________;
Fiscal year 2009:__________140__________________________.

Federal agencies with which federal contracts are held:

Current fiscal year (2011):__Army, Navy, USAF, DLA__________________;
Fiscal year 2010:__ Army, Navy, USAF, DLA, DHS_____________________;
Fiscal year 2009:__ Army, Navy, USAF, DLA _________________________.

List of subjects of federal contract(s) (for example, ship construction, aircraft parts manufacturing, software design, force structure consultant, architecture & engineering services, etc.):

Current fiscal year (2011):__Test equipment, cables, connectors, SBIR research_;
Fiscal year 2010:__ Test equipment, cables, connectors, SBIR research _______;
Fiscal year 2009:__ Test equipment, cables, connectors, SBIR research _______.

Aggregate dollar value of federal contracts held:

Current fiscal year (2011):_$6,133,456________________________________;
Fiscal year 2010:_________$6,707,002_________________________________;
Fiscal year 2009:_________$6,437,633_________________________________.

Federal Grant Information: If you or the entity you represent before the Committee on Armed Services has grants (including subgrants) with the federal government, please provide the following information:

Number of grants (including subgrants) with the federal government:

Current fiscal year (2011):________________________;
Fiscal year 2010:________________________;
Fiscal year 2009:________________________.

Federal agencies with which federal grants are held:

Current fiscal year (2011):________________________;
Fiscal year 2010:________________________;
Fiscal year 2009:________________________.

List of subjects of federal grants(s) (for example, materials research, sociological study, software design, etc.):

Current fiscal year (2011):________________________;
Fiscal year 2010:________________________;
Fiscal year 2009:________________________.

Aggregate dollar value of federal grants held:

Current fiscal year (2011):________________________;
Fiscal year 2010:________________________;
Fiscal year 2009:________________________.

DOCUMENTS SUBMITTED FOR THE RECORD

JULY 18, 2012

AIA
AEROSPACE INDUSTRIES ASSOCIATION

NDIA
National Defense Industrial Association

July 25, 2012

The Honorable Buck McKeon	The Honorable Adam Smith
2184 Rayburn House Office Building	2402 Rayburn House Office Building
Washington, DC 20515	Washington, DC 20515

Dear Chairman McKeon and Ranking Member Smith:

Thank you for the opportunity to testify before the House Armed Services Committee regarding the impact of sequestration on the defense industrial base. The issue is important and the consequences of not managing the industrial base appropriately could lead to inefficiencies and loss of critical capabilities. As we stated at the hearing, industry is currently downsizing and taking other steps necessary to manage the industrial base given the $487 billion that has already been cut from the Defense budget. The additional $500 billion under sequestration and the "meat axe" manner in which it will be applied will significantly impair our ability to take those actions that will be in the long term best interest of the Department of Defense and its supporting industrial base.

During the hearing, we were asked to provide answers for the record to two important questions. The first was to provide the Committee with detailed information that can be passed to constituents at home when they ask why Congress needs to take action to eliminate sequestration - asked by Congressmen Ryan of Ohio. The second request for information was from Chairman McKeon who asked us to provide the Committee with the areas where industry needs the Office of Management and Budget to provide guidance and clarity in order for us to most effectively manage the industrial base under the terms of sequestration.

In response to Congressman Ryan's request, we have enclosed the report of the Defense Industrial Base Task Force that we completed for the Secretary of Defense in November of last year, and the report recently released by Dr. Stephen Fuller of George Mason University *"The Economic Impact of the Budget Control Act of 2011 on DOD and Non-DOD Agencies"*. These two reports contain detailed information on the industrial and economic impacts of sequestration, which will help your constituents in understanding the negative consequences if this measure goes forward.

In response to Chairman McKeon's request, we have included the recent letter sent by industry to Acting OMB Director Zients that details the areas where we need greater information and clarity in order to most effectively manage the industrial base, and with the least disruption, once sequestration is implemented.

Chairman McKeon
Ranking Member Smith
July 25, 2012
Page 2

We want to thank you again for the opportunity to testify and if you have any further questions please contact Cord A. Sterling at (703) 358-1060.

Sincerely,

David Hess Chairman, AIA President, Pratt & Whitney/UTC	Sean O'Keefe Chairman, NDIA Chairman & CEO, EADS N.A.	Robert J. Stevens Past Chairman, AIA Chairman & CEO Lockheed Martin

AIA AEROSPACE INDUSTRIES ASSOCIATION NDIA National Defense Industrial Association PSC PROFESSIONAL SERVICES COUNCIL

November 11, 2011

The Honorable Leon Panetta
Secretary of Defense
United States Department of Defense
Washington, DC 20301-1000

Dear Mr. Secretary:

With significant austerity challenges facing the Defense Department, we wanted to provide you our assessment of potential industrial base impacts resulting from severe budget reduction scenarios under consideration by the Congress and the Department of Defense. To produce the assessment, the Aerospace Industries Association, National Defense Industrial Association and the Professional Services Council convened a joint Defense Industrial Base Task Force composed of small, medium and large aerospace and defense companies across the spectrum of manufacturing and services.

Twenty-eight of the companies represented on the Task Force ranked in Defense News' Top 100 (21 in the Top 50) Defense Companies with over $254 billion in 2010 defense revenues. Mid-tier and small business interests were represented through direct participation on the Task Force, as well as via extended outreach through the Association members.

The attached report provides our assessment of potential impacts under two scenarios: a $480 billion Defense budget reduction over ten years (2013-2022), and the $1 trillion 'sequestration' option. To an industry segment that is already executing significant personnel layoffs, planning on shuttering production facilities and reassessing near- term research and development investments, the added prospect of either of the above scenarios is both daunting and of grave concern. The defense industrial base that has reliably and oftentimes courageously contributed superior technologies, capabilities, and services to America's warriors over many years must not be allowed to wither or disappear as a result of imprudent budget reductions. It is critical that industrial base capabilities always 'be there' when needed to respond to immediate and urgent defense needs.

We know budget reductions are necessary. We also know the U.S. defense industrial base is a national strategic asset. We provide the information in the attached report in hopes that it will contribute to informed decisions and deliberate, well-thought out and well-managed actions.

Sincerely,

Marion Blakey
President & CEO
Aerospace Industries Association

Lawrence P. Farrell, Jr.
Lieutenant General, USAF, Retired
President & CEO
National Defense Industrial Association

Stan Soloway
President & CEO
Professional Services Council

DEFENSE EXECUTIVES ASSESS BUSINESS IMPACTS OF MAJOR BUDGET CUTS

Conclude further reductions will deter investment, weaken industrial base

According to senior executives at manufacturing and service companies that support the U.S. military, the $480 billion in additional budget cuts projected over the next decade could cripple certain defense sectors, resulting in an industrial base that is smaller, less innovative, and less responsive to urgent wartime needs. Impacts of major cuts would most likely include:

- Forcing firms to close production lines and lay-off skilled full-time workers – beyond the thousands already let go in the wake of previous budget cuts and program cancellations– specialized manufacturing capacity and human capital that cannot be regenerated without great cost and significant time;
- Reducing or eliminating investments in capabilities beyond those needed to meet existing contracts;
- Making defense companies and business units – manufacturing and service, up and down the supply chain – more likely to exit the sector altogether, consolidate further, or be divested by their parent corporation.

Consequently, defense executives predicted an erosion of the continuum of goods and services provided by industry – from R&D to advanced development and design, to production, and then sustainment and upgrade – that could result in critical gaps in military capability over time.

These conclusions, drawn from a questionnaire distributed to several dozen member companies of the Aerospace Industries Association (AIA), the National Defense Industrial Association (NDIA), and the Professional Services Council (PSC), confirm that the negative impacts have begun. The responses also suggest that the impacts could be mitigated over time if reductions are made, paced, and managed in a balanced manner and are combined with fundamental changes in the way DoD interacts with industry when it comes to compliance measures, cost- and risk-sharing, and program stability. Cuts beyond $480 billion, which most company executives expect in future budget requests even if sequestration is avoided, would render major segments of the defense industry unable to produce critical products and components, leaving wide gaps in the domestic capacity needed to sustain an acceptable margin of military superiority into the future.

Background & Assumptions

The aerospace and defense services industry finds itself in uncertain and potentially perilous times. The cancellation of several major weapons systems in the FY 2010 budget has already led companies to shed thousands of employees and curtail investment for the future:

- For example, at the beginning of this year Boeing announced the loss of more than 1000 jobs at its Long Beach factory, on top of the roughly 4,500 layoffs initiated in 2009;
- BAE Systems announced cuts of 600 positions at its Sealy, Texas facility, on top of 2,900 let go in 2010; and

- This summer, Lockheed Martin announced voluntary separation offers for up to 6,500 employees.

This cycle is playing itself out in increments of 50, 100, 200 jobs or more in labs, factories and other defense-related facilities across the country.

To take the temperature of the industry's corporate boardrooms in anticipation of further major defense cuts, the AIA, NDIA and PSC asked their companies' top executives to assess the impact of defense cuts of approximately $480 billion – the 10-year budget total expected to be submitted by the administration next year — up to the $1 trillion sequestration that would take effect if Congress does not enact a major budget reduction plan before January 2013.

Even if the trillion-dollar "doomsday" scenario is avoided, respondents were operating under the assumption that, based on past history, more cuts would be added on top of the $480 billion over the next decade. Respondents also believed that because savings to end-strength reductions and other personnel costs will take longer to materialize, cuts to the investment accounts – procurement, research, development, and testing – will be front loaded and could reach up to 60- to 70- percent of the total defense spending decreases in the first two to three years.

Defense Industry Boardroom Facts of Life

The United States relies on private, for-profit companies to produce the preponderance of the equipment and services needed by the U.S. military. Senior management at those companies must balance several key relationships in order to survive and succeed as a business enterprise: with investors in the capital marketplace; with skilled workers in the talent marketplace; and partnerships with suppliers and customers. These elements are intrinsically linked. Moreover, all rely on one quality above all else—stability.

Steady demand from the customer for the industry's unique products provides a generally stable revenue flow and basis for long-range strategic investment. Returns on investment for the defense industry traditionally have been modest compared to industries such as pharmaceuticals, petroleum, and software. It is the *stability* of revenue sources and levels that has made defense an attractive industry for investors.

Investors rely on this industry as a hedge in their portfolios to balance risk, and expect defense companies to make business choices that provide sufficient cash flow and an acceptable rate of return. Poor or declining returns in this sector will cause investors to put their money elsewhere, or incentivize corporations to divest themselves of their defense businesses, as happened when Northrop Grumman divested its Huntington Ingalls shipyard earlier this year.

Conversely, a financially healthy sector allows the U.S. defense industry to attract the technical and scientific talent needed to sustain innovation in new products and services, all of which enables the United States to retain its military edge.

Companies' Responses

Given these realities, the AIA/NDIA/PSC members' executives were asked to assess the impact of major defense budget cuts in the following areas:

- Investment – research and development, facilities, and intellectual property.
- Structure – supply-chain composition, mergers, acquisitions, and divestitures
- Workforce – retention of critical skills, attracting new talent, implications for science and technology education;
- Sector Health and Responsiveness

INVESTMENT

Companies are already curtailing new investments in plant, personnel, research and development. One company responded that "we have already put on hold any plans to expand to a second facility [consisting of] 50,000 additional square feet of manufacturing space."

Anticipating the next round of budget cuts, an aviation company has already reduced defense research and development spending, commenting that "if we do any R&D it will be in the commercial aviation sector." Generally, independent R&D expenditures are budgeted as a percentage of sales, thus expected declines in revenue will tie directly to less R&D spending and ultimately less of the kind of innovation that creates the products and technologies U.S. troops need to survive and succeed on the battlefield.

One of the greatest worries is that, collectively, government and industry leaders will miscalculate about what our military will need in the future and make investment and budget decisions accordingly. When future world events demand certain military capabilities at short notice, the manufacturing and intellectual capacity may not be there.

In the services industry, DoD's move towards "low price/technically acceptable" awards (even for complex needs) in conjunction with the Pentagon's efficiencies campaign, has shrunk margins and correspondingly the resources available for R&D, which traditionally comes out of a company's overhead. While this challenge will affect a wide array of companies, several respondents observed that the impact will be greatest on small and smaller mid-tier businesses—many of which are critical providers of engineering and other technical talent, that by definition are far less able to weather difficult times. Said one respondent, in a theme repeated by many: "cost pressure from both customers and competitors could further reduce internal R&D in order to maintain affordable and competitive overhead rates."

INDUSTRY STRUCTURE, SIZE & COMPOSITION

Many companies expect that, given the added uncertainty and perceived risk, even the lower $460 - $480 billion range of projected budget cuts could be the "tipping point" that causes capital markets – expecting a degree of stability in exchange for comparatively modest returns – to move money elsewhere. Larger companies would be incentivized to unload their defense portfolio altogether. However, the dim prospects for this sector are making it difficult to divest. "[I] don't think we will find buyers," one executive responded. "Probably better to shutter operations and wait."

One concern that is readily apparent from both large and small companies' inputs was the potential effects further down defense supply chains, often made up of smaller businesses that lack the capacity to withstand steep drops in orders. Those effects include:

- Verticalization - Dwindling revenue would push many 2nd and 3rd tier suppliers away from DoD-related business, thus forcing prime contractors unwilling to subsidize their ailing suppliers to bring many of those critical sources and services in-house. One prime contractor, reflecting the sentiments of most of his Tier I company colleagues, said his firm is already preparing to "in-source some of the (critical) functions we currently subcontract." The existing supply-chain "would be broken" according to a respondent from a prime contractor. Fewer suppliers would reduce competition and lead to higher costs overall.
- Globalization – Falling revenue and dim prospects would incentivize companies to shutter their U.S. factories and send remaining work to their facilities abroad. States like California, Texas, Georgia and Virginia, with large aerospace and defense presence, would be hardest hit, just as they were during the 1990s. To the extent business remains within the United States, lower tier firms would be the most adversely affected, as they would be unable to compete on a cost basis with operations based in developing countries. That will make it more difficult to control counterfeit parts, increasing cost.
- Innovation Loss – Lower tier suppliers have traditionally been a great source of innovation, given that new ideas can be rapidly prototyped and tested and the appetite for risk is greater. A broken supply chain combined with less incentive to invest means less new thinking, new technologies, and new products for our military.

WORK FORCE

Most of the industry is already reducing payrolls in response to previous program cancellations and current and projected defense spending reductions. In anticipation of future budget reductions, many companies have already decided to delay hiring highly technical positions, and "making do with hourly 1099 contractors." Others have begun reducing their workforces through attrition – by up to 5 percent in one company – but most view this as a first step to significant future layoffs. Looking towards the expected defense builddown, one respondent predicted "further layoffs of engineering and manufacturing workers of between 25 and 50 percent beyond current strained levels. "

On the services side, one company reported that it had laid-off 200 workers in the last two months and had frozen hiring in their government systems business unit. Other services companies were concerned about retaining employees with unique skills in systems architecture and program and sub-contract management, skills especially important to keeping costs under control. One respondent said: "We are losing people out of this industry who are seeing the writing on the wall that DoD is not the place to be if you want a stable job. Our customers are more and more...asking us to cut our staff with one day's notice."

All companies voiced concern about the ability to attract the best and brightest students to science and engineering degrees, and of those who do graduate with these skills, the perception of a diminishing industrial base with fewer cutting edge programs will make them less likely to work in defense sectors. Even in a difficult economy, there are ample opportunities and competition in the commercial sector for skilled scientists, engineers, and technicians. This problem will be compounded as a generation of designers and other experts approach retirement, without the funding or work to support a new cohort of workers to take their place.

This problem is especially acute in design, development and production areas unique to military systems. One respondent pointed out that the design of advanced algorithms and software for military radars is distributed among a very limited number of experts in a handful of companies.

SECTOR HEALTH & RESPONSIVENESS

The major defense sectors – aircraft, shipbuilding, C4ISR, munitions, missiles, space, ground vehicles, plus related services – assessed budget impacts in the areas of design, development, production, maintenance, support and responsiveness to urgent military needs. In general, both large and small companies concluded that the general impact of cuts in the $480 billion-range on top of those already executed in recent years would be moderate to significant. Beyond that level of reduction almost all respondents believe the impact will be significant across the board.

Most expect significant impact to design and build capabilities. As it stands, there are no manned combat aircraft in development for the first time in nearly a century. Lack of any new starts will make aircraft investments "speculative" according to one respondent, who predicted that some firms will assume the risk of retaining design and build capacity if there is an expectation that programs will go forward on schedule.

However, budget cuts typically cause postponements in production and, ultimately, reductions in quantity procured. An aerospace executive recounted the case of one major supplier for a major engine program that "tooled up" for production based on forecasts of sales volume. "As the deliveries were pushed to the right, the supplier could not meet his financial obligations and was forced into bankruptcy. " Reductions in procurement quantities raise unit costs. Several companies noted that Nunn-McCurdy breaches can be triggered by these actions, thus generating adverse publicity for a situation beyond any firm's control.

The fact that delayed modernization would lead to an older, more maintenance-intensive fleet could create some opportunities in the support areas for some companies. One aircraft manufacturer responded that if defense budget cuts stayed at the $460 - $480 billion level, "the build portion of our income would be impacted significantly. The repairs and support/spares will be impacted but would be manageable." In particular, "we expect the lack of new aircraft starts to force additional service life extension and capability upgrades to existing aircraft." However, those gains would be nullified by large force structure cuts to the military's inventory of ships, aircraft, and combat vehicles and the sub-systems that go with them.

Several munitions companies predicted dire consequences even at the $480 billion reduction level because this sector has little connection to any civilian market. "As the DoD budget goes, so does the munitions industrial base" replied one producer. In general, those companies considered to be at greatest risk are those of moderate or small size and with narrow product and service lines concentrated in the defense sector.

The services sector is already seeing diminishing margins because of DoD's increase of Lowest Price/Technically Acceptable (LPTA) contract awards, even for complex requirements. This "flight to price" rather than "flight to quality," as one respondent characterized it, will require significant process adjustments within the department, as well. Service companies believe that DoD's approach to pricing is at odds with its desire to improve innovation and access the best talent from its service support contractors. As a result of LPTA practices, "we are reevaluating investments in infrastructure and employee development and benefits... [The government seems] to think that the number of [contract employees] in chairs is more important than the quality of the work."

Insofar as budget cuts would delay purchase of new information technology, one services company anticipated that the resulting personnel cuts would have the most impact on the government's "outdated legacy systems that require expensive, but extremely outdated, technical knowledge."

Real concern also exists that the on-going reductions could potentially "hollow out" key capabilities, particularly those needed to support contingencies and sustain technology innovation. According to some respondents, a number of segments of the defense services market (cyber security, IT, equipment maintenance) are expected to stay in high demand for the future and thus will remain relatively stable at the lower end of projected budget cuts.

Both manufacturing and service companies responded that a smaller and less financially healthy defense sector will not have the capacity to surge weapons, equipment, and services to the battlefield in a way that the U.S. military has come to expect and rely on over the past decade.

Mitigating Measures

The companies were asked to consider measures that would ameliorate the impact of defense cuts on their ability to stay in the industry and produce the capabilities needed. Reflecting a common sentiment, one respondent said the government should "ensure cuts are moderate in the first three to four years to allow companies to smoothly transition downwardly from DoD programs." However, the historical record of past draw-downs plus the difficulty of achieving prompt savings in other areas strongly suggests that the department's investment accounts will bear the brunt of early cuts, giving companies little time to prepare or respond.

A company representative urged Congress and DoD to "carefully weigh cuts and cancellations to programs that are unique to the military and have no connection to the civilian sector... if cuts at this range are not carefully managed with an eye to the industrial base, critical capabilities and facilities could be lost even at the [$480 Billion] level of reduction."

An aerospace executive asked that Congress abstain from the recent habit of governing through Continuing Resolutions, which "limit the ability of the government and industry to execute programs and negotiate contracts efficiently, thus raising costs and constricting the critical flow of funding."

Many of the mitigation measures reflect longstanding industry priorities that are now all the more urgent given new budget realities. Those include:

- Creating a more equitable and sustainable arrangement for sharing the risks and costs associated with major weapons programs, especially during concurrent development of complex systems.
- Reducing compliance burdens and other unnecessary cost drivers. For example, the attempt to get cost data on commercial items will actually increase cost to the government by requiring collection of data that is not now kept and reduce the pool of suppliers willing to compete for DoD contracts.
- Approving multi-year budgets for long-term design and development programs, establishing firm requirements early in the acquisition process in order to avoid "requirements creep."
- Streamlining DoD acquisition processes by eliminating lower priority reviews, with a goal of accelerating the timeline for issuing contract awards by 30 percent.
- Increasing use of the private sector for research and development, as well as maintenance, repair, overhaul, and other key services, a sustainment model that preserves the industrial base while supporting exports, which benefits innovation and increases domestic employment.
- Accelerating implementation of export control reform, along with other actions to open international markets to U.S. industry.
- Investing more funding in science and technology education, research and mentorship programs, inspiring talented young people to pursue a defense-related aerospace career, in spite of the difficult budget situation.

With respect to services, respondents recommended a renewed focus on "how" the Department buys, in addition to what it buys. The "better buying initiatives" create some positive incentives for firms to retain core capabilities to meet the department's critical missions. However, services acquisitions continue to be treated monolithically, when each sector has a different character and competitive dynamics.

In this environment, a more intense collaborative dialogue between industry and the DoD would help mitigate the risks associated with constrained resources. In the past, increasing defense budgets could mask systematic flaws in the U.S. government's approach to dealing with the nation's industrial base; this is no longer possible.

In conclusion, both the executive and legislative branches must take sensible, long-term, measures to mitigate the negative impacts of the expected $480 billion reduction. Cuts beyond that, up to the $1 trillion sequestration level, would severely damage the Defense Industrial Base as a commercially viable enterprise, as a reliable and responsive provider of urgent wartime needs, and as a national strategic asset that is indispensable to the defense of the United States.

###

The Economic Impact of the Budget Control Act of 2011 on DOD & non-DOD Agencies

GEORGE MASON UNIVERSITY

Stephen S. Fuller, Ph.D.
Dwight Schar Faculty Chair and University Professor
Director, Center for Regional Analysis
George Mason University
July 17, 2012

For more information: secondtonone.org

The Economic Impact of the Budget Control Act of 2011 on DOD and Non-DOD Agencies

by

Stephen S. Fuller, Ph.D.
Dwight Schar Faculty Chair and University Professor
Director, Center of Regional Analysis
George Mason University
Arlington, Virginia

with

Chmura Economics & Analytics
Richmond, Virginia

prepared for

Aerospace Industries Association
Arlington, Virginia

July 17, 2012

The Economic Impact of the Budget Control Act of 2011 on DOD and Non-DOD Agencies

Summary of Research Findings

There is a broad consensus that implementation of the automatic federal spending reductions provided for in the Budget Control Act (BCA) of 2011 would have significant negative impacts on the U.S. economy in 2013. The Congressional Budget Office (May 2012) released its analyses of these impacts confirming what other independent organizations had already concluded—that if the provisions of the BCA of 2011 are implemented beginning January 2, 2013, the U.S. economy, which is still struggling to sustain its recovery more than three years after the end of the 2008-2009 recession, could be pushed into recession during the first half of 2013. The International Monetary Fund (IMF) released a report on July 3, 2012 with the same conclusion. Other analyses have reported on the impacts of these federal spending reductions or sequestration on specific industries and their conclusions are the same: that implementing BCA of 2011 would severely impact the economy in 2013 with these losses reflected in reduced Gross Domestic Product (GDP) and a broad based loss of jobs that could add an estimated 1.5 percentage points to the current U.S. unemployment rate.

This author released a report entitled "The U.S. Economic Impact of Approved and Projected DOD Spending Reductions on Equipment in 2013" on October 24, 2011 in which the economic effects of reduced spending for military equipment were calculated. This analysis determined that a combined $45.1 billion reduction in the purchase of military equipment and in Research and Development funding (BCA I and II) by the Department of Defense would reduce GDP by $86.5 billion and result in the loss of 1,006,320 direct, indirect and induced jobs across all sectors of the U.S. economy impacting every state and representing a decline of personal income (salaries and wages) totaling $59.4 billion. This analysis was restricted to the procurement of military equipment and R&D spending and excluded reductions in DOD civilian payroll and DOD outlays for operations and maintenance. It also excluded the projected spending reductions in the BCA of 2011 impacting non-DOD agencies and therefore only provided a partial assessment of the potential consequences of federal spending reductions under sequestration.

The economic impact assessment presented in this report includes all discretionary spending subject to cutbacks under the BCA of 2011 (both the effects of statutory limits and automatic reductions) for DOD and non-DOD agencies (e.g., Agriculture, Commerce, Education, EPA, Energy, Health and Human Services, Homeland Security, Housing and Urban Department, Interior, Justice, Labor, NASA, State, and Transportation). However, it excludes spending reductions for all federal mandatory programs such as Medicare. The Congressional Research Service report, "The

Budget Control Act of 2011: The Effects on Spending and the Budget Deficit When the Automatic Spending Cuts Are Implemented" (CRS Report) dated April 23, 2012, was relied upon for the magnitude and timing of these federal spending reductions. However, the spending reductions used herein vary slightly from those reported by CRS. Rather than using spending reductions from the baseline budget forecast, year-over-year changes in spending were used as these provide a more realistic measure of the actual reductions for calculating associated economic impacts.

The identified economic impacts occurring in 2013 constitute the greatest one-year reductions in GDP, personal earnings and employment. The post-2013 schedule of federal spending trends through 2021 moderate these first-year losses, resulting in overall ten-year economic impacts that are smaller than the impacts occurring in 2013, although these are still negative for the full period. As the initial impacts of the BCA of 2011 are so damaging to the U.S. economy, the focus of this report will be on 2013.

As currently formulated, the automatic spending cuts affecting DOD and non-DOD agencies' discretionary spending authorities beginning January 2, 2013 will:

- Reduce the nation's GDP by $215 billion;

- Decrease personal earnings of the workforce by $109.4 billion; and,

- Cost the U.S. economy 2.14 million jobs.

As a consequence of sequestration, GDP growth in 2013 will be reduced by two-thirds and unemployment will increase by as much as 1.5 percentage points raising the current national rate above 9 percent. These are the easily measured impacts.

Other collateral impacts will be driven by behavioral factors. The loss of consumer confidence may suppress spending, especially spending requiring credit such as for autos and housing. Personal saving may increase taking further spending out of the economy. Business investment and private sector hiring may be dampened as a result of increased uncertainty—contributing to further erosion of the national economy. These and other collateral impacts will enlarge the negative consequences of the initial federal spending reductions and contribute to further deepening of the economic contraction in 2013, thereby extending its duration and increasing its magnitude.

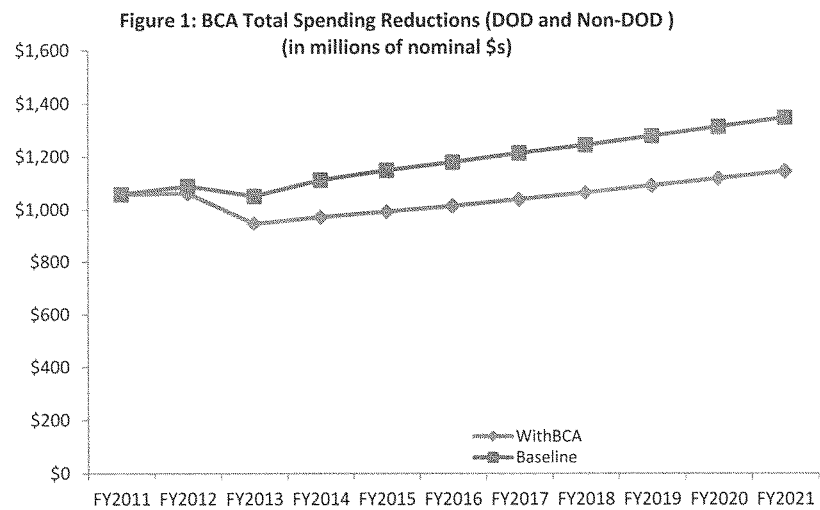
Other costs will occur over a longer timeframe resulting from deferred or foregone innovation by both federal agencies and private entrepreneurs. These disruptions to the U.S. economy will have cumulative impacts with far-reaching and potentially more significant consequences than these initial first-year impacts. While these are beyond the scope of this analysis they need to be recognized and understood.

Still, these initial economic impacts—the loss of GDP, personal income and jobs—are real and have measurable consequences. If they are allowed to occur as currently scheduled, the long-term consequences will permanently alter the course of the U.S. economy's performance, changing its competitive position in the global economy.

Automatic Federal Spending Reductions Provided For in the Budget Control Act of 2011

The BCA of 2011 was signed into law on August 2, 2011. Among other provisions, this Act provided for two major categories of federal spending reductions: (1) discretionary spending caps that became effective in FY 2012 and (2) automatic spending reductions that now will become effective January 2, 2013. This reduction in budget authority would result in decreased discretionary spending by DOD totaling $800 billion and by non-DOD agencies totaling $700 billion with a roughly $200 billion reduction in mandatory programs (mainly from Medicare) over this ten-year period.

The CRS Report has analyzed the federal spending reductions mandated by the BCA. This analysis confirms that these cutbacks result in a significant reduction in federal spending beginning in FY 2013. Under the BCA, the federal budget reductions reduce spending levels from a "baseline" trajectory as shown in Figure 1.

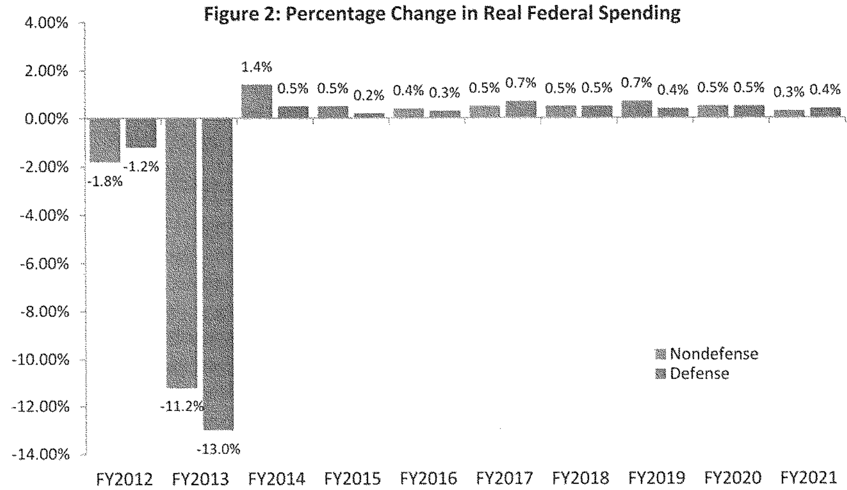


Source: Congressional Research Service

The largest year-over-year spending reduction would occur in FY 2013 due to the implementation of the automatic spending cuts with spending levels reduced 12.1 percent (in nominal terms) from FY 2012 levels (in FY 2012 spending will reflect a nominal increase over FY 2011). For DOD, this will represent a 11.5 percent reduction in spending in FY 2013 following a small (0.6 percent) nominal increase in FY 2012. For non-DOD agencies, their FY 2013 spending levels would decline by 9.8 percent following a year with no change in spending authority from FY 2011 (in nominal terms).

In subsequent fiscal years, the projected spending reductions from the baseline forecast would result in nominal increases in federal spending subject to BCA caps averaging 2.4 percent over the FY 2014-FY 2021 period. This rate of increase would also result in small "real" increases in spending although the actual gain in inflation-adjusted dollars will depend on the inflation rates over this period. Congressional Research Service calculations of spending levels by fiscal year for DOD and non-DOD for the FY 2012-FY 2021 period are shown in Figure 2.

Figure 2: Percentage Change in Real Federal Spending



Source: Congressional Research Service

The Economic Impact of the BCA of 2011 in 2013

This author's October 24, 2011 report entitled "The U.S. Economic Impact of Approved and Projected DOD Spending Reductions on Equipment in 2013" was limited to BCA reductions affecting DOD spending for military equipment and R&D and excluded reductions in DOD civilian payroll and DOD outlays for operations and maintenance. It also excluded the projected spending reductions in the BCA of 2011 impacting non-DOD agencies and therefore only provided a partial assessment of the potential consequences of sequestration-mandated federal spending reductions. The analyses presented herein include both DOD and non-DOD agencies subject to BCA required federal spending reductions.

The CRS Report presents estimates for the discretionary budget authority subject to BCA limits. This schedule of potential discretionary spending—the combined effects of statutory limits and automatic spending reductions—provides the inputs to the economic impact analysis presented herein. The annual changes in federal spending—year-to-year changes—provide the measure of direct federal spending reductions for DOD and non-DOD agencies.

Reductions in procurement spending are distributed across the primary sectors of the U.S. economy based on the General Services Administration (GSA) procurement database differentiating DOD and non-DOD purchasing patterns as reported in Tables 4 and 6. Reductions in federal payroll outlays are shown in a single-line item as a change in "federal payroll" on these tables.

Impacts of DOD Spending Reductions Under BCA

The estimated decrease in federal spending with the implementation of the Budget Control Act of 2011 (spending for FY 2012 and FY 2013) will reduce DOD spending by a total of $56.7 billion (see Table 4). This reduction in DOD spending is composed of payroll reductions totaling $7.1 billion and procurement reductions totaling $49.6 billion. These spending reductions would reduce U.S. gross domestic product by $94.5 billion.

These spending reductions and lost GDP would result in the loss of 325,693 direct jobs, including 48,147 civilian DOD employees. As shown in Table 4, the Professional and Business Services (PBS) sector would account for the largest direct job losses from DOD budget reductions. The sector would account for 133,883 direct jobs lost or 41.1 percent of the total direct job loss. This concentration of direct job losses reflects the impacts of DOD procurement spending reductions on contractors providing scientific, engineering and technical services.

These direct jobs losses would be accompanied by the further loss of 282,426 jobs among the suppliers and vendors that depend on DOD's primary contractors (indirect job losses) and 482,240 jobs that are dependent on the payroll spending (induced job losses) of the workers whose jobs depended on DOD's procurement and payroll spending that was reduced as a result of the BCA of 2011.

A total of 1,090,359 jobs with a total labor income of $46.5 billion would be lost due to DOD budget cuts in FY 2012-FY 2013. Of these total job losses, almost 70 percent would come from two high-value added sectors: 37.1 percent (404,507) would be manufacturing jobs and 32.2 percent (351,311 jobs) would consist of professional and business service jobs. The federal sector job losses would account for 9.8 percent of the total (107,220 jobs). Although representing smaller percentages, all of the remaining sectors would experience job losses as the impacts from DOD spending reductions spread across the national economy.

Impacts of Non-DOD Agency Spending Reductions Under BCA

Budget cuts impacting non-DOD agencies (FY 2012-FY 2013) are estimated at $59.0 billion including $33.8 billion in reduced federal payroll (see Table 6). These non-DOD spending reductions would reduce U.S. GDP by $120.5 billion. Non-DOD cutbacks would have a much greater direct impact on federal employment than DOD budget reductions due to the respective differences in procurement and payroll distributions.

Non-DOD agency budget cuts would generate direct employment reductions of 420,529 jobs with an estimated 229,116 jobs or 54.5 percent of these direct job losses consisting of federal workers. Professional and Business Services would lose 125,012 direct jobs (29.7 percent of the total direct jobs losses), reflecting the impacts on federal contractors providing scientific, engineering and technical services. Additionally, suppliers and vendors of primary federal contractors would lose 150,552 jobs. This loss of direct and indirect jobs would contribute to the loss of an additional 476,268 jobs dependent on the payroll spending (induced jobs) foregone due to these spending reductions experienced by non-DOD agencies.

In total, non-DOD agency budget reductions for the FY 2012- FY 2013 period would generate job losses of 1,047,349 with almost half of these (510,229) consisting of federal jobs and 31 percent coming from the professional and business services sector. These two sectors would account for 80 percent of the direct, indirect and induced job losses attributable to non-DOD agency budget reductions.

Total Economic Impacts Under BCA in 2013

These economic impacts are summarized in Table 1 below for DOD and non-DOD agencies. Combined, the budget reductions (statutory discretionary spending limits and automatic spending reductions) would result in the loss of 2.14 million jobs in 2013 and the loss of $215 billion in GDP. This job loss would add as much as 1.5 percentage points to the current unemployment rate and this sharp decline in GDP would erase two-thirds of the gains in GDP currently projected for 2013. The distribution of these job losses are shown in Table 3 and the state-level losses of gross state product and labor income (personal earnings) are presented in Tables 10 and 11.

Table 1

Summary of U.S. Economic Impacts of the Budget Control Act of 2011
Fiscal Year 2012 and 2013
(in billions of current year dollars)

Sources of Impact	Spending Reductions* DOD	Spending Reductions* Non-DOD	Total Impacts
Direct Impacts (1)	$56.7	$59.0	$115.7
Total Output (2)	$94.5	$120.5	$215.0
Personal Earnings (3)	$46.5	$62.9	$109.4
Employment (4)	1,090,359	1,047,349	2,137,708
Direct	325,693	420,529	746,222
Indirect	282,426	150,552	432,978
Induced	482,240	476,268	958,508

Sources: GMU Center for Regional Analysis; Chmura Economics & Analysis
*Direct, indirect and induced impacts resulting from BCA-mandated federal spending reductions during FY 2012 and FY 2013; excludes impacts from cuts in entitlement programs. (1) Congressional Research Service, (2) reduction from GDP, (3) lost labor income, (4) direct, indirect and induced jobs lost due to BCA spending reductions in FY 2012 and FY 2013.

Employment Impacts by State Impact of the BCA of 2011 in 2013

The estimated job losses under BCA, summarized in Table 1, can be disaggregated to the state level employment impacts based on the historic distribution of DOD and non-DOD payroll and procurement spending. By using the most recent state-level distribution (FY 2010) of federal spending for payroll and procurement disbursements for DOD and non-DOD agencies the potential state-level vulnerabilities can be identified. Actual agency budget reductions will have a different pattern depending on how each agency chooses to absorb these cuts in their operating programs and public service requirements. Still, this state-level distribution of impacts confirms that DOD and non-DOD spending patterns vary considerably across the states and that in many states, the non-DOD agency spending cuts will be the primary sources of potential employment losses.

Several states stand out as being particularly vulnerable to federal spending cuts. The ten states (including the District of Columbia) shown to have the greatest potential job losses from federal spending cutbacks are listed in Table 2. These ten states account for more than one-half (55.3 percent) of the total potential jobs losses, with California accounting for 10.5 percent and Virginia accounting for 9.7 percent representing a combined 20.2 percent of the job losses based on their FY 2010 share of DOD and non-DOD federal payroll and procurement outlays.

Table 2

Top Ten State Employment Impacts of the Budget Control Act of 2011
Fiscal Years 2012 and 2013

State	Job Losses* DOD Cuts	Job Losses* Non-DOD Cuts	Total Job* Losses
California	135,209	90,255	225,464
Virginia	136,191	71,380	207,571
Texas	98,979	60,494	159,473
DC	15,169	112,238	127,407
Maryland	39,395	75,400	114,795
Florida	41,905	37,554	79,459
Pennsylvania	39,941	38,513	78,454
New York	28,809	41,201	70,010
Massachusetts	41,469	19,028	60,497
Georgia	27,609	26,903	54,512

Sources: GMU Center for Regional Analysis, Chmura Economics & Analysis. *Direct, indirect and induced job losses resulting from BCA-mandated federal spending reductions during FY 2012 and FY 2013; excludes impacts from cuts in entitlement programs.

The full potential job loss distribution across all states is presented in Table 3.

Table 3

State Employment Impacts of the Budget Control Act of 2011
Fiscal Years 2012 and 2013

State	Job Losses* DOD Cuts	Job Losses* Non-DOD Cuts	Total Job* Losses
Alabama	26,845	11,933	38,778
Alaska	5,893	4,518	10,411
Arizona	35,248	13,941	49,189
Arkansas	3,601	5,548	9,149
California	135,209	90,255	225,464
Colorado	18,442	24,120	42,562
Connecticut	36,230	5,712	41,942
Delaware	65	2,137	2,202
District of Columbia	15,169	112,238	127,407
Florida	41,905	37,554	79,459
Georgia	27,609	26,903	54,512
Hawaii	7,857	2,831	10,688
Idaho	982	9,429	10,411
Illinois	23,245	30,411	53,656
Indiana	14,950	8,992	23,942
Iowa	5,238	5,878	11,116
Kansas	6,220	7,675	13,895
Kentucky	17,024	11,621	28,645
Louisiana	18,879	9,553	28,432
Maine	4,256	3,012	7,268
Maryland	39,395	75,400	114,795
Massachusetts	41,469	19,028	60,497
Michigan	13,531	17,679	31,210
Minnesota	4,911	11,122	16,033
Mississippi	5,238	6,434	11,672
Missouri	33,611	17,480	51,091
Montana	981	4,064	5,045
Nebraska	2,618	4,009	6,627
Nevada	4,256	6,155	10,411
New Hampshire	3,601	2,705	6,306
New Jersey	25,427	17,755	43,182
New Mexico	4,911	23,521	28,432
New York	28,809	41,201	70,010
North Carolina	11,895	17,434	29,329

Table 3 Continued

State	Job Losses* DOD Cuts	Job Losses* Non-DOD Cuts	Total Job* Losses
North Dakota	982	2,481	3,463
Ohio	21,280	19,123	40,403
Oklahoma	7,967	7,852	15,819
Oregon	2,946	9,025	11,971
Pennsylvania	39,941	38,513	78,454
Rhode Island	2,619	1,870	4,489
South Carolina	14,732	15,623	30,355
South Dakota	1,965	2,738	4,703
Tennessee	10,148	28,972	39,120
Texas	98,979	60,494	159,473
Utah	8,294	7,739	16,033
Vermont	2,292	1,770	4,062
Virginia	136,191	71,380	207,571
Washington	17,024	24,661	41,685
West Virginia	982	9,065	10,047
Wisconsin	27,609	8,946	36,555
Wyoming	654	2,125	2,779
Guam	2,181	491	2,672
Puerto Rico	2,181	3,056	5,237
Undistributed	25,872	43,177	69,049
Totals	1,090,359	1,047,349	2,137,708

Sources: GMU Center for Regional Analysis; Chmura Economics & Analysis. *Direct, indirect and induced job losses resulting from BCA-mandated federal spending reductions during FY 2012 and FY 2013; excludes impacts from cuts in entitlement programs. Columns and rows may not add up to the totals due to rounding.

Measuring Economic Impact: How To Read The Tables

The CRS report is the principal source for the distribution of budget reductions to DOD and non-DOD agencies and their magnitudes and schedule over the FY 2011-FY 2021 period. It is assumed that all non-DOD agencies will experience the same percentage cutback with the distribution between salaries and wages (payroll) and procurement being proportional to non-DOD agency's budget split between payroll and procurement as reported for FY 2010 (U.S. Census, Consolidated Federal Funds Report). The DOD cutback is assumed to be the same as reported in the CRS report.

Cutbacks from procurement were distributed across twelve major industry sectors based on the North American Industrial Classification System (NAICS). The distribution is based on the purchasing matrix from the GSA procurement database that reflects historic procurement data (2000-2010) for each agency reported by NAICS Industries. These federal budget reductions, distributed by industry sector, are shown in Tables 4, 6, 8 and 9. Reductions affecting federal payroll and their economic impacts are shown under the heading "federal payroll." Impacts affecting state and local government sectors are combined under the heading "Government." Other headings include: TWU – Transportation, Wholesale Trade and Utilities; FIRE – Finance, Insurance and Real Estate; PBS – Professional and Business Services; Trade – Retail Trade; Information – Information Services; Leisure – Leisure and Hospitality.

The IMPLAN Pro model was used to estimate the GDP impact, the direct labor income or personal earnings effects and the indirect and induced employment impacts of these budget cutbacks by industry sector.

The impacts of the budget cutbacks reported by NAICS Industry sectors were converted to occupational categories by using the national industry-occupation matrix. These are presented in Tables 5 and 7 for the direct employment effects for budget cuts affecting DOD and non-DOD agencies respectively for the FY 2012-FY 2013 period.

Direct federal spending reductions are the estimated changes in federal spending on a year-to-year basis; that is, budget levels in FY 2012 are compared to budget outlays in FY 2011 and for FY 2013 the value of cutbacks are the differences between FY 2012 and proposed budget levels for FY 2013 (with BCA). These differences vary slightly from the values presented in the CRS report that represent the difference between the proposed reduced budget level and the hypothetical baseline budget for FY 2013 rather than the year-to-year spending comparison.

Direct impact is the measure of the output value lost directly as a consequence of the federal budget cutback. For procurement, this value is equal to the value of the reduction in federal purchases. For payroll, however, direct impact measures the estimated value of the services that will be lost due to reductions in federal employment. As a result, the direct impact of reductions in federal payroll outlays is larger than the value of the direct payroll cutback. This difference explains why the total Direct Impact value is larger than the total value of the Direct Federal Spending Cut.

Total Impact is the sum of the Direct Impact and its indirect (impacts on suppliers and vendors) and induced (household income benefits) effects. It is the accumulated value of the direct spending lost and the lost monetary value that would have been achieved as these dollars where recycled through the economy being spent and re-spent with business and consumer outlays spreading out across all sectors of the national economy.

The GDP impact from this direct, indirect and induced spending—or the absence of this spending—accounts only for the non-duplicative, value-added portion of this economic activity and therefore is smaller than the Total Impact.

As shown in Table 4, the Total Impact of direct federal spending cuts affecting DOD over the FY 2012-FY 2013 period is projected to total $157.6 billion and will reduce GDP by $94.5 billion. Similarly, as shown in Table 6, non-DOD agency cutbacks for the same period would generate a Total Impact of $173.5 billion and reduce GDP by a total of $120.5 billion.

In addition, this loss of GDP as a result of federal spending cuts can be expressed in terms of lost jobs and labor income. Employment impacts include: (1) those resulting directly from the reduction in procurement and federal payroll spending, (2) the loss of employment by suppliers and vendors associated with the prime contractors and (3) the lost jobs dependent on the payroll spending of employees of the prime contractors and their suppliers and vendors. This payroll effect associated with DOD cutbacks during FY 2012 and FY 2013 would total $46.5 billion and would total $62.9 billion as a result of cutbacks impacting non-DOD agencies.

Conclusions

The research presented herein measures the magnitude and significance of economic impacts that will be generated as a result of the Budget Control Act (BCA) of 2011. These impacts can be identified as: (1) a decline in gross domestic product (GDP), (2) a decreased labor income and (3) a loss of jobs. While these impacts will extend over a planned ten-year period, their incidence has been shown to impact FY 2013 to the greatest extent, with the result that economic losses would reverse the positive GDP trend occurring since the recovery began in June 2009 and push the U.S. economy towards recession with the associated job loss raising the unemployment rate by as much as 1.5 percentage points above the current level.

The magnitude of economic impacts resulting from BCA over the combined FY 2012-FY 2013 period have been shown to be large and their impact on the U.S. economy to be significant:

- Combined DOD and non-DOD agency spending reductions totaling $115.7 billion in FY 2013 would reduce the 2013 U.S. GDP by $215.0 billion.

- These spending reductions would result in the loss of 746,222 direct jobs including cutbacks in the federal workforce totaling 277,263 and decreases in the federal contractor workforce totaling 468,959 jobs, thus affecting all sectors of the national economy.

- The loss of these 746,222 direct jobs and 432,978 jobs of suppliers and vendors (indirect jobs) dependent on the prime contractors would reduce total labor income in the U.S. by $109.4 billion.

- The loss of this labor income and the resultant impacts of reduced consumer spending in the economy would generate an additional loss of 958,508 jobs dependent on the spending and re-spending of payroll dollars associated with the direct and indirect jobs lost as a result of BCA.

- This loss of $215.0 billion in GDP and 2.14 million jobs in 2013 would erase two-thirds of the GDP gains projected for the year and raise the national unemployment rate by 1.5 percentage points by the end of 2013.

- These economic impacts would affect every state with their respective vulnerabilities to projected DOD and non-DOD spending reductions being determined by their agency mix and relative magnitudes of federal payroll and procurement. Based on current patterns of federal spending by state, ten states account for more than half of total federal payroll and procurement outlays. This significant concentration of federal spending represents a major threat to these states' economies in 2013. While other states may appear less vulnerable to federal spending reductions, these may also suffer significant impacts due to their smaller sizes or more specialized economic structures.

Table 4

Effect of DOD Spending Reductions on the National Economy, FY2012-13 Cumulative

	Total GDP (Direct+Ripple)	Labor Income (Direct+Ripple)	Employment Impact			
Sector	($Million)	($Million)	Direct	Indirect	Induced	Total
Natural Resource	$109.1	$49.0	359	421	531	1,311
Construction	$6,080.9	$3,048.3	25,949	16,906	26,493	69,348
Manufacturing	$31,534.6	$14,339.9	55,410	167,301	181,796	404,507
Trade	$3,620.6	$1,660.9	24,343	7,097	18,672	50,112
TWU	$2,424.4	$1,071.4	8,964	6,521	14,280	29,765
Information	$3,050.3	$1,333.7	7,383	10,210	12,963	30,556
FIRE	$127.9	$21.9	648	433	446	1,527
PBS	$28,102.9	$14,576.1	133,883	58,527	158,900	351,311
Education/Health	$1,113.9	$600.0	6,995	2,680	6,397	16,072
Leisure	$285.1	$132.2	2,909	778	1,203	4,890
Other Service	$729.3	$385.3	5,701	2,602	4,296	12,599
Government	$943.3	$506.2	5,003	842	5,295	11,140
Federal Payroll	$16,383.8	$8,791.9	48,147	8,107	50,966	107,220
Total	**$94,506.1**	**$46,517.0**	**325,693**	**282,426**	**482,240**	**1,090,359**

Effect of BCA of 2011 (DOD FY2012-FY2013)

	Direct Federal Spending Cut	Direct Impact	Total Impact (Direct+ Ripple)	Total GDP (Direct+Ripple)
Sector	($Million)	($Million)	($Million)	($Million)
Natural Resource	$70.1	$70.1	$186.0	$109.1
Construction	$3,693.5	$3,693.5	$10,654.4	$6,080.9
Manufacturing	$22,523.1	$22,523.1	$62,193.1	$31,534.6
Trade	$2,274.0	$2,274.0	$5,432.1	$3,620.6
TWU	$1,654.5	$1,654.5	$3,814.4	$2,424.4
Information	$2,008.7	$2,008.7	$5,144.7	$3,050.3
FIRE	$111.1	$111.1	$167.9	$127.9
PBS	$15,474.7	$15,474.7	$43,160.3	$28,102.9
Education/Health	$634.2	$634.2	$1,785.7	$1,113.9
Leisure	$179.3	$179.3	$472.7	$285.1
Other Service	$419.5	$419.5	$1,223.0	$729.3
Government	$534.7	$534.7	$1,272.4	$943.3
Federal Payroll	$7,099.5	$9,286.3	$22,099.7	$16,383.8
Total	**$56,676.9**	**$58,863.7**	**$157,606.3**	**$94,506.1**

Note: Columns and rows may not add up to the totals due to rounding.

Table 5

Direct Employment Impacts of DOD Cutbacks
By Occupation, FY 2013

Occupation Group	Jobs Impacted	Percent
Architecture and Engineering	40,036	12.3
Arts, Design, Entertainment, Sports, and Media	3,908	1.2
Building and Grounds Cleaning and Maintenance	5,862	1.8
Business and Finance	32,569	10.0
Community and Social Service	1,628	0.5
Computer and Mathematics	22,799	7.0
Construction and Extraction	24,101	7.4
Education, Training and Library	2,931	0.9
Farming, Fishing and Forestry	489	0.2
Food Preparation and Service	3,257	1.0
Health Care Practitioners and Technicians	8,142	2.5
Health Care Support	1,954	0.6
Installation, Maintenance and Repair	14,005	4.3
Legal	2,467	0.8
Life, Physical and Social Science	14,982	4.6
Management	23,776	7.3
Office and Administrative Support	41,689	12.8
Personal Care and Service	1,303	0.4
Production	30,615	9.4
Protective Service	22,147	6.8
Sales and Related	12,051	3.7
Transportation and Material Moving	14,982	4.6
Total	325,693	100.0

Note: Columns and rows may not add up to the totals due to rounding.

Table 6

Effect of Non-DOD Spending Reductions on the National Economy, FY2012-13 Cumulative

	Total GDP (Direct+Ripple)	Labor Income (Direct+Ripple)	Employment Impact			
Sector	($Million)	($Million)	Direct	Indirect	Induced	Total
Natural Resource	$169.0	$76.0	556	653	823	2,032
Construction	$2,561.9	$1,284.3	10,943	7,129	11,172	29,245
Manufacturing	$5,353.8	$2,434.6	9,416	28,431	30,895	68,743
Trade	$2,366.4	$1,085.6	15,926	4,643	12,216	32,786
TWU	$886.4	$391.7	3,280	2,386	5,226	10,892
Information	$1,281.9	$560.5	3,106	4,295	5,453	12,854
FIRE	$871.3	$149.3	4,417	2,952	3,037	10,406
PBS	$26,215.1	$13,597.0	125,012	54,649	148,371	328,033
Education/Health	$2,214.7	$1,193.0	13,922	5,334	12,731	31,987
Leisure	$105.5	$48.9	1,077	288	445	1,811
Other Service	$257.1	$135.8	2,012	918	1,516	4,446
Government	$328.7	$176.4	1,745	294	1,847	3,885
Federal Payroll	$77,889.6	$41,797.2	229,116	38,577	242,535	510,229
Total	**$120,501.4**	**$62,930.2**	**420,529**	**150,552**	**476,268**	**1,047,349**

Effect of BCA of 2011, Non Defense (FY2012-FY2013)

	Direct Federal Spending Cut	Direct Impact	Total Impact (Direct+ Ripple)	Total GDP (Direct+Ripple)
Sector	($Million)	($Million)	($Million)	($Million)
Natural Resource	$108.6	$108.6	$288.1	$169.0
Construction	$1,556.1	$1,556.1	$4,488.7	$2,561.9
Manufacturing	$3,823.9	$3,823.9	$10,558.9	$5,353.8
Trade	$1,486.3	$1,486.3	$3,550.4	$2,366.4
TWU	$604.9	$604.9	$1,394.5	$886.4
Information	$844.2	$844.2	$2,162.1	$1,281.9
FIRE	$756.6	$756.6	$1,143.2	$871.3
PBS	$14,435.2	$14,435.2	$40,261.1	$26,215.1
Education/Health	$1,260.9	$1,260.9	$3,550.4	$2,214.7
Leisure	$66.3	$66.3	$174.9	$105.5
Other Service	$147.9	$147.9	$431.1	$257.1
Government	$186.3	$186.3	$443.3	$328.7
Federal Payroll	$33,751.5	$44,147.8	$105,063.3	$77,889.6
Total	**$59,028.6**	**$69,424.9**	**$173,510.1**	**$120,501.4**

Note: Columns and rows may not add up to the totals due to rounding.

Table 7

Direct Employment Impact of Non-DOD Agency Cutbacks
By Occupation, 2013

Occupation Group	Jobs Impacted	Percent
Architecture and Engineering	21,447	5.1
Arts, Design, Entertainment, Sports, and Media	3,785	0.9
Building and Grounds Cleaning and Maintenance	10,093	2.4
Business and Finance	40,371	9.6
Community and Social Service	10,093	2.4
Computer and Mathematics	23,550	5.6
Construction and Extraction	15,139	3.6
Education, Training and Library	6,728	1.6
Farming, Fishing and Forestry	1,682	0.4
Food Preparation and Service	2,944	0.7
Health Care Practitioners and Technicians	13,877	3.3
Health Care Support	4,205	1.0
Installation, Maintenance and Repair	14,298	3.4
Legal	6,728	1.6
Life, Physical and Social Science	15,980	3.8
Management	24,811	5.9
Office and Administrative Support	103,030	24.5
Personal Care and Service	4,626	1.1
Production	8,831	2.1
Protective Service	62,238	14.8
Sales and Related	11,775	2.8
Transportation and Material Moving	14,298	3.4
Total	420,529	100.0

Note: Columns and rows may not add up to the totals due to rounding.

Table 8

Effect of DOD Spending Reductions on the National Economy, FY2012-21 Cumulative

	Total GDP (Direct+Ripple)	Labor Income (Direct+Ripple)	Employment Impact			
Sector	($Million)	($Million)	Direct	Indirect	Induced	Total
Natural Resource	$83.3	$37.4	281	330	416	1,026
Construction	$4,640.7	$2,326.4	20,306	13,229	20,731	54,267
Manufacturing	$24,066.2	$10,943.7	43,360	130,917	142,260	316,536
Trade	$2,763.1	$1,267.6	19,049	5,554	14,612	39,214
TWU	$1,850.3	$817.6	7,014	5,103	11,175	23,292
Information	$2,327.9	$1,017.9	5,777	7,990	10,144	23,911
FIRE	$97.6	$16.7	507	339	349	1,195
PBS	$21,447.2	$11,124.1	104,767	45,799	124,343	274,909
Education/Health	$850.1	$457.9	5,474	2,097	5,006	12,577
Leisure	$217.6	$100.9	2,277	609	941	3,827
Other Service	$556.6	$294.1	4,461	2,036	3,362	9,859
Government	$719.9	$386.3	3,915	659	4,144	8,718
Federal Payroll	$12,503.6	$6,709.7	37,676	6,344	39,882	83,902
Total	**$72,124.1**	**$35,500.3**	**254,862**	**221,005**	**377,364**	**853,232**

Effect of BCA of 2011 (DOD FY2012-FY2021)

Sector	Direct Federal Spending Cut ($Million)	Direct Impact ($Million)	Total Impact (Direct+ Ripple) ($Million)	Total GDP (Direct+Ripple) ($Million)
Natural Resource	$53.5	$53.5	$141.9	$83.3
Construction	$2,818.8	$2,818.8	$8,131.1	$4,640.7
Manufacturing	$17,188.9	$17,188.9	$47,463.8	$24,066.2
Trade	$1,735.4	$1,735.4	$4,145.6	$2,763.1
TWU	$1,262.7	$1,262.7	$2,911.0	$1,850.3
Information	$1,533.0	$1,533.0	$3,926.2	$2,327.9
FIRE	$84.8	$84.8	$128.1	$97.6
PBS	$11,809.8	$11,809.8	$32,938.6	$21,447.2
Education/Health	$484.0	$484.0	$1,362.8	$850.1
Leisure	$136.9	$136.9	$360.8	$217.6
Other Service	$320.1	$320.1	$933.3	$556.6
Government	$408.0	$408.0	$971.1	$719.9
Federal Payroll	$5,418.1	$7,087.0	$16,865.8	$12,503.6
Total	**$43,254.0**	**$44,922.9**	**$120,280.3**	**$72,124.1**

Note: Columns and rows may not add up to the totals due to rounding.

Table 9

Effect of Non-DOD Spending Reductions on the National Economy, FY2012-21 Cumulative

	Total GDP (Direct+Ripple)	Labor Income (Direct+Ripple)	Employment Impact			
Sector	($Million)	($Million)	Direct	Indirect	Induced	Total
Natural Resource	$108.4	$48.7	371	435	549	1,354
Construction	$1,643.4	$823.8	7,291	4,750	7,444	19,486
Manufacturing	$3,434.4	$1,561.7	6,274	18,944	20,585	45,803
Trade	$1,518.0	$696.4	10,611	3,094	8,140	21,845
TWU	$568.6	$251.3	2,186	1,590	3,482	7,258
Information	$822.3	$359.6	2,069	2,862	3,633	8,565
FIRE	$558.9	$95.8	2,943	1,967	2,023	6,933
PBS	$16,816.7	$8,722.4	83,294	36,412	98,858	218,565
Education/Health	$1,420.7	$765.3	9,276	3,554	8,482	21,312
Leisure	$67.7	$31.4	718	192	297	1,207
Other Service	$164.9	$87.1	1,340	612	1,010	2,962
Government	$210.8	$113.1	1,162	196	1,230	2,589
Federal Payroll	$49,965.5	$26,812.5	152,658	25,704	161,599	339,960
Total	**$77,300.5**	**$40,369.1**	**280,194**	**100,311**	**317,333**	**697,839**

Effect of BCA of 2011, Non Defense (FY2012-FY2021)

	Direct Federal Spending Cut	Direct Impact	Total Impact (Direct+ Ripple)	Total GDP (Direct+Ripple)
Source	($Million)	($Million)	($Million)	($Million)
Natural Resource	$69.7	$69.7	$184.8	$108.4
Construction	$998.2	$998.2	$2,879.5	$1,643.4
Manufacturing	$2,453.0	$2,453.0	$6,773.4	$3,434.4
Trade	$953.4	$953.4	$2,277.6	$1,518.0
TWU	$388.0	$388.0	$894.6	$568.6
Information	$541.5	$541.5	$1,387.0	$822.3
FIRE	$485.4	$485.4	$733.4	$558.9
PBS	$9,260.0	$9,260.0	$25,827.1	$16,816.7
Education/Health	$808.9	$808.9	$2,277.5	$1,420.7
Leisure	$42.6	$42.6	$112.2	$67.7
Other Service	$94.9	$94.9	$276.6	$164.9
Government	$119.5	$119.5	$284.4	$210.8
Federal Payroll	$21,651.2	$28,320.4	$67,397.1	$49,965.5
Total	$37,866.3	$44,535.4	$111,305.1	$77,300.5

Note: Columns and rows may not add up to the totals due to rounding.

Table 10

Gross State Product (GSP) Impacts of the Budget Control Act of 2011
Fiscal Years 2012 and 2013
(in billions of current year dollars)

State	GSP Losses* DOD Cuts	GSP Losses* Non-DOD Cuts	Total GSP* Losses
Alabama	$2.327	$1.573	$3.900
Alaska	0.510	0.537	1.047
Arizona	3.055	1.892	4.947
Arkansas	0.312	0.608	0.920
California	11.719	10.957	22.676
Colorado	1.598	2.683	4.281
Connecticut	3.140	1.078	4.218
Delaware	0.006	0.215	0.221
District of Columbia	1.314	11.500	12.814
Florida	3.632	4.366	7.998
Georgia	2.393	3.089	5.482
Hawaii	0.680	0.395	1.075
Idaho	0.085	0.969	1.054
Illinois	2.015	3.381	5.396
Indiana	1.296	1.112	2.408
Iowa	0.454	0.664	1.118
Kansas	0.539	0.859	1.398
Kentucky	1.475	1.406	2.881
Louisiana	1.636	1.224	2.860
Maine	0.368	0.363	0.731
Maryland	3.414	8.132	11.546
Massachusetts	3.594	2.491	6.085
Michigan	1.173	1.966	3.139
Minnesota	0.425	1.187	1.612
Mississippi	0.454	0.720	1.174
Missouri	2.913	2.225	5.138
Montana	0.085	0.422	0.507
Nebraska	0.227	0.439	0.666
Nevada	0.368	0.679	1.047
New Hampshire	0.312	0.322	0.634
New Jersey	2.202	2.141	4.343
New Mexico	0.425	2.435	2.860
New York	2.497	4.544	7.041
North Carolina	1.023	1.927	2.950

Table 10 Continued

State	GSP Losses* DOD Cuts	GSP Losses* Non-DOD Cuts	Total GSP* Losses
North Dakota	$0.085	$0.263	$0.348
Ohio	1.845	2.219	4.064
Oklahoma	0.691	0.900	1.591
Oregon	0.255	0.949	1.204
Pennsylvania	3.462	4.428	7.890
Rhode Island	0.227	0.225	0.452
South Carolina	1.277	1.776	3.053
South Dakota	0.170	0.303	0.473
Tennessee	0.879	3.055	3.934
Texas	8.579	7.460	16.039
Utah	0.718	0.894	1.612
Vermont	0.198	0.210	0.408
Virginia	11.804	9.072	20.876
Washington	1.475	2.717	4.192
West Virginia	0.085	0.925	1.010
Wisconsin	2.391	1.285	3.676
Wyoming	0.057	0.223	0.280
Guam	0.189	0.080	0.269
Puerto Rico	0.189	0.338	0.527
Undistributed	2.243	4.701	6.944
Totals	$94.506	$120.502	$215.008

Sources: GMU Center for Regional Analysis; Chmura Economics & Analysis. *Gross state product losses resulting from BCA-mandated federal spending reductions during FY 2012 and FY 2013; excludes impacts from cuts in entitlement programs. Columns and rows may not add up to the totals due to rounding.

Table 11

State Labor Income Impacts of the Budget Control Act of 2011
Fiscal Years 2012 and 2013
(in billions of current year dollars)

State	Income Losses* DOD Cuts	Income Losses* Non-DOD Cuts	Total Income* Losses
Alabama	$1.145	$0.840	$1.985
Alaska	0.251	0.282	0.533
Arizona	1.504	1.014	2.518
Arkansas	0.154	0.314	0.468
California	5.768	5.775	11.543
Colorado	0.787	1.392	2.179
Connecticut	1.546	0.601	2.147
Delaware	0.003	0.110	0.113
District of Columbia	0.647	5.876	6.523
Florida	1.788	2.283	4.071
Georgia	1.178	1.613	2.791
Hawaii	0.335	0.212	0.547
Idaho	0.042	0.494	0.536
Illinois	0.992	1.755	2.747
Indiana	0.638	0.588	1.226
Iowa	0.223	0.346	0.569
Kansas	0.265	0.446	0.711
Kentucky	0.726	0.740	1.466
Louisiana	0.805	0.651	1.456
Maine	0.181	0.191	0.372
Maryland	1.681	4.196	5.877
Massachusetts	1.769	1.328	3.097
Michigan	0.577	1.021	1.598
Minnesota	0.209	0.612	0.821
Mississippi	0.223	0.375	0.598
Missouri	1.434	1.182	2.616
Montana	0.042	0.216	0.258
Nebraska	0.112	0.227	0.339
Nevada	0.181	0.352	0.533
New Hampshire	0.154	0.169	0.323
New Jersey	1.084	1.127	2.211
New Mexico	0.209	1.247	1.456
New York	1.229	2.355	3.584
North Carolina	0.504	0.998	1.502

Table 11 Continued

State	Income Losses* DOD Cuts	Income Losses* Non-DOD Cuts	Total Income* Losses
North Dakota	$0.042	$0.135	$0.177
Ohio	0.908	1.160	2.068
Oklahoma	0.340	0.470	0.810
Oregon	0.126	0.487	0.613
Pennsylvania	1.704	2.313	4.017
Rhode Island	0.112	0.118	0.230
South Carolina	0.628	0.926	1.554
South Dakota	0.084	0.157	0.241
Tennessee	0.433	1.570	2.003
Texas	4.223	3.942	8.165
Utah	0.354	0.467	0.821
Vermont	0.098	0.110	0.208
Virginia	5.810	4.817	10.627
Washington	0.726	1.408	2.134
West Virginia	0.042	0.472	0.514
Wisconsin	1.177	0.695	1.872
Wyoming	0.028	0.114	0.142
Guam	0.093	0.044	0.137
Puerto Rico	0.093	0.175	0.268
Undistributed	1.104	2.431	3.535
Totals	$46.517	$62.937	$109.447

Sources: GMU Center for Regional Analysis; Chmura Economics & Analysis. * Personal earnings lost due to losses of direct and indirect employment resulting from BCA-mandated federal spending reductions during FY 2012 and FY 2013; excludes impacts from cuts in entitlement programs. Columns and rows may not add up to the totals due to rounding.

AEROSPACE INDUSTRIES ASSOCIATION

Marion C. Blakey
President and Chief Executive Officer

June 27, 2012

Mr. Jeffrey Zients
Acting Director
Office of Management and Budget
Executive Office of the President
Washington, D.C. 20503

Dear Mr. Zients:

Thank you for taking the time to meet with us on June 13, 2012 regarding the impact of federal budget sequestration, scheduled to take effect January 2, 2013. We appreciated the thoughtful exchange with you and your staff.

As we discussed, sequestration will have devastating effects on our economy and U.S. national security, and we believe it will result in terrible public policy if it goes into effect. Currently, however, sequestration is the law. Absent intervening action it will become reality in under six months.

Our companies have responsibilities to carefully assess the likely impacts on their businesses and to manage, and where reasonably possible, mitigate the negative consequences. Their abilities to do this effectively, however, are constrained by the significant uncertainties regarding sequestration, including what actions Congress might take and how the executive branch will interpret and apply existing law. Accordingly, clarification and policy guidance on a number of issues discussed during our meeting and highlighted below would be helpful. This will better enable our members to plan and lessen at least some of the impacts of sequestration.

(1) <u>Employee considerations, including those covered under the Worker Adjustment and Retraining Notification (WARN) Act</u>. The WARN Act establishes a general federal requirement for a 60-day advance notice to certain affected employees facing layoffs or facility closures. We are greatly concerned that companies will have to consider issuing a notice to a broad population of their workforce in the October and November timeframe. Specific guidance would be helpful from your office to federal agencies on the allowability of WARN related costs that contractors could incur, as well as any steps agencies should take to mitigate negative impacts.

(2) <u>The scope of funding subject to sequestration</u>. Of particular concern is whether prior year unobligated balances will be included in the resource baseline for defense sequestration and whether military pay accounts will be excluded from the baseline. Including unobligated funds in the baseline would likely result in a larger cut in defense acquisition programs, above and beyond the required across-the-board reduction to the Fiscal Year 2013 base budget.

(3) Level of sequestration application. Important to any planning exercise is an authoritative understanding of whether sequestration will be implemented at the individual "Program, Project, and Activity" (PPA) level or at some higher aggregate level. The PPA approach, which provides the executive agencies with the least amount of discretion, will result in an even more significant number of contract changes that will be difficult to execute in a timely manner, disrupt program execution, and create additional substantial costs to the government. Industry would appreciate clarification from your office on whether this is the approach that will be used.

(4) Contract impacts. We believe that sequestration will result in significant contract changes including Requests for Equitable Adjustment (REAs) and possible program terminations. These actions would represent potentially large and unbudgeted costs to the government. Guidance on how these changes will be implemented is important to understanding the post-sequestration budget and contracting environment.

(5) Approach to new requests for proposals prior to sequestration. The core of this issue is the cost basis of near term proposals that would otherwise assume rate structures for overhead and other expenses that would be in place absent sequestration. We believe clear advance policy guidance on this issue would be beneficial to both the government and industry.

(6) Differing government approaches to sequestration planning/preparation. In the absence of federal-wide guidance, the potential exists for agencies and departments to pursue independent approaches (slow down vs. speed up, etc.) in a 'run-up' to sequestration. Program offices and contracting officers need clear guidance in this area, and that guidance should be shared with industry to facilitate an orderly planning process.

We expect that other issues will arise as we proceed further into our assessment and planning efforts, but at present, the above issues are of most pressing concern.

Thank you again for taking the time to meet with us and your attention to these matters. We look forward to receiving your response and suggested plan of action to address these important concerns. Establishing as much clarity as possible on these and other important questions will help all of us prepare for the very unfortunate possibility of sequestration.

Best regards,

Marion Blakey

Marion C. Blakey

cc: David P. Hess, Chairman, AIA; President, Pratt & Whitney, UTC
Wes Bush, Vice Chairman, AIA; Chairman, CEO & President, Northrop Grumman Corporation
Robert J. Stevens, Former Chairman, AIA; Chairman & CEO, Lockheed Martin Corporation

WITNESS RESPONSES TO QUESTIONS ASKED DURING THE HEARING

JULY 18, 2012

RESPONSES TO QUESTION SUBMITTED BY MR. MCKEON

Mr. STEVENS, Mr. O'KEEFE, and Mr. HESS. In response to Chairman McKeon's request, we have included the recent letter sent by industry to Acting OMB Director Zients (**on page 136**) that details the areas where we need greater information and clarity in order to most effectively manage the industrial base, and with the least disruption, once sequestration is implemented. [See page 41.]

RESPONSES TO QUESTION SUBMITTED BY MR. RYAN

Mr. STEVENS, Mr. O'KEEFE, and Mr. HESS. In response to Congressman Ryan's request, we have enclosed the report of the Defense Industrial Base Task Force that we completed for the Secretary of Defense in November of last year (**on page 103**), and the report recently released by Dr. Stephen Fuller of George Mason University, "The Economic Impact of the Budget Control Act of 2011 on DOD and Non-DOD Agencies" (**on page 111**). These two reports contain detailed information on the industrial and economic impacts of sequestration, which will help your constituents in understanding the negative consequences if this measure goes forward. [See page 36.]

Ms. WILLIAMS. [The information was not available at the time of printing.] [See page 36.]

○