## OFFICE OF MANAGEMENT AND BUDGET

### Office of Federal Procurement Policy

### Value Engineering

**AGENCY:** Office of Federal Procurement Policy, Office of Management and Budget.

**ACTION:** Notice of Final Revision to Office of Management and Budget Circular No. A–131, ''Value Engineering''.

**SUMMARY:** The Office of Federal Procurement Policy (OFPP) in the Office of Management and Budget (OMB) is publishing final revisions to OMB Circular A–131, Value Engineering, to update and reinforce policies associated with the consideration and use of value engineering (VE). VE is a well-established commercial practice for cutting waste and inefficiency that can help Federal agencies reduce program and acquisition costs, improve the quality and timeliness of performance, and take greater advantage of innovation to meet 21st century expectations and demands. The revisions are designed to ensure that the Federal Government has the capabilities and tools to consider the use of VE for new and ongoing projects, whenever appropriate.

**FOR FURTHER INFORMATION CONTACT:** Curtina Smith, OFPP, *csmith@omb.eop.gov.*

**SUPPLEMENTARY INFORMATION:**

### A. Overview

VE refers to an organized effort to analyze functions of systems, equipment, facilities, services, and supplies for the purpose of achieving an agency's essential functions at the lowest life-cycle cost, consistent with required levels of performance, reliability, quality, and safety. VE challenges agencies to continually think about their mission and functions—in the most basic terms—in order to determine if their requirements are properly defined and if they have considered the broadest possible range of alternatives to optimize value. It promotes ''share-in-savings'' by encouraging contract holders to identify ways to reduce the cost of performance on existing contracts and share with the government in the savings produced from the results. Most importantly, VE enables agencies to achieve greater fiscal responsibility and operate within tighter budgetary constraints. By identifying and eliminating unnecessary program and acquisition costs that do not contribute to the value, function, and performance of the product or service, VE can permit programs to continue delivering the same, or an even higher, level of service for less money—a critical capability for managing in a fiscally austere environment.

Industry first developed VE during World War II as a means of continuing production, despite shortages of critical materials and labor, by analyzing functions to generate alternative materials or systems to accomplish the required tasks at a lower cost. The Federal Government subsequently adopted this tool as a mechanism to incentivize contractors to continually think of ways to drive greater efficiency in their production methodologies by allowing them to share with the Government in the savings generated by their value engineering change proposals.

Over the past several decades, a number of agencies have successfully integrated the use of VE analysis into their management activities. These agencies have reported life-cycle savings through the use of VE in a broad range of acquisition programs, including those involving defense systems, civil works, transportation, construction, engineering, environmental, and manufacturing projects. According to recent reports of VE activities submitted to OMB, VE has generated billions of dollars in savings and cost avoidance. For example, the Department of Defense (DOD) reported cumulative savings of over $10 billion in FYs 2011 and 2012. The Department of Transportation's Federal Highway Administration reports that annual savings for Federally-funded state construction projects have ranged from just over $1 billion to nearly $2 billion between FYs 2010 and 2012. The Department of State reports that it has used VE to identify hundreds of millions of dollars in total life cycle savings since FY 2008—saving well over $40 for every one dollar invested in VE studies.

In 1988, OMB issued Circular A–131 to help agencies in their efforts to establish and improve VE programs so that they realize the benefits of using VE techniques to reduce nonessential contract and program costs. See 53 FR 3140. The Circular was revised in 1993 to require the use of VE as a management tool. See 58 FR 31056. OMB's Office of Federal Procurement Policy issued a series of memoranda in the 1990s to remind agencies of their responsibilities under the program.

Despite the demonstrated ability of VE to facilitate more fiscally responsible management and smarter buying, and its continued popularity in the private sector, Federal agency use of VE has waned in recent years. Insufficient management attention and questions about its applicability to performance based contracting and other buying practices have resulted in VE not being considered in situations where it could have helped agencies save resources. The revisions being made to the Circular are designed to clarify the role of VE in helping agencies meet twenty-first century demands and deliver better value to the taxpayer.

### B. Circular Revisions

On June 8, 2012, OMB's OFPP issued a notice in the **Federal Register** of proposed changes to Circular A–131 (See 77 FR 34073, available at *http://www.whitehouse.gov/sites/default/files/omb/procurement/a131-circular-changes-draft.pdf*), which proposed revisions that would:

- Reflect present-day buying strategies and practices by explaining that VE can be used with other management improvement tools, such as lean six sigma, and clarifying that consideration of VE should not exclude services, such as those acquired with performance-based specifications, and construction, including projects where design-build methods are used;
- Adjust the threshold for considering the application of VE, primarily to take into account inflation;
- Reduce the number of projects on which agencies are required to report to OMB, update the reporting format to include a description of the methodology used to calculate savings, and eliminate requirements for a detailed cost summary of program results from inception to date; and
- Remove the provision from the current Circular requiring agency IGs to conduct an automatic audit of VE programs every two years, instead allowing agency management to work with their IGs to consider when review of VE activities may be warranted and relying on review of agency VE programs to be considered over time through internal control assessments of acquisition functions conducted in connection with OMB Circular A–123, *Management Accountability and Control.*

As a result of public comments (discussed below) and discussion with Federal agencies, OFPP is finalizing the proposed Circular with certain changes and additional refinements. Specifically, these changes and refinements to the Circular, which largely address matters relating to scope, agency responsibilities, and application, include:

- Establishing a definition of ''value engineering study'' for purposes of the Circular to recognize that VE may be tailored and scaled based on factors such as the cost or complexity of the project, the stage in the project lifecycle, and project schedule.

- Clarifying that VE is a process generally performed in a workshop environment by a multidisciplinary team of contractor and/or in-house agency personnel (such as an integrated project team (IPT)), which is facilitated by agency or contractor staff that is experienced, trained and/or certified in leading VE teams through a series of specific phases.
- Directing agencies subject to the Chief Financial Officers Act (CFO Act) to identify a senior accountable official responsible for ensuring the appropriate consideration and use of VE, including maintaining agency guidelines and procedures for identifying agency programs and projects with the most potential to yield savings from VE studies and reporting results to OMB.
- Requiring CFO Act agencies to maintain guidelines and procedures for identifying programs and projects with the most potential to yield savings from VE studies.
- For new projects and programs, increasing the threshold for considering VE from $1 million to $5 million, to recognize that the application of VE has the greatest value early in the investment lifecycle on high dollar programs and projects.
- For existing projects and programs, granting to agencies the discretion to determine the extent to which VE shall be applied, but requiring agencies to establish criteria to help agency managers determine when VE may be suitable.
- Clarifying that documentation must be maintained to explain the basis of waivers and, where VE studies are conducted, the reason for not implementing recommendations made in the studies.
- Emphasizing that VE can also be used with acquisition and commodity management techniques, such as strategic sourcing and modular contracting, to improve performance and quality, lower cost, manage risks more effectively, and shorten project delivery.

The complete text for the final revised OMB Circular A–131, ''Value Engineering'' is available on the OMB Web site at *http://www.whitehouse.gov/omb/circulars_a131/.*

**C. Public Comments**

In response to its June 8, 2012 notice of proposed changes to Circular A–131, OFPP received public comments from thirteen respondents, including a number of comments expressing support for the renewed attention on this management tool. Copies of the public comments received are available for review at *http://www.regulations.gov/#!docketDetail;D=OFPP-2012-0002.* A short summary of the comments and OFPP's responses and changes adopted in the final revised Circular are described below:

1. *Applicability.* Several respondents commented on the applicability of the Circular's policy. Specifically, concern was raised that the requirement for agencies to use VE ''where appropriate'' is too vague and should be clarified.

OFPP seeks to focus the application of VE where it is likely to have the greatest value while allowing agencies to tailor the use of the tool to meet their mission needs. To clarify this goal, the final Circular requires VE for all new agency projects and programs if the project cost estimate is at least $5 million, except where the agency expressly waives the requirement. This threshold (which is substantially higher than the $1 million threshold in the current version of the Circular) recognizes that VE generally has the greatest impact when it is applied early in the investment lifecycle to higher dollar programs and projects. That said, agencies are encouraged to establish a lower threshold for their agency, as appropriate, after taking into account: (i) The historical costs of their major acquisitions, (ii) projects that have a significant impact on lifecycle costs or agency operations, and (iii) projects with a significant potential for repeat savings, such as manufacturing projects where savings can be applied to future units produced.

The final Circular gives agencies discretion to determine the extent to which VE shall be applied to existing programs and projects, but requires agencies to establish criteria to help agency managers determine when VE may be suitable. Criteria might include a combination of factors such as the priority of the program or project to the agency and the presence of cost overruns, performance shortfalls and/or schedule delays.

Furthermore, the final Circular requires CFO Act agencies to designate a senior accountable official to strengthen accountability for the meaningful consideration of VE. This official's responsibilities include (i) maintaining agency guidelines and procedures, (ii) making training available for program, project, acquisition, information technology, and other agency personnel, (iii) developing plans for using VE and ensuring that funds necessary for conducting agency VE studies are identified and included in annual budget requests to OMB, and (iv) making sure VE activities are appropriately documented and results are reported to OMB.

2. *Measurement of net life-cycle cost savings.* One respondent stated that coverage in the proposed revisions discussing how to measure the net life-cycle cost savings from value engineering, conflicts with the Federal Acquisition Regulation (FAR) clause 52.248–1(b) ''Government costs,'' which states that the term does not include the normal administrative cost of processing the Value Engineering Change Proposal (VECP). The respondent stated that the Circular should be revised to include administrative costs in the overall life-cycle cost within the context of executing the value engineering function at the agency level.

OFPP has revised the wording of the final Circular to clarify that the net life-cycle cost savings from value engineering is determined by subtracting the Government's cost (including administrative costs of processing VECPs that were excluded in calculating VECP saving shares) of performing the value engineering function over the life of the program from life-cycle savings generated by value engineering function.

3. *Coverage in the FAR.* One respondent stated that the current coverage of VE in the FAR is complex and should be updated to (1) reflect a more streamlined and user-friendly approach to the value engineering change proposal process, (2) encourage broader application of VE in situations where use of VE could save money and allow both parties to share in the savings.

OFPP agrees that successful use of VE requires that application to Federal contracts be clear and practical to use. OFPP intends to work with FAR Council members to consider potential regulatory revisions that might help to simplify its application in Federal acquisition. It also intends to work with the Federal Acquisition Institute and the Defense Acquisition University on appropriate training materials for the acquisition workforce.

**Joseph G. Jordan,**

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