

**Partnered Government:  
The Whole is Greater than the Sum of the Parts**

by

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The Center for Public Policy and Private Enterprise, in the University of Maryland School of Public Policy, provides the strategic linkage between the public and private sector to develop and improve solutions to increasingly complex problems associated with the delivery of public services—a responsibility increasingly required to be shared by both sectors. Operating at the nexus of public and private interests, the Center researches, develops, and promotes best practices; develops policy recommendations; and strives to influence senior decision-makers toward improved government and industry results.

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## **Executive Summary**

The 21st century has ushered in a series of major challenges for our country. The list is staggering, and includes, most importantly, national security; but the other challenges are near equal in importance: health care, energy, environment, education, aging infrastructure, and the fiscal crisis, to name a few. Most, if not all, of these challenges are complex and largely open-ended. In order to respond to these challenges, federal agencies will need to create solutions, often in areas generally unfamiliar to public entities. As a result, federal agencies will need to partner with private and non-profit entities to develop and manage these solutions, and to provide the resultant services – with, of course, the government in the management and oversight role (as the ultimately responsible party, but with significant support from the private and non-profit sectors). Much of the government’s work is already done through this type of partnering.

“Partnered government” is a broad term we use to refer to this joining up of different government agencies with one another, as well as with the private sector and non-profit sector. These relationships are based on a shared set of goals and objectives that give direction to member activities. They also have a shared “worldview” and awareness, that allows them to see the dynamic external environment in a consistent manner and better respond to challenges as they arise. This report is concerned with the partnering of the public and private sectors within the federal government, with a particular focus on the Department of Defense.

An appreciation of the current environment is helpful in understanding the need for greater and more effective partnered government. Significant factors influencing the environment include: rapidly changing information technology, which has altered the nature of work and significantly increased productivity in world-class commercial firms and in federal agencies; domestic economic constraints that will limit federal discretionary spending, including defense appropriations; national demographics (specifically, the aging workforce), and their impacts on the DoD and federal workforce; and the increased reliance on private firms to provide support to the military (even in war zones – for example, today there are over 200,000 contractors involved in Iraq and Afghanistan).

When faced with these changes, one is inclined to ask “what is the proper role of government?” The federal government has had a long-stated policy that the government will not produce

products or provide services that are available in the private sector. However, the American public has increasingly asked government at all levels to provide more and more services, which, in many cases were historically provided solely by government employees. Beginning in the 1980's, the assumption that implementation of government services must be carried out by government workers, has been increasingly questioned. Local governments and federal agencies competed services between the current government employees and the private sector; and in some cases the work was simply privatized by letting private companies bid for the government capital equipment and the performance of the work (and, in many cases, the employees affected moved to the private sector). These local government initiatives resulted in cost savings ranging from 20 percent to 60 percent. This initiative was also adopted at the federal level, with equally dramatic results—savings averaging approximately 30 percent; with, in many cases, significant performance improvements.

In most cases, the government's role has shifted from being "the provider of goods and services" to becoming the "manager of the provider of goods and services." Government employees should continue to perform those tasks identified as "inherently governmental" tasks. However, non-inherently governmental tasks should be competitively awarded – with the government selected to do those tasks that it can do more efficiently and effectively than the private sector counterparts. This shift allows for the greatest synergism of commerce and government.

To further examine these issues, the Center for Public Policy and Private Enterprise at the University of Maryland's School of Public Policy hosted a Thought Leadership Forum, April 1-3 2009, entitled "Partnered Government: The Whole is Greater than the Sum of the Parts," supported by the CGI Initiative on Collaborative Government. The forum output highlighted key lessons learned from the presentations, the case studies, and participants experiences; and concluded with strategies and potential future public policy actions recommended by the forum participants in order to improve the operation of government programs through more effective partnering, (primarily with private sector firms, but also with nonprofit organizations and other government agencies). The forum participants developed the following recommendations, which we have placed into the three critical categories for successful partnering: "Creating an Environment that Facilitates Partnered Government," "Competition Creates Good Partners," and "Implementing Partnered Government."

## **Box -- Recommendations**

### **Creating an Environment that Facilitates Partnered Government**

#### **OMB Should:**

- *Identify Inherently-Governmental Functions*

#### **Department and Agency heads should:**

- *Identify “critical positions” that need to be performed by government personnel*
- *Develop new approaches to Eliminate Organizational Conflicts-of-interest and Personal Conflicts-of-interest*
- *Develop the Required Human Capital*

#### **OPM should:**

- *Improve the Hiring Process*

### **Competition Creates Good Partners**

#### **Department and Agency heads should:**

- *Reduce Barriers-to-Entry*
  - *Enforcing policies limiting use of government-unique standards, specifications and certifications.*
  - *Keeping systems “open” – eliminate proprietary architectures and interfaces.*
  - *Expanding the use of non-traditional contracting authorities.*
- *Ensure Competitiveness at the Prime Level and Sub-Tier Levels by expanding the use of competitive dual-sources*
- *Where Possible Reduce the Government Monopoly*

### **Implementing Partnered Government**

#### **Department and Agency heads should:**

- *Change the culture to make effective partnering a top management priority*
- *Develop a Process to Build Partnering Relationships*
- *Ensure consistent program leadership by maintaining stability of key personnel*

## **Program Leadership Should:**

- *Develop and maintain communications to build trust between government representatives and contractors.*
- *Where possible co-locate public-private teams*
- *Identifying the appropriate contract type*
- *Develop appropriate metrics and incentives for both the public and private sector organizations*

# I. Introduction

The 21st century has ushered in a series of major challenges for our country. The list is staggering, and includes, most importantly, national security (and more holistically defined e.g. including homeland security, pandemics, etc.), but the other challenges are near equal in importance; health care, energy, environment, education, aging infrastructure, and the fiscal crisis, to name a few. The Obama Administration is developing strategies to cope with these, and the public is generally supportive, with a hope that these initiatives will be successful. As a result, however we can anticipate that the government, as it has during other periods of crisis, will be asked to provide more services. This growth in responsibility has resulted in increasing levels of federal spending. Consequently, federal government expenditures, as a percent of the gross domestic product (GDP), have grown from approximately 8 percent in 1900, to approximately 36 percent through most of this decade. When the response to the current financial crisis is included, expenditures are expected to exceed 45 percent of the gross domestic product in 2009.<sup>1</sup>

Most, if not all, of the major challenges the federal government faces are complex and largely open-ended. Federal agencies will need to adjust their missions and transform their operations--especially with the growing budgetary constraints. They also will need to create solutions by thinking outside of the box, generally unfamiliar territory to public entities. Government agencies are often unable to tackle these problems with in-house resources, and will need to partner with private and non-profit entities to successfully address them.

As a result of the growth in responsibility, much of the government's work already is done through this type of partnering. These relationships have been described as "...a complex set of episodic and ongoing relationships among an array of public, private, and non-profit organizations, each playing a specialized role in implementing public policy. Some of these relationships are formal and contractual and some are not."<sup>2</sup> In public- private relationships, "partnering" allows government agencies and departments to leverage the technical expertise, efficiency, and cost-saving practices of the private sector. In many cases, the private sector has a greater variety and number of technical experts, and is generally more efficient in the management of the production of goods and services (and can often provide

them more effectively than can government agencies – primarily because the private sector is operating in a competitive market environment).

Partnered government is further characterized by a shared set of goals and objectives that give direction to member activities. They also have a shared “worldview” and awareness, that allows them to see the dynamic external environment in a consistent manner and better respond to challenges as they arise.<sup>3</sup> These relationships, based on improved communication, will also have a greater likelihood of knowledge creation, as well as developing innovative solutions. With Partnered government, the public and private sectors can draw on each others’ strengths and minimize their weaknesses. In order to gain the most effectiveness, we believe these relationships must take place in a competitive environment; otherwise there is a lack of incentives to achieve the desired high level of service performance, with increased efficiency.

Furthermore, most current public-private relationships are governed by formal contracts. As these programs become larger, the contracts often have greater specificity of each party’s obligations and responsibilities, frequently making it difficult to develop appropriate measures of productivity. Technical uncertainty, caused by rapidly changing technology creates yet another challenge. These factors encourage more complex contracts, which the government hopes will result in the required outcomes; but, generally increase transaction costs, and often do not perform as desired. In fact, these complex contracts may actually signal distrust, and encourage opportunistic conduct, which often leads to adversarial attitudes and behavior.<sup>4</sup>

With partnered government, we envision increasing the focus on the attributes of relationally-governed transactions; these transactions are dependent on social relationships and processes (which are built on mutual trust and commitment), and have been shown to promote the desired norms of flexibility (adapting to changing circumstances), solidarity (promoting a bilateral approach to solving problems), and information exchange (a willingness to share information). And, although formal contracts and relational exchanges have been considered as substitutes, some have argued that they are in fact complimentary.<sup>5</sup> We believe when managers couple their necessary formal contracts with increased levels of

relational governance, they can reduce their transaction costs and improve their partnering outcomes.

It is also important to note that Partnered government is not limited to public-private ventures. Partnered Government can also occur between entities *solely within* the public and non-public sectors. With public-public relationships, partnering enhances efficiency by breaking down the traditional vertical and horizontal barriers established by federalism and bureaucratic organizational behavior.<sup>6</sup> Similar efforts have taken place within the non-public sector as well.<sup>7</sup>

This report is concerned with the partnering of public and private sectors within the federal government, with a particular focus on the Department of Defense. The Department of Defense (DoD) is one of the largest and most complex organizations in the world. DoD's budget dwarfs that of the world's largest corporations, it employs millions of people that operate worldwide. It is in the process of transforming its force structure, as well it all of its business systems, while simultaneously conducting global military operations. It faces the same general, as well as some unique, environmental, workforce, structural and cultural challenges (which will be discussed in greater detail in the next section). DoD will need to exploit all the benefits of partnered government to effectively respond to these challenges. However, we believe the report's findings are applicable to all government agencies.

## **II. Wye River Thought Leadership Forum**

The Center for Public Policy and Private Enterprise at the University of Maryland's School of Public Policy hosted a Thought Leadership Forum, on April 1-3 2009; entitled "Partnered Government: The Whole is Greater than the Sum of the Parts." The Forum, funded through a grant from CGI Initiative on Collaborative Government, was held at the Aspen Institute's Wye River Conference Center on the Eastern Shore of Maryland. The Forum brought together 21 senior government officials, business leaders (from a range of federal government organizations and private sector firms of various functions and sizes) and academics. The list of attendees is presented in Appendix II.

The purpose of the Forum was to examine the challenges to effective partnering and develop recommendations so that government partnering can simultaneously achieve maximum effectiveness, efficiency, transparency and accountability. Our goal was to facilitate serious discussion and examine the issues surrounding partnered government. The Forum included presentations on three case studies to specifically identify challenges, barriers, and valuable lessons that would help in the formulation of our findings and recommendations.

The Forum began with an introductory presentation by the Honorable Jacques S. Gansler, former Under Secretary of Defense (Acquisition, Technology & Logistics). Dr. Gansler reviewed national security and financial challenges the nation will continue to face, and how they create a particularly demanding environment (see the summary in the Appendix) for many government programs. In the face of these challenges, DoD, and all government agencies, must increasingly strive to deliver higher performance with increased efficiency. To accomplish this, DoD must leverage all available expertise within government, private industry, and academia. Many programs already partner extensively with other organizations, but in many cases this often creates new management challenges, and often faces organizational, cultural, and regulatory barriers.

Then three case studies were presented (see the summaries in the insets):

- U.S. Army Logistics Modernization Program (LMP),

- Defense Logistics Agency's Business Systems Modernization (BSM) Program, and the
- DoD Business Transformation Agency (BTA).

These cases were followed by Shay Assad Director of the Defense Procurement Acquisition Policy and Strategic Sourcing, who presented the OSD perspective and Stan Soloway (President and CEO of the Professional Services Council) highlighted four keys to partnering.

Forum participants recognized that government today is executed through an ever-widening network of public and private providers, and concluded that partnered government is necessary. Contractors long have played an integral role in the development of equipment and systems in response to the government's often-unique needs, as well as the delivery of more routine support services; such as building maintenance, food service, and information technology services. They are, however, increasingly being asked to perform tasks that impact billions of dollars in spending; such as supporting the acquisition of DoD's major weapon systems, or performing complex systems engineering tasks. Contractor personnel frequently work side-by-side with federal employees on many of the same mission-critical tasks. This is based not only the environmental factors discussed earlier in the report, but the strengths, weaknesses and other characteristics of public and private entities that include: a lack of critical expertise among public servants; contractors' greater agility and flexibility compared to government employees; and ceilings on the authorized number of public employees, which often preclude hiring the number of employees required.

This report highlights key lessons learned from the forum and case studies. It also includes strategies and potential public policy actions recommended by the Forum participants to improve the operation of government programs through more effective partnering. Although the focus of partnering is meant to be between private sector and public entities, the lessons drawn from the discussions and case studies can be applied to collaboration with nonprofit organizations and among government agencies.

***Case Study One:  
U.S. Army Logistics Modernization Program***

The conflicts of the early 1990s revealed the fundamental weaknesses of the Army's outdated logistics information technology systems. In order to address these problems, the Army has undertaken an aggressive, multi-program effort aimed at adopting best business practices. The Logistics Modernization Program (LMP) is the U.S. Army's principal initiative to modernize their logistics information systems and transform their acquisition and inventory management processes. LMP is accomplishing these goals by replacing the Army's 30-year old in-house legacy systems, the Commodity Command Standard System (CCSS) and the Standard Depot System (SDS), with an Enterprise Resource Planning (ERP) system that utilizes the private industry's best business practices. On December 29, 1999, the Army awarded a ten-year \$680 M contract to maintain the legacy systems while developing and implementing the new ERP system. In early 2003, the contract was extended for two more years to address additional program requirements.

The first of LMP's four deployments occurred on July 7, 2003. Although LMP exhibited superior performance, the system encountered numerous problems. In mid 2006, the Army instituted a yearlong strategic pause to address these problems.

During this time, the Army made several key changes to LMP. First, command of the program was transferred to the Army's Program Executive Office for Enterprise Information Systems (PEO EIS), an organization with more experience with ERP implementation and service contracting. The PEO EIS established a new centralized leadership structure and altered the end-user and middle management training program. Second, LMP's new leadership altered the existing contract structure to allow for greater flexibility in funding research, development and testing projects. Third and finally, the Army made an aggressive effort to gain compliance with several federal regulations that had eluded program managers during the first deployment of LMP.

With the necessary programmatic changes made and the strategic pause lifted, the Army is now preparing for the remainder of its other deployments. The second phase of implementation occurred in March 2009. The remaining two deployments are tentatively scheduled for December 2009 and September 2010. Once the fourth deployment is fully integrated, the LMP will achieve its full operating capability.

Currently, LMP is deployed at 14 locations nationwide with approximately 4,300 users while operating at 80% total functionality. After fourth and final deployment in 2010, LMP will extend across 104 locations with 22,000 users. The program will manage over \$40 Billion in goods and services, and process over 100,000 transactions daily. At 100% functionality, LMP will be one of the world's largest, most complex ERP systems in operation.

Several lessons were learned from LMP's development. They include:

- developing better communication;
- preparing for significant cultural resistance;
- developing relevant employee education to effectively work in the new ERP environment;
- assigning the proper office to manage the LMP;
- preventing unnecessary system software customization to ensure seamless information flow;
- selecting the proper kind of contract structure for both effectiveness and flexibility; and
- establishing proper communication and unified strategic vision between public and private entities.

## **A. Creating an Environment that Facilitates Partnered Government**

The federal government partners with contractors to provide a wide range of services; partnerships can be formed at many levels and take many different forms. Some of these services can include basic services, such as custodial, building maintenance, and landscaping; administrative services; and, in many cases, complex professional management and information technology services. These latter services can closely support governmental functions, such as engineering services to develop specification, integrating automated systems, procurement planning, or assistance with budget preparation. Some of these closely support inherently-governmental functions, which are not always consistently interpreted.

Forum participants recognized that successful management of the partnered government interface is critical to successful performance of most government functions. More and more products and services that have traditionally been provided by the government are now being contracted to the private sector, with government employees managing these contracts. In many cases, the role of the government has shifted from being the “doer” to being the “manager of the doers.” However, there are still many government employees performing functions that are “inherently governmental;” all Forum participants agreed that these functions need to be more clearly and unambiguously defined, and, and of course, must be performed by government employees.

In addition to clarifying the definition of “inherently governmental” functions, participants identified a need to address conflicts-of-interest issues. The resultant forum discussions about how to avoid conflicts-of-interest were lively and identified several strategies. For examples, conflicts-of-interest may arise when contractors support key mission-critical tasks that have the potential to influence government decisions at the front end of the acquisition process, such as, examining alternative ways to acquire desired capabilities; they sometimes help interpreting requirements, and assist in the design and evaluation of requests for proposals, as well as assisting in evaluating the responses to those proposals. During an acquisition, contractor employees often recommend actions to program offices to correct other contractors’ performance problems, and sometime they are asked to analyze other

contractors' cost, schedule, and performance data. These activities present an opportunity for conflicts-of-interest.

### **Conflicts-of-Interest**

Two types of conflicts were discussed.

- **Organizational conflicts-of-interest (OCI)** occur when a contractor has an interest that might bias the firm's judgment (for example, when selecting a sub-contractor), or create an unfair competitive advantage because of impaired objectivity (which can arise when the work involves evaluation), unequal access to information, or biased ground rules. Participants discussed the case of a consulting company that was on contract to a government program office, and simultaneously was a subcontractor to the system developer. Although the consulting firm had established a "firewall," between their two teams, there was still an appearance of organizational conflict-of-interest.
- **Personal conflicts-of-interest (PCI)** occur when actions are influenced by a desire for personal gain. Conflicts-of-interest among government employees have always been a concern. With the growing role of contractors in DoD's work environment, policy makers recognized the need to create policies that address potential conflicts-of-interests with and among contractors. Contractor employees often work inside DOD facilities, alongside DOD employees, creating a multi-sector workforce. However the personal conflict-of-interest policies in place for government employees generally do not apply to the contractor employees.

The Department of Defense has taken some action to address the concerns of contractor conflict-of-interest. The 2007 National Defense Authorization Act (NDAA) required DoD to convene a panel of senior leaders representing a cross section of the Department to eliminate areas of vulnerability of the defense contracting system that allow fraud, waste, and abuse to occur.<sup>8</sup> The panel, so far, has released two annual reports, and continues to review current practices that seek to ensure contracting integrity, and make recommendations for improvement.<sup>9</sup> The issue was also specifically addressed by the Weapons System Acquisition

Reform Act of 2009 (see inset for a description of the Act). The full effect of this legislation is still unknown.

Apparent conflicts-of-interest, especially as it relates to the expenditure of taxpayer dollars, can undermine the public's confidence in individuals, corporations and government organizations. The participants concluded that conflicts-of-interest policy must recognize the increasing integration of the government's workforce. Moreover, the threshold for conflict, which should intuitively be higher for a large company, is not necessarily true, since large companies are closely watched by public investors (i.e., "Wall Street") and the press. Smaller firms working on smaller contracts should also receive adequate oversight and application of OCI/PCI policy. . Participants concluded that managing these OCI/PCIs must be a joint responsibility of the government, along with its industry partners.

## **Human Capital**

One of the most important challenges that the government faces is related to developing the human capital necessary for a future work environment that is conducive to partnered government. The discussion focused on several human capital challenges faced by the federal government, in general, and by DoD specifically. These challenges stem from a combination of demographic changes and skills gaps, that both drive the need for, and affect the implementation of, partnered government. During the last decade there were major reductions in total numbers of government employees, but these reductions were made without focusing on the makeup of the workforce. The DoD acquisition workforce, in particular, remains under-resourced, under-manned, and under-supported. Moreover, the government is also faced with over 30 percent of its employees from the "baby boomer generation" being eligible to retire within the next 5 years. These trends are creating the need for the federal government institutions, especially DoD, to improve hiring practices in order to overcome demographic challenges, and to facilitate partnered government.

Forum participants identified several other human capital challenges that must be addressed to improve the government's ability to effectively partner with the private sector. Based on technological changes, the existing workforce doesn't have the required mix of knowledge, skills, training and experience. For example, the private sector is well ahead of the

government in developing integrated and extended enterprise management systems. As a result, most of the people with the requisite expertise and experience for the development of these enterprise systems are in the private sector. However the government's personnel system does not have the ability to quickly bring in functional experts from the private sector, nor compensate them at levels comparable to the private sector, in most cases.

## **Recommendations**

### **OMB Should:**

#### ***Recommendation One: Identify Inherently-Governmental Functions***

Currently, the guidance on identifying “inherently-governmental” tasks is fairly broad, and as a result, inconsistently interpreted. Clear guidance must be provided to Departments and Agencies so they can unambiguously identify those individuals performing the narrow band of work that is truly “inherently governmental.” After identifying the commercial activities that are performed by civilian employees or military services members that are not inherently government or mission critical, the government should take the necessary steps to introduce competition from private firms. It is clear from all of the available data that when competition is introduced, government service improves, and costs generally decrease significantly – no matter whether the winner is in the public or private sector.<sup>10</sup> While the key is shifting from a monopoly to a competitive environment, the goal must always be to get better performance at a lower cost.

### **Department and Agency heads should:**

#### ***Recommendation Two: Identify “critical positions” that need to be performed by government personnel***

In addition to those positions that are identified as “inherently governmental,” Departments and Agencies need to identify other “critical positions” that must be filled by government personnel to help ensure achievement of the required outcomes. These are a small number of experts providing critical evaluations and advice on issues driving contractor-supported programs. This is particularly important for services, such as management and professional

support, studies and analyses, and systems engineering and technical support. Government officials must always be able to make sound judgments on what the requirements should be, the estimated costs, and whether the contractor is performing according to requirements. Given the expanding role that contractors play in the government workforce, government employees should receive periodic training in the preceding competencies.

***Recommendation Three: Develop new approaches to Eliminate Organizational Conflicts-of-interest and Personal Conflicts-of-interest***

Organizational Conflicts-of-interest (OCI) policy must recognize the increasing integration of the economy, with ongoing government need for contractors that can provide independent, objective advice and support. Consequently OCI management and due diligence must be a central part of acquisition planning and cannot be left to arbitrary policies of avoidance. Vertical integration, however, has virtually eliminated firms that are not a part of a major developer/integrator. New approaches, such as using companies not part of the historical defense contracting community **or** the creative use of limited liability company (LLC) and/or proxy structures (to create independent entities that can provide that service) must be implemented. Furthermore, the government should be “involved” with a program’s prime contractor, to ensure the selection of the most appropriate sub-contractors.

Congress recently passed defense acquisition reform legislation that included steps to prevent OCI. The guidelines established by the Panel on Contracting Integrity to reduce OCIs should be tailored to various government departments and implemented immediately.

Contractors can potentially have significant influence over many government program decisions. Those individuals should be subject to the same PCI policy as government employees, which cover areas such as: their stock holdings, spouse employment, and gifts. DoD should develop a consistent policy for contractors for personal conflict-of-interest. And then require the selected contractor to enforce the policy.

***Recommendation Four: Develop the Required Human Capital***

Strong program management and partnering require a fresh, strategic approach to human capital. Government agencies need to rethink and retool current organizational and personnel

planning to adjust to a networked environment. Without developing staff capabilities, government agencies will not be in position to get the most out of their partnering relationship. Government organizations need to identify the critical business and technical skills required to effectively operate in this new environment. They need to prioritize workforce resources and development strategies to ensure they can fill the inherently-governmental and critical positions. Although currently there is a great deal of attention on contracting officers, there may be an even bigger challenge in related disciplines, where talent supply is limited across the economy, such as engineering, systems engineering, and program management. Care should be taken, however, not to impose hiring quotas on organizations, which could result in a focus on quantity, as opposed to quality (managers must be careful not hire individual at grades and salaries higher than their experience warrants). Finally, agencies should provide their subordinate organizations the maximum flexibility to manage their workforce in a manner consistent with their particular mission.

## **OPM should:**

### ***Recommendation Five: Improve the Hiring Process***

Based on the demographics of the federal workforce, the Federal Government expects to lose a significant portion of its workforce to retirement. The Government's ability to replace lost skills and experience will depend on its ability to efficiently and effectively recruit, hire, and retain high-performing employees. The current Federal hiring system is a cumbersome process, making recruiting and hiring new employees time consuming. This is often exacerbated by time required to obtain a security clearance, once an employee is hired. As a result many applicants get frustrated, give up and seek employment elsewhere. Efforts to improve the federal government's hiring process must be accelerated.

Recently the OMB and OPM issued important policy memos seeking to reform and streamline the federal hiring process. The Memos focused on several key areas including:

- reducing hiring time,
- simplified language on applications,

- informing job candidates of their status
- increasing involvement of hiring managers in all important parts of the hiring process.<sup>11</sup>

We recommend that OPM and OMB implement these reforms immediately.

***Case Study Two:  
DLA's Business Systems Modernization***

The Defense Logistics Agency (DLA) is DOD's largest combat support agency; it manages a supply chain that in 2008 provided \$42 Billion in sales and services. Beginning in 1998 DLA decided to radically overhaul its COBOL-based IT system and business processes, implementing an ambitious transformation effort called the Business Systems Modernization (BSM) program.

BSM's overall goal was to move DLA into a lean, agile, proactive, and integrated operation; capable of quickly meeting warfighter needs, improve the Agency's performance through better processes and business arrangements, while ensuring a diverse, enabled, empowered, and motivated workforce that delivers and sustains supply chain excellence. This meant changing both the agency's underlying business practices and philosophy, and its IT system. In order to move forward on BSM's transformation, the DLA decided to partner with a private firm with experience in IT system integration. On August 10, 2000, after an extensive competition, DLA signed a contract for the project.<sup>1</sup>

In order to achieve the desired goal, DLA and its partners had to overcome several challenges. First was to deal with cultural changes—DLA was transforming from stove-piped functions to enterprise-wide processes, incorporating best practices via Commercial off-the-Shelf and Government off-the-Shelf based tools, and replacing the 35-year old Material Management Systems, with its embedded processes. Second, BSM was much more than a new software system, and significantly impacted the roles of thousands of employees. Users of the new ERP program needed training before and after gaining access to the new system, as part of an extensive training program that included classroom and computer-based activities.<sup>1</sup> These training programs helped achieve buy-in from the thousands of affected employees, and contributed to a smooth transition to the new ERP.

The new supply chain management system provided many tangible benefits to the warfighter; including improved materiel availability, reduced customer wait time, reduced cost and improved data integrity.<sup>1</sup> The logistics response time for items managed within BSM has improved approximately 16%, and the time from receipt of requisitions to Materiel Release Order has been reduced from hours to minutes.<sup>1</sup> Additionally, the system will pay for itself with cost savings by the end of 2009, and will finally allow the agency to pass a proper financial audit.

Although DLA BSM is a business system designed for one specific agency within DOD, there are many lessons that can be drawn from this ERP implementation. First, top leadership support and involvement in all aspects of the program are critical for success. Another major lesson learned from DLA BSM is the importance of change management and the need to mitigate risks associated with organizational change. Third is re-training and education to achieve buy-in from the thousands of affected employees and contributed to a smooth transition to the new ERP. Finally, robust testing procedures are important as they identify important problems with the new system.

## **B. Competition Creates Good Partners**

Forum participants concluded that effective partnered government is dependent on maintaining a competitive environment. Congress recognized the benefits of competition and required its use with the Competition in Contracting Act of 1984. The mandate is simply stated—competition is very beneficial, therefore maximize its use. Participants, however, emphasized that competition should not be an end in and of itself, but a means to increase the scope and quality of options made available to the government. Competition should not be maximized, but optimized. Participants agreed that if a contractor was continuously improving the firm’s performance, while reducing costs, then there was no reason to compete that program. If, however, that was not the case, then competition was an imperative – so the “option” must be maintained.

In the case of the defense industry, there are frequently a limited number of qualified providers of required services. This is primarily a result of the industry consolidation that occurred during the 1990s, shrinking dozens of defense firms into the handful of large defense firms that exist today. Industry consolidation has successfully continued through vertical integration, as a new measure for cutting costs and increasing efficiency. Furthermore, the barriers to entry for firms seeking to join the Defense market are extremely high. These include knowledge of federal acquisition regulations, specialized accounting and reporting requirements, the need for security clearances, and the ever-present consideration of Washington politics.

As a result of these barriers, it is quite difficult for new firms to enter into defense markets—the barriers-to-entry are just too high. Participants discussed the need to reduce these barriers to the extent possible, by, for example, limiting the use of government unique specifications, standards, and certifications. Government agencies should also eliminate proprietary architectures which make it difficult to “plug in” the state-of-the-art technology as it becomes available and is needed. Additionally, DoD should take advantage of all the flexibilities offered in the Federal Acquisition Regulations, as well as the use of non-traditional contracting authorities. For example, “Other Transactions Authority (OTA)” is available; but its use has been limited by several factors; but principally, they have been restricted by a

broad misperception of their potential and the risks involved. OTA permits a form of contracting for research, development and conducting prototype projects (and their production and deployment follow-ons) that is an alternative to military contracting under the Defense Acquisition Regulations and related statutes and regulations. The goal of OTAs is to enable greater access to commercial suppliers, in order to satisfy many defense requirements. Education in the applicability and use of OTAs is clearly required.

DoD must also continue reviewing and evaluating the impacts of potential mergers and acquisitions, with a goal of maintaining at least two (and in some cases more) viable suppliers. In order to achieve this, DoD needs to ensure that funds for competitive dual-source production are made available, and the necessary oversight and management structure exists, when the development planning process begins.

Participants also discussed the use of technology to reach out to get ideas and inputs from a greater range of players, as a way to enhance competition. Google, for example, has a process that enables and encourages employees to post new ideas to an internal website. Other employees can critique and add to these. The concepts that generate the most interest on this “buzz meter” can then be more carefully evaluated and developed. They believed this strategy could be used to gain input from both users and innovators.

## **Recommendations**

### **Department and Agency heads should:**

#### ***Recommendation Six: Reduce Barriers-to-Entry***

DoD must lead the effort to remove or reduce the many barriers that prevent non-traditional firms from entering the defense business sector. This effort should be aimed at accepted rules, regulations, and practices within the defense market that often create barriers-to-entry. Reducing these barriers will allow the DoD to increase competition by reaching beyond the traditional defense companies, as well as to seek transformational technologies and services. The goal is to generate greater competition among traditional and non-traditional firms, in

order to enhance the solutions available to the government, improve performance, and reduce costs. Specific actions include:

- **Enforcing policies limiting use of government-unique standards, specifications and certifications.** Government policy is to use performance specifications when acquiring new systems, and to use military specifications and standards only as a last resort. This policy needs to be reemphasized and enforced to maximize the competitive field.
- **Keeping systems “open” – eliminate proprietary architectures and interfaces.** An Open Architecture (OA) allows such a policy to be more easily applied. It provides a framework for developing interoperable systems that are more easily developed and upgraded. As a result, an OA enables a “plug and play” capability from components and systems that are assembled and connected in a way that the replacement of one component has a minimal effect on the other parts of the system. This allows the user to “plug in” state of the art systems and components as they are developed and needed. An OA can still accommodate proprietary systems, as long as they meet the OA interface requirement.

As the case studies highlighted, it is particularly important, during the development of complex systems, for the government to have access to independent, third party advice—especially when defining architectures and/or interfaces. Programs should look to partner primarily with academia, research centers and labs, and standards development organizations for the development of open architectures – and systems engineering firms that do not work for hardware contractors, and have no special interests they are trying to sell. These sources should have the necessary expertise and an objective view.

- **Expanding the use of non-traditional contracting authorities.** DOD should expand its use of OTAs, recognizing them as an equal alternative to traditional contracting, and using them to attract commercial firms that typically spurn DoD business. OTAs have proved to be a better, faster, cheaper way to conduct defense research, development, and prototype projects compared to using traditional procurement contracts. They have demonstrated outstanding utility and benefit to DoD projects in basic, applied and advanced research, prototype projects relevant to weapons and weapons systems, and in

distinctively innovative transactions. Using OTAs has the potential to greatly expand the number of firms willing to work with DoD.

***Recommendation Seven: Ensure Competitiveness at the Prime Level and Sub-Tier Levels by expanding the use of competitive dual-sources***

DoD must continue reviewing and evaluating the impacts of potential mergers and acquisitions, with a goal of maintaining at least two viable suppliers in mature defense markets. In areas requiring innovation or that have exceptionally high demand, a greater number of suppliers should be maintained. The same should hold true in any critical sub-tier; the concern, regarding vertical-integration, is that if one prime contractor owned the only supplier of a critical subsystem that would put them at a very significant competitive advantage against other primes. The goal must be maintaining a competitive environment, while discouraging anti-competitive horizontal or vertical consolidation.

Competition, built in from the beginning of acquisition planning, is critical to ensure that its benefits can be harnessed throughout the process. Because of the current, phased design and development requirements for system acquisition, natural cutoff points exist for competition to be introduced to the process. Competition is largely accepted at the initiation of development and for production. However, the option of competition during production is often resisted, even though it is the key to ensuring a real incentive is given for contractors to meet cost, schedule, and performance requirements.<sup>12</sup> Competition during production permits firms to compete during the production process in stages or phases for the award of additional production, allowing for the avoidance of monopolist tendencies that occur from a sole-source, award-winning producer. Ultimately, empirical data have shown that competition during production results in higher performance at lower costs, and steeper learning curves (a more rapid rate of learning) achieved by both suppliers.

DoD needs to ensure the funds for competitive dual-source production are made available when the development and planning process begins. To effectively partner, when maintaining this increased level of competition, the government program office will require a larger, more experienced staff to manage the increased workload, and provide the necessary oversight and management structure to support a competitive dual production environment.

### ***Recommendation Eight: Where Possible Reduce the Government Monopoly***

Government should continue to introduce competition into commercial activities currently performed by civilian employees or military service members i.e. all those functions that are not inherently governmental or critical. This will allow public sector employees a fair opportunity to bid and/or partner with the private sector. It is clear from all the available data that when competition is introduced, government service improves, and costs generally decrease significantly—no matter who wins. The key is shifting from a monopoly to a competitive environment. The goal must always be to get better performance at a lower cost.

#### **DOD AND PRIVATE SECTOR PERSPECTIVES ON ACQUISITIONS**

Mr. Shay Assad emphasized the challenges of DoD acquisitions; buying everything from integrated complex weapons systems to ordinary commodities. In spite of the challenges, Mr. Assad underscored his belief that DoD's contracting officials were doing a good job, as evidenced by the low rate of "bid protests" that are filed with the Government Accountability Office.

Mr. Stan Soloway (President and CEO of the Professional Services Council) highlighted four keys to partnering:

- Partnering involves multiple layers; they can involve the program office infrastructure, to developing requirements, to the program itself.
- The need to identify and mitigate the program's risk. And, although the Government's risk is paramount, the industry's risk, also important, is most times poorly understood or improperly addressed.
- Many current policy directions need to be adequately dealt with, such as the increased emphasis on insourcing; the DCAA pass/fail policy--where a minor issue could cause a firm to fail its audit; and the occasional "political" intrusion; where, for example, Congress defines "inherently governmental" for specific contracts as opposed to a substantive definition applied consistently across the government. These policy confusions are all counter to a partnered environment.
- The government's acquisition workforce, which remains under-resourced, under-manned, and under-supported.

***Case Study Three:  
Business Transformation Agency***

The business transformation efforts within DoD began in July 2001, by the Secretary of Defense. However their successes were slow, limited and expensive; costing \$440 million over five years. Things changed when Congress mandated, in the National Defense Authorization Act (NDAA) for FY 2005, that the DoD must certify and approve any business system modernization costing over \$1 million during a system's development and modernization lifecycle. Certification is to be performed by a Defense Business Systems Management Committee (DBSMC), and chaired by the Deputy Secretary of Defense. Investment Review Boards (IRBs) were established to analyze the impact of IT modernizations investments over \$1 million, and make recommendations to the DBSMC.

Out of this framework, the Business Transformation Agency (BTA) was established, with a \$350 million budget, to provide day-to-day management of the DoD enterprise-level reform. It has four focuses: 1) greater support for joint warfighting capabilities, 2) strategic resourcing decisions need better management information for sound decisions affecting human resource capabilities, 3) reduce costs of business operations, and 4) enhance the DoD's stewardship to the American people by enhancing accountability and service.

In order to achieve these goals, the BTA realized it needed to partner with private sector entities. As noted earlier, the public sector has greater knowledge and experience with rapidly changing technologies than the public sector and an ability to make wholesale transformation of entire business processes within a highly collaborative environment. The BTA, however, continues to face many challenges. Each component within DoD has its own unique values, organizational structure, culture, power structure, and legacy processes and systems, which are independent of each other. To address and overcome these challenges, successful business transformation requires access to personnel with the right skills sets.

Although many challenges remain, the business transformation effort at DoD has experienced significant improvements since the major 2005 course correction. From this trial-and-error phase, several lessons were drawn: First is to have the proper mechanisms for the desired business transformation. In this case it was the BTA and the Investment Review Board. The second lesson was ensuring a high level of government leadership by establishing Chief Management and Deputy Chief Management Officer positions that involve Under Secretaries and Senior-level Service officers. Third is an emphasis on improving performance and efficiency. This was done by establishing the position of a Performance Improvement Officer and the institutionalization of CPI/LSS (Continuing Process Improvement/Lean Six Sigma). Finally, lots of patience and persistence are needed. Entrenched organizational cultures do not change overnight; transformation may span over the course of several agency Directors' terms. Continuity of ongoing transformation efforts requires consistent leadership that is assisted by the proper of governance structures (as mentioned earlier).

### ***C. Implementing Partnered Government***

Government today is executed through an ever-widening network of providers, both public and private. When developing a major government program, senior leaders must anticipate partnering for most major government programs. There are, however, many political, cultural, and organizational factors that significantly impact how different parts of an organization interact with each other, as well as how it interacts with external organizations. Senior leaders must develop a process that identifies and defines a clear vision of the program objectives, maps those objectives to the enterprise priorities, and then aligns other subordinate priorities. This will help to avoid conflict and/or overlap of efforts in the future. Next, they must identify the required resources, the potential partners, and their role in the program. At that point, a business case should be developed and a partnering strategy identified (program staff augmentation, advice, and development team). Finally, the leaders must engage their partners to develop the program strategy and conduct the planning, and then follow through with the execution. Forum participants noted constant communication is critical for leaders to accomplish these tasks.

As the cases demonstrated, many major government programs are long-term affairs. Long-term leadership, however, can be a challenge in government; since government agencies are led by political appointees, lending themselves to high rates of leadership turnover. Adding to complexities, the average tenure of Senate-confirmed appointees is only about 3 years. Though the average tenure of politically appointed senior officials also tends to vary between government agencies, within DoD, the turnover rate is much higher. From 1949 through 1999, the average tenure of Secretary of Defense and Deputy Secretary of Defense were 30 months and 23 months respectively; and among other senior DoD official, the most common tenure was between 11 and 20 months.<sup>13</sup> These challenges ripple down to lower levels, particularly with senior military leaders. As highlighted by the cases, many of the large government initiatives easily transcend these time frames, with schedules that approach a decade or longer, and by no means, as one participant noted, are they a “one tour success event.”

To overcome this problem for their Business Systems Modernization program, for example, the Defense Logistics Agency established a Modernization Executive Board, with a senior executive from every functional area to establish and maintain program tenets. The program had to adhere to these tenets unless a change was approved by the board. The board members buy-in and involvement, from concept through implementation, created enough momentum to see the program through development with minimum changes. When appropriate, DLA also included the Systems Integrator in these and smaller-group partners' issue resolution sessions.

Another challenge relates to the culture of the DoD acquisition community, both within the government and the private sector. Most of the personnel and organizations have years of experience developing requirements-driven, specification-constrained, custom-designed and built components and systems. Now, they are asked to incorporate constantly-evolving, market-driven, commercial systems. Additionally, DoD's prescriptive rules potentially inhibit contractors from developing initiatives and good business judgment to simultaneously craft transactions advantageous to DoD while honoring the interests of its business partners. Forum participants agreed that in order to make the required culture changes, leadership involvement at all levels is paramount.

Participants agreed that the concept of partnering can be confusing to government managers, who feel much more comfortable working strictly inside a contract framework, with its specified performance expectations. The resultant culture frequently results in risk-averse behavior that can inhibit innovation. Achieving a partnering relationship is more about developing trust, common objectives, and an expression of commitment. It complements, but does not replace a contract, and (when effective) works to reduce the friction within the performance of the contract. These relationships are built on open communications between both parties with a full appreciation of the program and its business risks. These communications can be aided by co-locating teams, as was done in the Army's LMP program.

Moreover, the participants identified a critical issue—the need to use an appropriate contract type, depending on the programs risk, requirement uncertainty, and technology maturity.

Program leaders must analyze these factors, consider all contract types and terms, and select the optimal contract that is equitable to both parties.

These relationships, anticipated to be long term, can also be formalized. DLA, for example, has formal Strategic Partnership Agreements with several of its major vendors, with whom it expects to have long-term relationships. These agreements are signed by the firm's CEO and the Director of DLA. Participants observed, however, that laws and policies are often interpreted in a way that does not promote a partnering culture, but in fact inhibits it.

## **Recommendations**

### **Department and Agency heads should:**

#### ***Recommendation Nine: Change the culture to make effective partnering a top management priority***

Virtually all major government initiatives will require partnering, particularly with the private sector. Ensuring that these relationships are effective must be a top management priority. In order to achieve the desired results from partnering will, however, require a major cultural change in public organizations. Public-private relationships often become adversarial contractual relationships rather than partnerships. Both the public and private sector must adopt a “win-win” approach, and focus on shared, broad outcomes, not narrow organizational ones. Rather than being compliance-driven (rules-driven), they need to look at the “art of the possible” and find ways to make partnerships beneficial for both parties.

The Navy successfully demonstrated this “win-win” approach with its partnering to provide logistics support for Auxiliary Power Units (APU) used on several different U.S. Navy aircraft. This unique agreement had Navy civilian employees performing touch labor, while the contractor performed an increased role in traditional government functions, such as supply support, repair, and repair management (using best commercial practices). The contractor, was incentivized to increase performance and reduce costs, given greater flexibility and control in configuration management, and provided program stability, with a 10-year, firm-fixed-price contract (5 year base and one-year options).<sup>14</sup> The Navy achieved

significantly improved availability (from 65 percent to 90 percent), while the logistics response time decreased from 35 days to 6.5 days.

Furthermore, government employees need to be provided the necessary authority to achieve the required cooperation and integration needed for the program's execution (for example, ensure members assigned to integrated product teams (IPTs) are empowered to make decisions within their areas of expertise).

Employees must have the training and tools needed to do their jobs. Demographic trends, specifically the aging national workforce, are creating the need for government agencies to expand training and education programs. Agencies should establish a professional development program based on an "open systems" approach, including access to corporate universities, web-based training, and other cutting-edge programs to develop critical business thinking and decision-making skills.

To better prepare the government workforce for partnered government, professional development programs should focus on the flexibilities of the Federal Acquisition Regulations, as opposed to its limitations. Additionally, based on the pace of development and change, government agencies should create cross-fertilization opportunities between the government and industry. Using techniques such as rotational assignments (between government and industry – both ways) would not only offer valuable experience for government personnel in the private sector but also offer valuable insight for private industry experts into the unique challenges faced by government officials.

***Recommendation Ten: Develop a Process to Build Partnering Relationships***

Department and Agency heads must plan for partnered government by creating an agile "multi-sector" workforce that optimizes its mix of military and civilian employees, contractors, other government agencies, and non-profit and academic partners. Each opportunity must be undertaken with a "win-win" approach. Agencies should adopt a process that identifies the capability need, maps that need to an enterprise priority, aligns it with the owners of subordinate strategic priorities, identifies the required resources and potential partners, develops a business case, then identifies a partnering strategy. Using this

strategy, the program can then organize for successful execution. Moreover, creating a process involving all stakeholders will help to ensure their buy-in at an early stage of program development. The required partners can then be successfully integrated to achieve maximum effectiveness.

***Recommendation Eleven: Ensure consistent program leadership by maintaining stability of key personnel.***

Frequent changes in key personnel often lead to significant changes in an organization's priorities, goals, and strategy. These changes, as well as changes to the organization's strategy to achieve its goals and objectives, can also significantly impact relationships with partnering organizations. Frequent leadership turnover also strengthens the existing organizational culture, which may make it more difficult to form partnerships with the private sector. Long-term, or permanent, employees may be reluctant to participate in organizational change initiatives that significantly change their day-to-day responsibilities; which can make developing partnerships with other organizations more difficult.

Consideration should also be given to creating a program governance structure that can help to bridge changes in key personnel. The Defense Logistics Agency successfully helped to provide consistent leadership for its Business System Modernization program by creating the Modernization Executive Board (MEB). The Board guided the development of the BSM program, and also ensured that change was driven down through the organization—providing continuity to the modernization process. The Board's guidance, leadership, and involvement were major contributors to the program's success.

The lack of sustained leadership also often contributes to program delays and setbacks. Program delays, setbacks, and cost overruns can create tension among stakeholders, including between partnering organizations. Without strong leadership, relationships between partnering organizations can deteriorate. To the degree possible, senior government leaders must ensure that there is program continuity, especially with key program leadership.

## **Program Leadership Should:**

***Recommendation Twelve: Develop and maintain communications to build trust between government representatives and contractors.***

One key to success with partnered relationships is for the government representatives and the contractor to maintain open, uninterrupted communications to build mutual trust.

Participants pointed out information sharing and increased awareness is empowering and motivational. This process can and should start before the solicitation for partnership is released, so that the government representatives can better understand the partners' equity and value. In addition, early interaction can break down the rigid structure of formal communications that exists in the government's traditional contracting process, while allowing for potential partners to provide their input on the contract requirements. This enables the partners to synchronize the program's needs with current capabilities and technologies faster. Although all partners may not be equal, when they have common objectives they will move in the same direction. Partnered government will not work when there is an adversarial relationship between the government staff and the contractor.

***Recommendation Thirteen: Where possible co-locate public-private teams***

Group cohesion and communication are vital for successful partnering. To facilitate the most beneficial synergy between private and public entities, co-locate partnered teams in the same facility or place them within close physical proximity to each other is recommended. This can improve communications, help to cement relationships, build team cohesiveness, and increase trust levels.

***Recommendation Fourteen: Identifying the appropriate contract type***

Equally important is selecting the appropriate type of contract; which is the primary mechanism government contracting professionals use to mitigate the risks inherent in the acquisition of supplies, systems, and services. The contract type determines the degree of risk and any associated costs of the risk allocated between the contractor and the DoD. Firm fixed-price contracts appear very attractive, since a majority of the risk of the cost of performance is allocated to the contractor; and can be effective when requirements are

known and stable, and the technical risk is low. If that is not the case, such as in the LMP program, then other structures (cost plus award fee, for example) have proven to be far more effective.

***Recommendation Fifteen: Develop appropriate metrics and incentives for both the public and private sector organizations***

Forum participants agreed that program output metrics (specific, measurable, and achievable within the required timeframe) are critical for government agencies to achieve the desired partnered program results. These metrics (both performance-based and cost-based) should be tailored for desired outcomes, and be designed to achieve the desired behavior from both federal employees and contractors. For large, complex programs, the appropriate metrics will enable performance and cost targets to be set, progress to be assessed, identification of corrective actions, and lessons to be learned.

The metrics are also necessary to hold organizations accountable for their performance. The program's incentives structure must answer the question "what's in it for me?" That answer will generally be different for each partner, and must be tailored accordingly. At DLA, for example, the government team had bonuses tied to the delivery of contractor deliverables.

## ***Weapon System Acquisition Reform Act of 2009***

On May 22, 2009 Congress passed Weapons System Acquisition Reform Act of 2009. Co-sponsored by Senators Carl Levin and John McCain, that enhances the organization and procedures of DoD Major Defense Acquisition Programs (MDAPs). Relevant to this report is Section 207 which discusses avoiding organizational conflicts.

Section 207 mandates that the Undersecretary for Acquisition, Technology, & Logistics revise the Defense Supplement to the Federal Acquisition Regulation to provide guidance and tighten existing requirements concerning OCIs by contractors in MDAPs.

*The revised regulations required by subsection:*

*(a) shall, at a minimum—*

*(1) address organizational conflicts-of-interest that could arise as a result of—*

*(A) lead system integrator contracts on major defense acquisition programs and contracts that follow lead system integrator contracts on such programs, particularly contracts for production;*

*(B) the ownership of business units performing systems engineering and technical assistance functions, professional services, or management support services in relation to major defense acquisition programs by contractors who simultaneously own business units competing to perform as either the prime contractor or the supplier of a major subsystem or component for such programs;*

*(C) the award of major subsystem contracts by a prime contractor for a major defense acquisition program to business units or other affiliates of the same parent corporate entity, and particularly the award of subcontracts for software integration or the development of a proprietary software system architecture; or*

*(D) the performance by, or assistance of, contractors in technical evaluations on major defense acquisition programs;*

*(2) ensure that the Department of Defense receives advice on systems architecture and systems engineering matters with respect to major defense acquisition programs from federally funded research and development centers or other sources independent of the prime contractor;*

*(3) require that a contract for the performance of systems engineering and technical assistance functions for a major defense acquisition program contains a provision prohibiting the contractor or any affiliate of the contractor from participating as a prime contractor or a major subcontractor in the development or construction of a weapon system under the program; and*

*(4) establish such limited exceptions to the requirement in paragraphs (2) and (3) as may be necessary to ensure that the Department of Defense has continued access to advice on systems architecture and systems engineering matters from highly-qualified contractors with domain experience and expertise, while ensuring that such advice comes from sources that are objective and unbiased.*

It also requires The Panel on Contracting Integrity (established under the John Warner National Defense Authorization Act for Fiscal Year 2007) to present recommendations to the AT&L Undersecretary on measures to eliminate or mitigate OCIs in MDAPs. The legislation directs The Panel to continue to serve until at least the end of 2011.

Sources: Public Law 111–23—May 22, 2009, “Weapons System Acquisition Reform Act of 2009.”

## **Appendix I—The Environment that’s Driving the Changes**

An understanding of the current environment is necessary to analyze the need for an increasingly and more effectively partnered government. These factors include rapid changes in information technology, domestic economic constraints that will limit defense appropriations, national demographic shifts impacting the DoD workforce, and the increased reliance on private contractors to perform commercial activities. This section will explore these factors and their impact on partnered government.

### ***A. The IT Revolution***

Continual innovation in IT is making computing and networking cheaper and faster, while improving and expanding its capabilities. The IT revolution accelerated throughout the 1980s and 1990s, as personal computers became ubiquitous and the Internet was introduced, allowing for new business models (i.e. electronic commerce); and, more importantly, enabling significant changes to how businesses organize. Information can now be made available anywhere in the organization, and functions can be consolidated and geographically displaced. Additionally, employees can more easily form networks and collaborate.

IT has changed the nature of work in many ways, allowing for the automation of repetitive clerical and administrative tasks. IT is more recently being used for far more advanced applications in virtually all types of organizations. Companies and government agencies are applying networked IT to help with complex tasks such as enterprise resource planning and supply chain integration. In “world class” organizations, it is possible to monitor business operations in “real-time,” rather than wait for monthly or quarterly reports. As a result, many firms have been able to transform their IT investments into significant gains in productivity and efficiency. For example, in 1987 Wal-Mart had 9% market share and was 40% more productive than its competitors. By 1995, Wal-Mart increased its market share to 30%, with 48% greater productivity, even as its competitors had aggressively increased their own productivity. These improvements were due in large part to the extensive use of IT to improve its supply chain.<sup>15</sup>

In addition to driving improved business operations, developments in IT have catalyzed and fueled the growth of globalization. With the capacity and speed of information networks, many different tasks can be parceled out and performed virtually anywhere, as long as there is Internet access. As a result, businesses experience the effects of increased global competitive pressures; in turn, many businesses are forced to transform their operations to meet the needs created by these new conditions. Businesses that embrace these new technologies and successfully integrate them into their business operations will gain a competitive advantage in their industry.

The integration of information technology into business models is not without risk. IT investments typically require a significant amount of capital, and do not always produce the expected benefits. However, business transformations within companies such as General Electric and IBM demonstrate how IT can help produce competitive advantages.

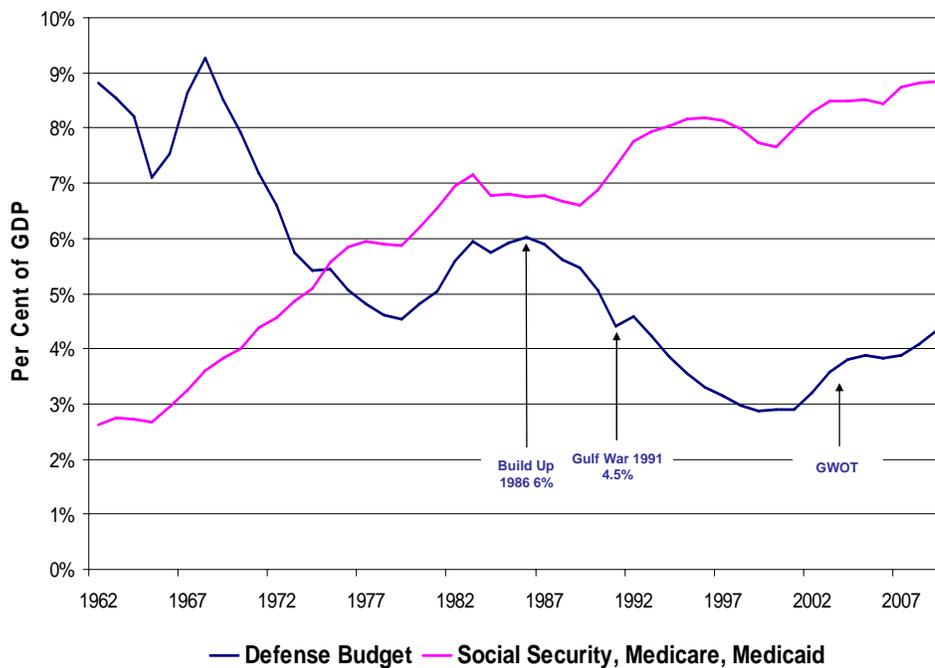
If harnessed by the private sector to improve productivity and efficiency, these same technologies can potentially produce similar results in the public sector, even as they may introduce new concerns about information assurance and cybersecurity. Unlike the examples in the commercial sector, however, many federal government IT initiatives have proven to be challenging and generally have not achieved the desired results. The DoD, for example, has only made progress in realizing the potential of information technology, and still uses 2,005 generally non-interoperable logistics business systems.<sup>16</sup> As a result, DoD is still far from world-class and is significantly less capable than the commercial sector in managing its supply chain, yet does so at far higher costs. The DoD must partner with the private sector to more rapidly leverage the gains of IT, in order to transform its business systems and attain the kinds of gains in productivity achieved by the private sector.

### ***B. Domestic Budgetary Outlook***

The United States faces several long-term budgetary challenges. These challenges, and the impact they will have on the domestic economy, will directly contribute to the ability of the DoD to transform as needed for the twenty-first century. The U.S. will have a rapidly increasing financial burden as baby boomers age by 2020; the number of people between the ages of 65-84 is expected to rise by nearly 50 percent,<sup>17</sup> and mandatory spending on

programs such as Social Security and Medicare will undoubtedly increase. 2008 was expected to be the first year where many “baby-boomers” begin to enter retirement age. However, by 2018, “...all but the youngest baby-boomers will be of retirement age. Aggravating the situation is a much smaller pool of workers immediately following the baby-boomers.”<sup>18</sup> By 2030, the annual growth rate of Social Security spending is expected to rise from 4.3 % of GDP to 6.1%,<sup>19</sup> while Medicare and Medicaid are projected to grow to 9% of GDP by 2035.<sup>20</sup> Spending on these programs is directly tied to the rising cost of living and healthcare in the United States; as depicted in Figure 1, these expenses have outpaced defense spending as a percent of GDP. Although defense spending has been increased since the Cold War drawdown, it is nowhere near historic record levels as a percent of GDP.

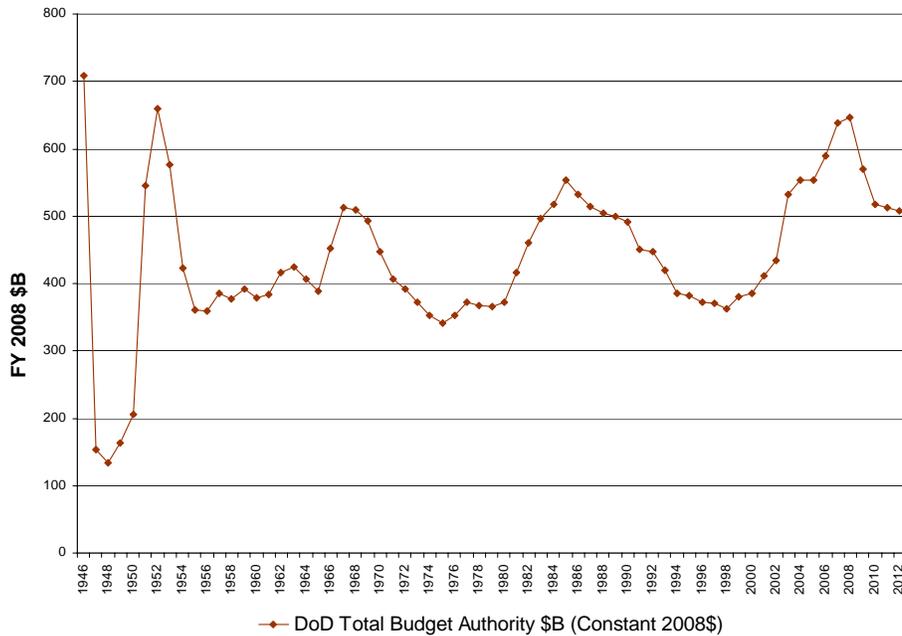
**Figure 1: Defense and Selected Entitlement Spending as a Percent of GDP.<sup>21</sup>**



Additionally, the DoD has come to rely on “supplemental” funding, which will likely be ceased or be significantly reduced as early as FY 2009. This is due to the weary attitudes of Congress and the general public toward the war in Iraq. Finally, given the rising costs of military personnel compensation, annual health care and facilities programs, it is clear that a sizable portion of “defense discretionary” spending will not be available, and has been

already earmarked for future requirements. Even though defense budgets are currently well above the Cold War average (as shown in Figure 2), they will likely decline significantly based on past historic trends.

**Figure 2: DoD Total Budget Authority (In Constant 2008 US Dollars).<sup>22</sup>**



2007 includes \$93.4 billion supplemental appropriations request.  
 2008 includes \$141.7 billion request for GWOT operations.  
 2009 includes \$50 billion projected for GWOT operations.

Source: Historical And Projected Funding For Defense: Presentation Of The FY 2008 Request In Tables and Charts By Steven M. Kosiak, CSBA, June 7, 2007

The rising costs of mandatory entitlement programs, coupled with the enduring projected budget deficits, will create an inevitable downward pressure on all future government discretionary spending; as a result, it can be expected to have a significant impact on DoD budgets. This will serve to constrain the funds available for recapitalization, modernization and transformation of the military. Future DoD budgets will require hard decisions, and will be dependent on a reengineering of processes and the efficient use of resources as a source of funds for these requirements.

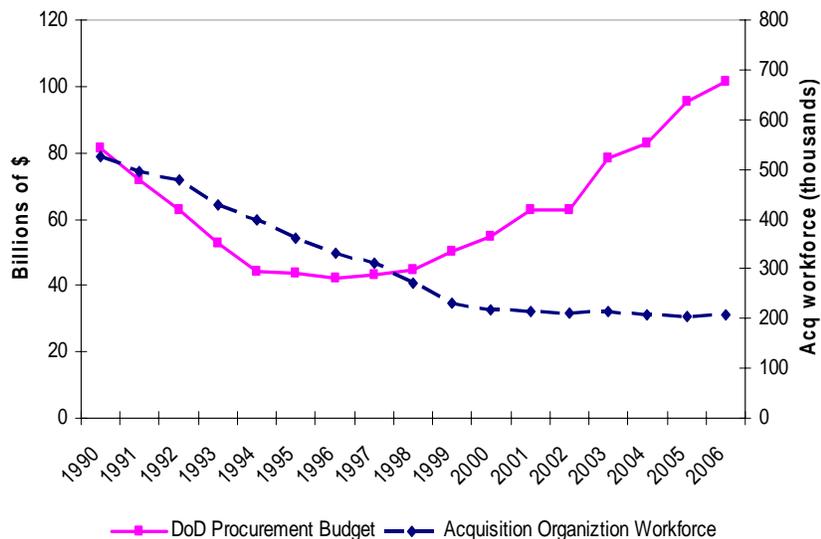
### C. The DoD Workforce

DoD faces three human capital challenges in its efforts to transform logistics: acquisition workforce cuts, demographics and personnel requirements for support functions.

#### Acquisition Workforce Cuts

Due to budget cuts at the end of the Cold War, the DoD's civilian workforce was significantly reduced via voluntary turnover, retirements and freezes on hiring authority. Between fiscal years 1989 and 2002, the civilian workforce shrank by approximately 38 percent; the acquisition component of the workforce was hit especially hard. Commensurate increases in acquisition personnel did not occur despite major increases in the defense budget in the years following these cuts,<sup>23</sup> as can be seen in Figure 3 below. Such personnel reductions place additional pressure to perform on the remaining acquisition employees. These trends could be exacerbated by the new Federal Employee Retirement System, which encourages greater job mobility. FERS will attract seasoned Federal employees to the private sector, making institutional memory and experience harder to retain.<sup>24</sup>

**Figure 3: Procurement Budget Compared as with Acquisition Workforce Size**



Source of workforce data: DoD IG Report D-2000-088 Feb 29, 2000 & DoD IG Report D-2006-073 April 17, 2006

Source of budget data: Annual Defense Reports, available at [http://www.dod.mil/execsec/adr\\_intro.html](http://www.dod.mil/execsec/adr_intro.html). Procurement supplementals for FY2005 and FY2006 not yet reflected in Annual Defense Reports were obtained from Congressional Research Service Reports.

Recent initiatives to try and correct these deficiencies seek to hire an additional 9,000 government acquisition professionals by 2015, beginning with 4,100 in 2010. These new personnel would replace contractor staff that have been supporting acquisition task.<sup>25</sup>

Numbers of personnel alone, however, will not be sufficient; they need to gain the requisite experience. So, for example, if acquisition interns are hired, then partnering with experienced industry people will still be required.

### *Demographics*

As of 2006, baby boomers represented over 64 percent of DoD's workforce, while generation X and Y civilian personnel only represented a combined total of 28 percent.<sup>26</sup> As of 2008, 18 percent of the civilian acquisition workforce (20,000 employees) was eligible for retirement. In addition, another 20 percent (22,500 employees) will be eligible to retire within the next five years.<sup>27</sup> These demographic conditions highlight the potential knowledge and experience gaps that exist, as many workers of the older generations may not be up to date on modern, cutting-edge supply chain management methods. This could have the effect of negatively impacting DoD's effort to transform logistics.

This situation also brings to light the serious need for the active recruitment of acquisition personnel as older generations retire. The government's effort to meet staffing needs, however, will be complicated by competition with the private sector. This is exacerbated by the falling numbers of engineers and scientists graduating from American universities. Replacing them with foreign-born engineers will be problematic for national security agencies because of security clearance requirements.<sup>28</sup>

There are also management challenges when dealing with younger workforce generations. Unlike baby boomers, generation X and Y workers have less personal attachment to their employers. They tend to work more independently and look for new ways to professionally advance themselves. This can be achieved through new job opportunities and acquiring more marketable skills and experience.<sup>29</sup> Learning to successfully manage these traits will be a challenge for executives.

### *Personnel Requirements for Support Functions*

DoD's tooth-to-tail ratio, or the ratio of those personnel that perform combat duties to those in support activities is 15:85. This means that there are roughly 5.5 support personnel for every individual that is performing combat duties. This ratio has remained fairly constant over the last decade.<sup>30</sup>

Industry best practices dictate that management must continuously evaluate and reduce overhead, identifying and improving (and/or divesting) low value-added areas to continuously reduce inefficiencies and organizational overlaps. During the period in which many "world class" firms have made significant strides in improving their efficiency, the DoD has not made any significant reduction in its overhead.

#### ***D. Contractor support to the Warfighter***

After the Cold War and the breakup of the Soviet Union, the United States made the decision to significantly downsize its armed forces. The DoD reduced or eliminated many of its maneuver units and an even larger portion of its combat service support units. This downsizing effort provided an opportunity to turn over many military support functions to private firms, while reserving core warfighting functions for the military. As a result, when units are deployed there is now an enduring need for contractors on the battlefield—their presence is no longer optional or marginal.

The Government Accountability Office (GAO) recently estimated there to be 5,000 government civilians and 9,200 contractor employees deployed in support of U.S. forces during the first Iraq War. By the time the U.S. deployed forces to the Balkans in 1995, Halliburton's Kellogg, Brown & Root division (KBR) employed between 5,000 and 20,000 contractors to both build and operate bases and perform dozens of other support functions for as many as 20,000 soldiers carrying out peacekeeping operations in the former Yugoslavia. In Bosnia, the U.S. Army peacekeeping force of 6000 soldiers was supported by 5,900 civilian contractors.<sup>31</sup> The number of contractors involved in Operation Iraqi Freedom is approximately 265,000.<sup>32</sup> Figure 4 shows the ratio of uniformed military personnel to contractors for several conflicts.

**Figure 4: Ratio of Military to Contractor Personnel in Historical Comparison<sup>33</sup>**

<b>Military Engagement</b>	<b>Ratio of Uniformed Personnel to Contractors</b>
<b>Korean War</b>	<b>2.5 to 1</b>
<b>Vietnam War</b>	<b>5 to 1</b>
<b>Balkans</b>	<b>1 to 1</b>
<b>Operation Iraqi Freedom</b>	<b>1 to &gt;1</b>

Recently, news reports have expressed growing concern over the cost of using private contractors to support the warfighter, particularly in hostile theaters. The Wartime Contracting Commission's first report largely focused on the mismanagement and inefficiency of the LOGCAP program.<sup>34</sup> Notwithstanding the issues of proper oversight, contractors have in general provided vital logistics and support services under extremely challenging and dangerous conditions.

Moreover, a 2005 Congressional Budget Office report identified several advantages to using contractors instead of federal civilians and military personnel to provide this type of support. Contractors often have the capacity and capability to provide personnel with skills and expertise that military forces may lack, as they already provide these benefits to CONUS based forces, local governments and commercial clients. Additionally, using contractors provides DoD with flexibility, allowing them to leverage the experience of retired or separated military personnel. Finally, when the military retains an occupational specialty, they are generally required to maintain an entire career track, to include students and instructors.

The report also found that the costs for performing the same functions in wartime conditions were similar between contractors and military personnel. However, the Army's costs were almost 90 percent higher than the contractor's when peacetime costs were included. This is because contractor support can be scaled back significantly if necessary, but the military needs the required personnel plus a training and rotation base in the force structure.<sup>35</sup>

A more recent Congressional Budget Office (CBO) study examined the cost of private security contractor (PSC) personnel compared to active duty military personnel, and found

them to be similar; however, peacetime costs for contractors were again found to be substantially lower.<sup>36</sup>

### ***E. The Proper Role of Government***

In 2009, President Barack Obama stated that he seeks to review and revise the government's use of contractors. This is largely driven by the belief that it saves money, and the perception of "wasteful" spending on private firms to perform functions once done by government employees.<sup>37</sup> However, the forces pushing toward greater use of outside third parties to perform government functions have not decreased, but increased. This leads one to ask what the proper role of the government ought to be.

In fact, many of the services are currently being provided by the private sector efficiently and effectively. Contractors provide a variety of services, including routine administrative and support functions, cutting edge systems development and integration and the provision of consulting services and advice. They can act independently, or work side by side with government employees to create a multi-sector workforce. The role of the government must evolve, especially as needs, technology and commerce change. The private sector provides access to a workforce that is agile (with its structure and mix quickly adapted to evolving requirements), scalable, and with lower cost than organic government employees due to constant competitive pressure. Government employees should only perform "inherently governmental" tasks and only those non-inherently governmental tasks it can do more efficiently and effectively than their private sector counterparts. The government's role has shifted from being "the provider of goods and services"; they have become the "manager of the provider of goods and services." This allows for the greatest synergism of commerce and government.

This shift began in the 1980's, when the assumption that government services must be carried out by government workers was increasingly questioned. This began first at the state and local level, where people asked, "Why is driving a bus an inherently governmental job? What would happen if it was competitively awarded to private sector firms?" In an effort to meet tight budgets, local officials attempted to implement competitions for this work. They tried a variety of techniques, to include allowing private sector competition for the work

among firms that specialized in that business; competing the work between the current government employees and the private sector; and in some cases the work was simply privatized by letting private companies bid for the government capital equipment and employees.

This approach was embraced at the Federal level by the free-market oriented administrations of Ronald Reagan, and later George H.W. Bush. In the 1990s, a new approach at administrative reform took hold, with a goal to “reinvent government.” Shortly after his election, President Clinton empowered Vice President Al Gore on March 3, 1993 to lead the National Performance Review (NPR), the best-known of these reinvention initiatives.<sup>38</sup> The NPR was established to provide the new Administration with a series of recommendations on how to make the government more efficient. Gore led an intensive six month study, including officials from across the federal and state governments and public sector practitioners. The framework for this effort was derived from over a decade of evolving management practices in the public and private sectors that had been collectively dubbed the “reinventing government movement.”<sup>39</sup> The Administration noted that previous efforts to restructure the federal government had fallen short or set reform standards too low. As Perry Davis pointed out in 1986, the impact of previous bureaucratic reforms were “path dependent, meaning, ... reform strategies have been shaped more by what already exists than by the desired model of public administration.”<sup>40</sup>

The NPR’s official report delivered 254 recommendations that included several calling for reduction of the government workforce through privatization and restructuring. The report aimed to reduce the federal workforce back 12 percent, equating to approximately 252,000 jobs and 2,000 field offices. In 1996, President Clinton pronounced in his state of the union address that “the era of big government is over,” referring to the reduction of the federal government workforce by nearly a quarter of a million jobs. At that point, the federal government workforce was the smallest it had been in more than 30 years. It was estimated that these personnel cuts saved over \$10 billion annually.<sup>41</sup>

President George W. Bush attempted to reinvigorate the government restructuring effort initiated by the Clinton Administration’s NPR. In August 2001, the Bush Administration

released the President’s Management Agenda (PMA), which stated that public sector jobs would be subject to competition with private sector providers.<sup>42</sup> Following the PMA and a congressional mandate, the Office of Budget and Management (OMB) indicated that one-half of the reported 849,389 “not inherently governmental” jobs would be opened up to market competition by 2005. In the past 8 years, implementation of the PMA has been limited (in spite of the cost savings and performance improvements) due to substantial resistance from federal employee unions and certain members of Congress.

A recent study examined the competitions won by either an in-house MEO or private contractors. If one examines the MEO’s proposal for full time equivalent (FTE) employees, the data illustrates (see Figure 5) how introducing competitive forces can drive gains in productivity and efficiency in government operations—even when the government wins. The difference between the total number of authorizations studied and the final average MEO full-time equivalents (FTEs) was large. As could be expected, the MEO proposals that won had the largest reduction of positions, with a 44 percent decrease from total authorizations. The MEO proposals that lost did not have as large a reduction, but even these proposed 28 percent fewer FTEs to perform the same tasks that were being currently performed.<sup>43</sup>

Winning Bidder	Number of Competitions Won	Civilian Positions Competed (Excluding Direct Conversions)	MEO FTEs* (Excluding Direct Conversions)	% Decrease from Civilian Authorizations to Government MEO FTEs
In-House	525 (44%)	41,793	23,253	44%
Contractor	667 (56%)	23,364	16,848	28%
Total	1,192	65,157	40,101	38%

**Figure 5. DoD “Competitive Sourcing” Demonstrated Results 1994 – 2003.**

One of the major concerns of competitive sourcing is that savings will not be realized. The Center for Naval Analysis (CNA) conducted a study that examined the actual (realized) savings from the DoD competitive sourcing after the work had been completed. The results of the study, which compared the actual realized savings with expected savings, are illustrated in Figure 19. For the studied sample of 16 competitions, the analysis indicated savings were in fact realized over time. The expected savings were 35 percent, with the effective savings rate was remarkably close at 34 percent, demonstrating that the savings did

not diminish over the solicitation period. When all wage, scope and workload changes are included, an observed savings rate of 24 percent was observed. The savings are real and are sustained over time.<sup>44</sup>

Competitive sourcing has been very successful in improving the efficiency of the provision of services within the DoD. The introduction of competition (versus its prior monopoly) could serve to immensely aid DoD in achieving its future cost savings goals, with 30 percent savings being a conservative estimate. At the same time, competition helps participants to exceed existing performance requirements, as performance is found to improve or remain stable after the competitions. At the same time, competitive sourcing grants the organic government workforce an opportunity to bid to retain the work, as opposed to other strategies such as outsourcing or privatization. In spite of these successes, competitive sourcing continues to meet with stiff resistance from employee labor unions, which often results in Congressional restrictions.

Some would argue that the government loses control when it partners with the private sector, and that government managers have more control when employees report directly to them. The reality, however, is different: government managers have little ability to hire, reward or fire government employees. Moreover, most government organizations lack the ability to measure performance in terms of overall cost. In a competitive market, federal managers can manage and monitor total program costs based on the performance measures required in a contract.

In spite of the many advantages to focusing government employees on their appropriate role, that is performing the “inherently governmental” functions, and partnering with the private sector, there remains much resistance to this effective partnering strategy.

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## End Notes

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