Preface

This document reports the proceedings of a joint U.S.-U.K. conference on Privatizing Military Installation Assets, Operations, and Services, held April 14-16, 2000 at Ditchley Park, Oxfordshire, U.K. The conference was sponsored by the Assistant Secretary of the Army for Installations and Environment and was attended by senior military leaders, government civilians, and industry representatives from the U.S. and U.K.

Four background papers prepared for the conference — covering an overview of U.K. privatization and outsourcing initiatives and comparing U.K. and U.S. Army initiatives in housing, base operations, and logistics — will be published as a separate volume. These background papers and the conference proceedings should be of interest to government, military, and industry readers who would like to learn about existing U.S. and U.K. outsourcing and privatization efforts, as well as how the military might make more effective use of the private sector in providing support functions.

This research was sponsored by the Assistant Secretary of the Army for Installations and Environment and conducted in the Military Logistics Program of the RAND Arroyo Center. The Arroyo Center is a federally funded research and development center sponsored by the United States Army.

Summary

The U.S. Department of Defense (DoD) and the U.K. Ministry of Defence (MoD) face a common challenge: to modernize their forces to meet changing military threats during a period of reduced budgets. To meet this challenge, both DoD and MoD are increasingly interested in leveraging private sector capital and expertise in the provision of defense activities and support services. While both countries have reduced their force structures and defense spending substantially since the end of the Cold War, the U.K. has been more aggressive than the U.S. in pursuing such private sector involvement. As the U.S. Army seeks to improve the performance and reduce the cost of support services, greater use of private sector capabilities and resources is an essential strategic objective.

This document is a summary of a three-day conference on privatizing military installation assets, operations, and services held at Ditchley Park in Oxfordshire, England, on April 14-16, 2000. The conference was organized by the Assistant Secretary of the U.S. Army for Installations and Environment. The purpose of the conference was to bring together U.S. and U.K. defense officials, U.S. Army leaders, and commercial contractors from both countries to discuss the British experience with privatization and explore its applicability to the U.S. Army. Much of the conference was devoted to small group sessions exploring the potential for privatization in three functional areas: housing and other base facilities, base operations and services, and logistics. This document summarizes the discussions of these working groups, and identifies themes common to all.[1]

OVERVIEW OF THE CONFERENCE

The conference began with a plenary session during which opening remarks were made by the conference co-chairmen, the Honorable Richard Cheney, former U.S. Secretary of Defense, and Field Marshal Lord Vincent, former U.K. Chief of Defence Staff. The themes of the conference and issues for discussion were introduced and explicated in a keynote address by the Honorable Mahlon Apgar IV, the Assistant Secretary of the Army for Installations and Environment. The address was followed by responses from Mr. Martin Kitterick of PricewaterhouseCoopers and Dr. David Chu of RAND, representing the organizations that prepared background materials for the conference. The participants then broke up into three working groups to discuss how these themes and issues applied to housing, base operations, and logistics.

The Housing Working Group discussed privatization in light of two major ongoing initiatives, the U.K. MoD's Private Finance Initiatives for housing, and

[1] The conference agenda and biographical sketches of participants are contained in the appendixes. Background papers prepared by RAND in support of the conference are being published in a separate volume.

the U.S. Army's Residential Communities Initiative. The discussion concentrated on the following subjects:

- The appropriateness of private sector involvement in housing
- Reasons and strategies for recapitalizing military housing stock
- The pros and cons of transferring ownership and management of housing facilities
- Forging successful partnerships with industry
- The roles of tenants and local communities
- Identifying and overcoming barriers to privatization

The Base Operations Working Group used the U.K. experience as a springboard to discuss strategies and opportunities for private sector involvement to improve deteriorating conditions on U.S. Army bases resulting from underfunding of base operations. The discussion focused on the following topics:

- Acknowledging the scope of infrastructure decay
- Determining which functions and services are appropriate for private sector involvement
- Clarifying incentives for base commanders to contract out for services
- Creating appropriate and flexible partnerships with the private sector
- Implementing cost accounting measures
- Managing political challenges

The Logistics Working Group discussed how long-term partnerships might be used to integrate contractors into a strategic vision of the military supply chain. The group considered the following issues:

- Defining logistics and privatization
- Identifying candidates for privatization
- Developing a strategic vision for privatization
- Creating internal incentives for privatization
- Organizing new military-industry structures
- Attracting and selecting the best contractors
- Managing and monitoring contracts

COMMON THEMES

Each working group presented a short report during the final plenary sessions of the conference, and participants from the other working groups were invited to respond. As the full group discussed the reports, several common themes emerged. These can be grouped under four broad questions.

Why Do We Need Privatization?

If support costs cannot be decreased from their current levels, the military will have to either reduce its force structure or slow down modernization. Private sector contracts can help the military renovate housing and base facilities without requiring substantial up-front investment of public sector funds. The private sector can also absorb some risks related to service provision, and it can

improve service performance by bringing a broad expertise in business processes and practices.

What Activities Are Appropriate for Privatization?

Each of the working groups struggled to define military core competencies that should be excluded from private sector involvement, other than clearly military activities such as war fighting and maintenance of military ethos, and which should be open to potential privatization. Although it proved difficult to draw a clear dividing line between military, civilian, and contractor functions, each group agreed that a strategic approach was needed to integrate the three, particularly in deployed environments.

How Can Public-Private Partnerships Be Established?

To make effective use of private sector providers, the public sector partner must replace adversarial contracting relationships with long-term partnerships based on common goals. Conference participants identified three key components to successful partnerships: designing contracts to elicit outcomes rather than specifying inputs; establishing performance metrics and linking them to contract incentives; and sharing benefits between the public and private partners.

How Can We Create Incentives for Privatization?

Conference participants shared ideas about how the U.S. Army can elicit deeper organizational and political support for private sector involvement in military support services. They identified a number of potential incentives to encourage political leaders and base commanders to implement privatization, such as using pilot projects to test new concepts and demonstrate successful innovation, and allowing base commanders to keep a share of the savings from privatization.

NEXT STEPS

Conference participants agreed that the forum created a valuable exchange of ideas and information between military leaders from the U.S. and the U.K., as well as among individuals from the public and private sectors. They expressed interest in a continuing dialogue, including visits to sites where innovative privatization initiatives have been implemented.

Based on their interactions with MoD and industry representatives, U.S. Army participants resolved to pursue the following action plan:

1. Establish a permanent, ongoing forum, such as this conference, for continued U.S.-U.K. exchanges.
2. Develop new forms of contracting for privatization that focus on "public – private partnerships."

3. Engage former U.S. Secretaries of Defense to support and work for the advancement of privatization efforts in the U.S.
4. Seek policy statements in support of privatization efforts from Secretary of Defense Cohen and the White House.
5. Develop a strategic vision for the military's privatization efforts, with the assistance of private-sector experts.
6. Work with the Office of Management & Budget, Members of Congress, and their staffs to ensure a thorough understanding of the programs proposed and gain their commitments to key initiatives.
7. Gain key military commanders' support for privatization.

List of Acronyms

Acronym	Definition
ARMA	Army Rocky Mountain Arsenal
BAH	Basic Allowance for Housing
BRAC	Base Realignment and Closure
CDMP	Community Development and Management Plan
CFQ	Competing for Quality
CONUS	Continental United States
DoD	Department of Defense
ETA	Early Transfer Authority
FY	Fiscal Year
IT	Information Technology
MHPI	Military Housing Privatization Initiative
milspec	Military specification
MoD	Ministry of Defence
NTC	National Training Center
OMB	Office of Management and Budget
OSD	Office of the Secretary of Defense
PFI	Private Finance Initiative
PPBES	Planning, Programming, Budgeting, and Execution System
PPP	Public-Private Partnership
PwC	PricewaterhouseCoopers
QDR	Quadrennial Defense Review
RCI	Residential Communities Initiative
RFP	Request for Proposals
RFQ	Request for Qualifications
U.K.	United Kingdom
U.S.	United States
VIP	Value Improvement Program

1. Introduction

On April 14-16, 2000, the Assistant Secretary of the Army for Installations and Environment convened a conference to compare the United States and United Kingdom experiences with privatizing military installation assets, operations, and services. The conference was held at Ditchley Park in Oxfordshire, England.

The purpose of the conference was to bring together U.K. and U.S. defense officials, U.S. Army leaders, and commercial contractors who supply military services, to discuss the British experience with privatization and explore its applicability to the U.S. Army. The list of participants is given in Appendix A.[2] The Assistant Secretary of the Army for Installations and Environment commissioned and distributed background reports designed to focus conference discussion on private sector involvement in three major areas of U.S. and U.K. interest: Housing and Other Base Facilities, Base Operations and Services, and Logistics.[3]

The conference was jointly chaired by the Hon. Richard B. Cheney, former U.S. Secretary of Defense, and Field Marshall The Lord Vincent, former Chief of Defence Staff for the U.K. Ministry of Defence (MoD). Both co-chairmen now represent private sector defense contractors. After an opening plenary session to introduce the themes of the conference, three small working groups — each dedicated to discussing one of the three areas of interest — met in concurrent sessions and then presented their conclusions to the entire assembly in closing plenary sessions.[4] Specifically, conferees were asked to consider the following questions:

- Housing and Other Base Facilities
  - How has the U.K. military recapitalized its housing stock?
  - What are the advantages and disadvantages of transferring ownership and management of housing facilities?
  - What roles should tenants and local communities play?
  - How should the Army forge new partnerships with industry?
- Base Operations and Services
  - How can the military retain control over privatized services?
  - How might the Army garner political support for private sector involvement?
  - What standards should govern private contractors' performance?
  - How can the U.S. provide both new and traditional services in nontraditional ways?
- Logistics
  - Which functions are appropriate for privatization?

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[2] Biographical sketches of the participants can be found in Appendix B.

[3] These background papers will be published as a separate volume.

[4] The conference agenda is included in Appendix C.

- What might a new military-industrial structure look like?
- How pervasive should private sector involvement be?
- What can the Army do to ensure sustainable support for privatization efforts?

BACKGROUND

As the United States Army seeks to improve the performance and reduce the cost of support services, greater use of private sector capabilities and resources is an essential strategic objective. While the United States and United Kingdom have reduced their force structures and defense spending substantially since their respective peaks in the 1980s, the U.K. has pursued privatization of defense activities and support services much more aggressively than the U.S.

The U.K. began to increase private sector involvement in defense activities in 1983, with the privatization of government-owned defense firms such as British Aerospace, Rolls-Royce, and Royal Ordnance. It also began outsourcing support activities such as aircraft maintenance, vehicle repair, management of government-owned dockyards, and food and janitorial services. During the 1990s, the U.K. MoD decreased support costs significantly through base closures, consolidation of training activities, public-private competition to provide services, and outsourcing of pilot training and equipment maintenance. In 1996, the MoD completed privatization of 60,000 military housing units in a single major transaction. In 1999, the first large-scale privatization of an entire British Army base was awarded.

Over the last decade, the Competing for Quality (CFQ), Private Finance Initiative (PFI), and Public-Private Partnership (PPP) programs have been used to promote increased efficiency in the MoD. Between 1992 and 1997, CFQ reviews of 163 defense activities were completed, representing a total operating cost of approximately £1.5 billion. Estimated annual savings of £335 million (23 percent) are expected to result from these reviews. Another £500 million of activities will be reviewed over the next few years.

In general, the U.S. Army is more constrained than the U.K. MoD in pursuing private sector involvement. Members of Congress tend to be protective of military bases, DoD civilian jobs, and military construction spending in their states or districts. As a result, Congress has placed a variety of restrictions on outsourcing and privatization. In particular, Congress prevents the Army from contracting out any support activity that employs more than 10 civilians without first subjecting the activity to public-private competition. The rules governing these competitions are laid out in the Office of Management and Budget's Circular A-76, originally written in 1966 with revisions in 1979, 1983, and 1996 (hence, they are often referred to as "A-76 competitions").

The Army had an active A-76 program during the early 1980s, but problems with the competitions caused Congress to pass the "Nichols Amendment," which was in effect from 1987-1995. This law gave installation commanders final authority to decide which functions to study for outsourcing. As a result of the Nichols Amendment, very few competitions were completed between 1989 and 1996.

In 1995, the Clinton Administration began a new push to increase outsourcing in order to generate funds for equipment modernization. Subsequent studies have estimated that outsourcing and privatization can potentially generate substantial savings. The 1997 Quadrennial Defense Review (QDR) recommended that the services compete, outsource, or privatize specific infrastructure functions, for an estimated annual savings of $2.5-$3 billion by FY04. So confident is DoD of achieving these goals that it has already removed $11 billion in projected savings from budget projections for the FY00-05 period.

In response to these recommendations, the Army has outlined an aggressive program of public-private competition. It has committed to compete activities employing 73,000 personnel (67,000 civilian and 6,000 military) with expected cumulative savings of $3.1 billion over the FY00-05 period. However, substantial obstacles to privatization exist. Private contractors are critical of the public-private competition process, saying it is too long and expensive, and that it is biased toward the government's bid.

In summary, Britain's efforts to privatize military support functions began later than those in the United States, but they have been more successful. This conference, "Privatizing Military Installation Assets, Operations, and Services," was envisioned as a forum for U.K. MoD officials to share insights about their privatization experience with U.S. Army leaders, with the goal of improving the Army's chances of successfully implementing its current privatization agenda.

ORGANIZATION OF THIS REPORT

The remainder of this report documents the proceedings of the conference. Section 2 summarizes the remarks made in the opening plenary session and provides the full text of the keynote address by the Assistant Secretary of the Army for Installations and Environment, which lays out the themes of the conference. Sections 3, 4, and 5 describe the discussions of the working groups on housing, base operations, and logistics, respectively. Section 6 summarizes the common themes addressed by the three working groups and the overall conclusions of the conference.

2. Opening Plenary Session

The Opening Plenary session of the U.S.-U.K. conference on privatizing military installation assets, operations, and services convened at 1630 hours on Friday, April 14, 2000. Opening remarks were made by the conference co-chairmen, the Honorable Richard Cheney, former U.S. Secretary of Defense, and Field Marshal The Lord Vincent, former U.K. Chief of Defence Staff. The U.S. conference host, the Honorable Mahlon Apgar IV, Assistant Secretary of the Army for Installations and Environment, then set the tone for the conference with a keynote address outlining privatization efforts in the U.S. and U.K. Mr. Martin Kitterick of PricewaterhouseCoopers (PwC) and Dr. David Chu of RAND, representing the organizations that prepared background materials for the conference, presented responses to Secretary Apgar's speech.

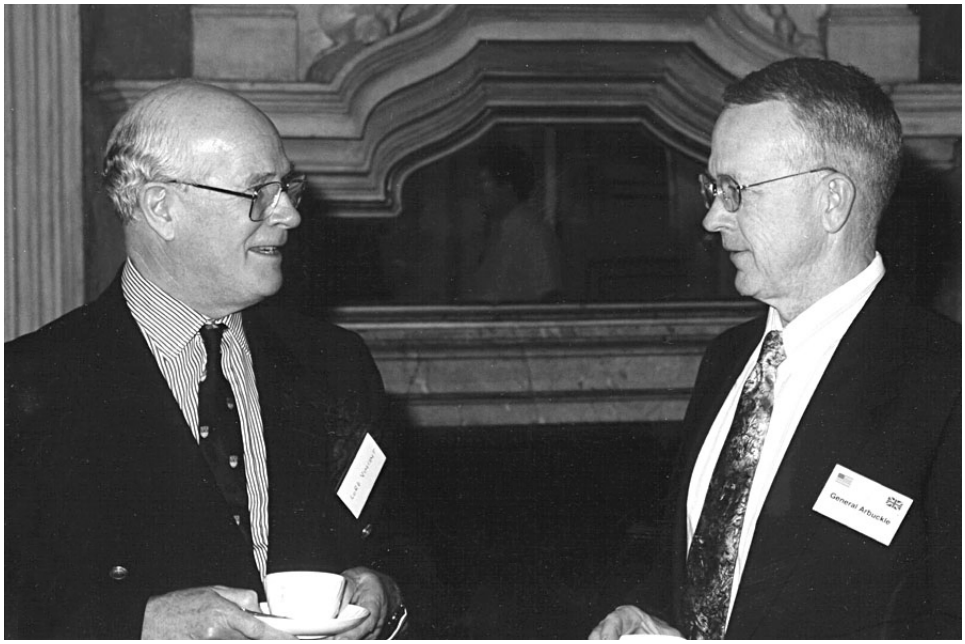
This section paraphrases the extemporaneous remarks of the co-chairmen and respondents, and provides the full text of the keynote address.

OPENING REMARKS

U.S. Co-Chairman: The Honorable Richard B. Cheney

I have approached the question of privatization of defense support services from several different perspectives: first as a member of Congress, then as Secretary of Defense, and currently as Chairman and Chief Executive Officer of Halliburton. Although Halliburton's core business is energy services, engineering, and construction, about 15% of our business relates to Brown & Root Services, which is involved the logistics contract to support the U.S. Army in the Balkans, and the ownership and operation of the Devonport dockyard in the U.K. Based on my experience, privatization holds tremendous potential for the U.S. military services, DoD, and taxpayers. My general impression is that the our British colleagues are far ahead of us in the U.S. in the extent to which they have adopted changes in culture, attitude, and style of operation that are required for successful privatization efforts.

The U.S. Department of Defense (DoD) faces a variety of internal and external obstacles to increasing private sector involvement in defense activities. As a defense contractor, I have found that policies and approaches to privatization can differ within the U.S. Army and the DoD. Another challenge for DoD is to develop a strategy for countering political resistance. This conference is not intended to focus on politics; rather, it provides a tremendous opportunity for us to share experiences, and to learn how the U.S. might take advantage of the concepts and principles that are embodied in the U.K. experience. Involving the private sector in installation assets, operations, and services would improve the U.S. Army's capacity to achieve its overall objectives.



U.K. Co-Chairman: Field Marshal The Lord Vincent

I have also approached the question of privatization both as a Ministry of Defense customer and as a private sector provider. This conference will review the evolving process of privatization from a wider perspective than has been done in the past, because participants from varying backgrounds can compare their respective experiences. In the past, we in the defense sector often failed to look for wider and more cost-effective support from the private sector. During the early decades of the Cold War, much of our military manpower was raised by conscription. Manpower was inexpensive and we tended to use it fairly extravagantly. Our main challenge was to provide it with relevant weapons and equipment, together with the overall capability and sustainability that would be needed if deterrence failed. In those days, we had few incentives to exploit emerging private sector practices, which we are now examining much more deliberately.

We now operate all-volunteer professional forces in both of our countries, and we have to attract people in a highly competitive market and pay comparable salaries. The DoD and the MoD are looking for people with the appropriate commitment and skills required for military operations, and these recruits are expensive to train. Thus, military manpower is much more costly today, and it is clearly in our interest to use it only where its special characteristics are essential and cannot be secured with better value for money and greater efficiency elsewhere.

In some ways, the Cold War era closed our minds to wider opportunities for private-sector support, and some of that culture of closed minds still remains with us. However, if one examines the more distant past, such as the Marlborough campaigns of the early 1700s, on his march to the Danube and the

battle of Blenheim, when he crossed the Rhine at Koblenz, he had contractors there with complete new uniforms and shoes for his Army. So it has been done in the past.

We also failed to notice how fast and how widely the private sector was changing its practices. When Margaret Thatcher began her energetic drive for privatization, it began to open our eyes to some of the opportunities that were available. The MoD's approach to privatization has been developed further since that time, particularly by the Front Line First study, which examined what we should do in-house to maintain our operational capabilities, and what we could seek to do more cost-effectively by looking at the private sector. A new dimension has been added by the Private Finance Initiative and the Public-Private Partnership initiatives that flowed from it, which transfer risk to the private sector and bring in private sector investment funds to support defense activities. One of our greatest challenges has been to change the MoD culture to look with more open minds at what is available in the private sector, and how these practices can be applied more effectively in the defense sector.

While many of the U.K.'s privatization efforts have been successful, some resistance remains. The just-in-time theory might be fine for making motor cars, but it worries commanders who have to face up to the consequences of a "just-not-in-time" outcome. We must now address the question of how far we should carry this process forward into the operational environment. This issue is ripe for exploration at this conference.

KEYNOTE ADDRESS: THE HONORABLE MAHLON APGAR, IV

Thank you, Secretary Cheney and Lord Vincent. Greetings and a warm welcome to all of you. Before my remarks, I would like to acknowledge and thank several people: Under Secretary of the Army, the Honorable Dr. Bernard Rostker, who supported my proposal for this conference from the first, and helped me navigate through the Scylla and Charybdis of our contracting system to enable it; our Ambassador, His Excellency Philip Lader, who took a personal role in encouraging several of you to attend; Dr. David Chu of the RAND Corporation and Mr. Martin Kitterick of PricewaterhouseCoopers (PwC), whose teams have done an insightful job of documenting the U.K. and U.S. experience to date; Sir Nigel Broomfield, our co-host, and his Ditchley team, who are providing this unique venue and superb support for this meeting; and in many ways most important of all, our British colleagues at the Ministry of Defence, especially Mr. John Spellar, Mr. Roger Jackling and Mr. Peter Ryan, who enthusiastically supported the project and helped to assemble this impressive array of talent. We are grateful to all of you for giving up two days on a weekend to join us, and we hope you'll depart with new acquaintances and new ideas.



Introduction

The U.S. Department of Defense, or DoD, and the U.K. Ministry of Defence, or MoD, have faced similar challenges in recent years. We have each downsized significantly, and are restructuring and modernizing our military forces. Faced with tight budgets, we must reduce excess infrastructure and overhead to sustain the warfighting mission.

To help meet these challenges, each defense organization has turned to privatizing, partnering, and outsourcing functions that support the warfighter. This trend toward greater reliance on the private sector — which for the purposes of this conference I will call "privatization" — has intensified, despite changes in political parties and administrations in both our countries. While I cannot speak for the U.K., I believe that reliance on the private sector in planning, financing, developing, and managing U.S. military installations will continue to grow, whatever the outcome of this year's presidential election.

We are hosting this conference to compare experience and to share knowledge about privatization. We have much to learn from each other about several core issues — for example:

- how to determine which responsibilities and functions are "inherently governmental" and which could involve the private sector, in some form, even if they have not in the past
- how to design and execute a "privatization strategy" for base operations and support services
- how to build broad support for privatization among legislators, as well as civilian and military leaders in the executive branch.

I'm going to begin our dialogue with a personal perspective on privatization — what it means, why it is important and what impedes it. Then, I'll highlight

some of the initiatives and pilot projects we are pursuing in the U.S. Army. Finally, I'll suggest an agenda of key issues to help crystallize our discussions over the next two days.

My perspective on privatization is defined both by my current role in the Army and my roots as an entrepreneur and consultant to many global corporations for over 30 years. I have also been struck by the common threads of experience that have been revealed in our recent discussions with the MoD, and in the RAND and PwC research we commissioned. With the foundation of knowledge and relationships we build during this conference, I hope that we will agree on ways to sustain the dialogue, to deepen the research, and to help forge new policies for privatization in supporting the common defense of our Nations.

A Perspective on Privatization

What Does Privatization Mean?

In the U.S. Army's Office of Installations and Environment, we see privatization as a means, not an end. We've adopted the theme "Privatization through Partnership" to convey the spirit of partnering with private enterprise to improve performance, reduce costs and attract capital. We need private-sector partners to help us become more efficient and effective in three main areas: the design, construction, maintenance, operation, and management of Army installations; the preservation and reuse of historic properties for both Army and non-Army users; and the conservation, compliance, cleanup, and site-disposal functions of environmental stewardship and land management.

Privatization has two components — attracting private capital to help fund our programs and operations, and enlisting private enterprise in designing and executing programs. Over the past few years, the Army's efforts to privatize utilities, family housing, and land cleanup have focused mainly on capital. The intent has been to leverage the Army budget through new sources of funds. Indeed, the Army's landmark housing privatization program was initially named "Capital Ventures Initiative," highlighting this purpose (we have since renamed it "Residential Communities Initiative," or RCI, to convey a more robust strategy of developing and managing as well as funding master-planned Army communities).

However, capital alone is not enough. Army posts also need to benefit from what I call the "4 Es" of private enterprise — the Entrepreneurship, Efficiency, Effectiveness and Expertise that industry — especially business, financial, and real estate services firms — can bring to government. This means leveraging the ideas, knowledge, and capabilities of private enterprise throughout our installations — from training ranges and motor pools, to housing and community facilities, to base operations and support services, to land conservation, restoration, and reuse.

This broad view of privatization differs from narrow definitions that describe the sale of government assets to the private sector. Through a wider lens, we can see that privatization for today's military is more about managing and delivering services than it is about ownership and control of assets. It embraces the process of transferring and inculcating the attitudes, ideas, skills,

and techniques of private enterprise into many current functions that are not uniquely military.

These characteristics are the real genius of our respective market economies. The financial capital we need is fungible — it can be provided by governments as readily as by investors. The intellectual capital of dynamic entrepreneurial firms, on the other hand, is a much scarcer resource the military must tap. In short, privatization through partnership is not only about new funding mechanisms and "best business practices," important as those are; it is also about ingenuity in the art and science of land use and development, asset management, and operating services on our military installations.

Privatization through partnership is, by definition, a two-way relationship — whether it's among individuals, within organizations, or between businesses and government. The "partnership" may take various legal forms. But the key to success is found in the process and character of the relationship — identifying mutual interests, gaining mutual understanding and respect, agreeing on mutual responsibilities, and maintaining effective negotiation throughout the partnership's life.

My definition of privatization is also different from those who use it synonymously with outsourcing. Outsourcing has been standard practice in our Army for some years, as it has in corporate America and in the U.K. It is the process of contracting with outside, independent organizations to provide support services faster, better, or cheaper than we can, mainly because those services are their core business, but not ours. Outsourcing does not shift responsibility for performance or change the nature of the service. It merely changes the way the service is supplied. For example, when we outsource trash collection or publication of the post newsletter, we retain the responsibility for ensuring that the service is accomplished on time and on budget — and that it meets our quality standards and other requirements. Outsourcing offers only limited scope for changing the way the military does business or realizing economies of scale from its investments.

Privatization, on the other hand, goes much deeper. It means shifting some or all of the responsibility for planning, organizing, financing, and managing a program or activity from the Army to private contractors and partners, while retaining some interest in the operations and benefits of the program. It may also involve transferring some or all of the use of Army assets, such as land, buildings, and equipment, from the Army to a private entity. The U.K. appears to have taken giant strides toward this end in its Public-Private Partnerships, and I hope we'll hear more in this conference about these efforts.

What Can be Privatized?

In my view, any military function or activity that does not have to be performed by military personnel — especially one that is mirrored by a large, diverse, competitive market in the private sector — is a candidate for privatization. This concept may seem self-evident, especially to you in the U.K., yet it is relatively new to our Army and to DoD as a whole.

Determining where and how to involve the private sector begins with the Army's mission. For each mission element, the Army unit can be either a provider or a customer of the resources it needs, or it can be both. Privatization,

in this context, means engaging with the private sector for the provider role wherever possible.

Privatization won't produce lasting benefits if it is seen only as a "quick fix" for immediate problems. The most effective privatization contracts are long term, and the Army must first accept the necessity of taking this step. In short, privatization initiatives should be viewed as part of a well-conceived, long-term strategy of organizational reform.

Military real estate is a prime strategic asset that requires a long-term view. Yet it is also a leading candidate for relinquishing the provider role. Nearly all military activities that could be privatized use real estate in some fashion. The Army's plant replacement value is estimated to be $220 billion — about twice the value of our entire equipment stock. And anecdotal evidence we've gathered with the help of PwC and others suggests that the market value is much higher. If we could shed excess real estate, "monetize" a portion of its value, shift the burden of building and maintaining it to others, and redeploy the savings to modernize our essential military-unique facilities, the Army would reap substantial benefits.

Our present strategy and structure obscure the fact that most military real estate is a dual-use asset: that is, it can be used either for a military purpose or a civilian one. Renovation and construction of dual-use real estate — as well as long-term service contracts and leases that include real estate — can be funded through private enterprise.

The Army can employ three main privatization structures:

- In "conventional" projects, the private sector designs and builds facilities, while the Army owns, manages, maintains, and funds them.
- In a "prime contracting" arrangement, the private sector maintains properties as well as designs and builds them.
- And in "full" privatization, the government acquires the rights to an entire package of facilities and services from private firms, consortia, or "systems integrators" — large, multi-functional organizations that increasingly service the real estate and facilities management needs of major corporations and governments.

The Army can privatize geographically — nationally, regionally, on several sites, or site-by-site. Or it can privatize based on the type of asset and use — infrastructure, training facilities, housing, storage, and shops as examples. Both approaches can work together, as the U.K. has shown by privatizing its entire military housing portfolio.

In evaluating the scope of real estate privatization, the most important "best business practice" of all is managing real estate as a portfolio — not as a series of separate facilities and projects — because the way in which any one parcel is used affects the value and logical uses of all of the other parcels — especially those in close proximity.

To develop a strategic view of its real estate, the Army is beginning to analyze its properties along two dimensions: their strategic importance — that is, the asset's relative value to the Army's mission -- and their resource requirements — that is, the amount and cost of resources that asset will use during its life-cycle. For example, the Army usually would retain and protect

assets with high strategic value and low resource requirements. But wherever possible, it would sell — or even give away — assets with low strategic value and high resource requirements, and reinvest in assets with higher strategic value. This latter category holds the most promise for privatization, because it engages the entrepreneurial imagination and capabilities of private enterprise in redeploying resources for higher economic value.

In addition to a strategic view, privatization requires unrelenting innovation. That means a continuing flow of fresh ideas — not only the few big ideas that set the course, like "build to local market standards" and "provide guarantees against military risks," but the hundreds of small ideas that actually drive the process of day-to-day change. In business, ideas have immediate, direct, unfiltered impact if they are pursued with passion and perseverance. One of the Army's main management challenges is to allow sharp ideas to stay sharp and focused amid the dynamics of day-to-day politics and organizational processes.

Why Do We Need Private Partners?

Historically, the military has tended to avoid partnerships, for understandable reasons. Army posts were designed to keep people out, not to provide them easy access. Moreover, military culture values self-sufficiency: in time of war, soldiers depend on themselves and their team members, not on "outsiders." But our current aspirations for modernization, constrained by our financial limitations, force us to look outside our own ranks for help. There are three main reasons for this change in course.

First, after years of major force reductions, we are now saddled with a large number of underutilized properties, equaling millions of square feet of buildings and acreage. We simply cannot afford to carry this excess inventory of land, buildings, and other facilities. It diverts attention and resources from readiness needs such as modernizing the force and improving our soldiers' quality of life. Privatization can be the means to leverage the experience and techniques of private enterprise in releasing economic value that is now locked up in underutilized and illiquid property assets for other Army requirements.

The second reason we need private partners is to shorten the recapitalization cycle and leverage our investments in construction and maintenance, environmental compliance, land cleanup and disposal, and base operations. We need immediate action and breakthrough solutions. At our current rate, we recapitalize our facilities on average every 200 years. Our $6 billion backlog of inadequate Army family housing would take at least three decades to clear under current budget limits and procedures. Because government budgeting lacks the flexibility to incorporate the "spikes" required for capital investment, privatization can convert those spikes into annual operating expenses.

The third reason is that private enterprise can help us "see" and capitalize on the military market in new ways. Consider the consumer market for goods and services, both on-post and off-post. By one estimate, individual military consumers spend $1.8 trillion every year — and this market is growing. While its size alone is dramatic, an equally important fact is that military people are superb customers — they pay on time, they have predictable needs, they maintain their affiliations, and they seek value for money. The active-duty



soldier is only the visible capstone of this market. Its base is the large and growing pool of military families, reservists, retirees, and veterans who are sustained by deep institutional loyalties and substantial benefits. Our installations now service a large percentage of this market, yet we forego much of its spending power. To improve our installations, we must capture more of this market in concert with area businesses and other providers.

Obstacles in Forging Public-Private Partnerships

With all this potential, one would think it would be easy to partner with private enterprise. But alas, it's not. We face enormous obstacles to privatization in the U.S., and I've been intrigued to learn that our British colleagues have not found it much easier. Fortunately, you in Britain have had far more recent success in this area than we have, and you have already tackled many of the difficulties we are just now addressing. In this conference, we hope that we can learn from your experience and that you'll help us leapfrog some of the barriers that we face.

The first — and arguably most fundamental — obstacle is the lack of an "Innovation Motive" to create ideas and apply ingenuity in meeting needs and solving problems. For example, as an entrepreneur, I believed I could do anything to create new products and services that the law does not proscribe. But, as a government executive, I am told I can act only when enabled to do so by authorities that prescribe the boundaries of action. That's a crucial difference.

Because of this mind set, most government executives I work with are filled with caution when they face privatization. One of my most creative staff members puts it this way: "When a new way of doing things is first suggested, the business executive asks, 'Is there a need? Will it make money? When can we

start?' The government executive asks, 'Do I have the authority? Is it funded? Am I covered by an existing policy?'" The difference in institutional climate is profound: one attitude promotes action and clear direction; the other invites delay and obfuscation.

This principle of acting only when explicitly authorized can be debilitating. For example, in our Pentagon office, we identified more than 20 changes that could improve efficiency and/or effectiveness. All of the proposals have precedents in corporate America. But only a few are presently authorized by law, covered by regulations, and accepted by the institutional culture. Implementing this package of changes, or any number of other improvements, would require us to press for new legislation and/or revised regulations, and to change the culture — an arduous and time-consuming process.

Procurement policies and procedures are another major obstacle. Even when privatization is authorized, the Army is still impeded from managing in the most efficient manner. Politicians are understandably protective of military bases, civilian jobs, and military construction spending in their districts. As a result, any support activity employing more than 10 civilians cannot go directly to private contract — Congress requires that it be subject to a public-private competition. Under these rules, government employees must be given a chance to streamline or reengineer their processes for comparison with the best private-sector bid.

The good news is that competition of this sort can lead to 10 to 30 percent cost savings and better-quality service. The bad news is that the process is slow and cumbersome, and drives competition down to the lowest level of activity, placing a large resource burden on the Army and the bidders. Furthermore, the private sector argues that these competitions are unfairly biased toward the government's bid, because private firms must base their cost projections on actual past performance, while the government may base its projections on hypothetical estimates of what it could achieve if it streamlined its organization. Had major corporations been subjected to such limitations in the past decade, they would not have achieved the turnarounds and business process reengineering successes that have helped fuel our current economic boom.

In a further attempt to achieve savings from public-private competitions, DoD asked the Services to designate positions as "commercial activities," which can be subject to competition, or "inherently governmental," which cannot. But these definitions limit innovative contracting arrangements. Broader societal goals also come into play. For example, contract set-asides are required for small, minority-owned, and women-owned businesses, making it more difficult to bundle small contracts for individual services into broad contracts for a range of related services. And some activities, such as security guards and fire fighters, are excluded from public-private competition without regard to the specific requirements of individual installations or the opportunities for cost savings and efficiencies.

When we do partner with the private sector, our selection, payment, and administrative systems remain cumbersome and inflexible. Part of the problem is a risk-averse, "them" and "us" culture. We micromanage contractors and spend heavily to audit small amounts. The Request for Proposal process, which

I'll discuss later, requires overwhelming detail, rewarding bidders for their expertise in navigating the process rather than solving the problem. Task orders routinely take weeks to obtain. Payment rules are complicated and onerous; payment delays for new contractors may run to several months. One of our major new service providers under privatization documented a 36-step procedure for each monthly bill against an agreed scope of work, and experienced a 90-day delay in payment of a $300,000 invoice because they didn't include a self-addressed stamped envelope with their bill! True tales like this deter the most able partners from working with us. And while these problems can be readily identified and conceptualized, they are very difficult to fix.

From my personal experience, the procurement system has several basic limitations. First, the division of responsibility between the "client" and the "contract authority" — a principle that is intended to avoid conflicts of interest — can delay and distort contractor selection. Next, the boundary between government employees and contractors is an increasingly artificial but very costly distinction as one attempts to forge seamless teams that combine the best talents of both sectors. Finally, the typical contracting officer's training and predilection toward "least cost" over "best value" influences selection and contract administration, often resulting in lower-quality services and even higher costs to the government in the long run.

With the division of responsibility come the "gatekeepers." A host of lawyers and administrators ensure compliance with a labyrinthine network of rules and regulations, including Acquisition Regulations, funding procedures, legal interpretations, and "administrivia." All these requirements have important justifications, and failure to follow them can have serious consequences.

Herein lies the next major obstacle: the "excessive interest" taken in privatization programs at several levels — by legislators, DoD, and internal staffs. In government, new programs — and the resources that support them — are constantly under a high-powered microscope. Oversight can quickly descend to micro-management at an excruciating level of detail, thereby creating an environment that frustrates rather than encourages innovation. Our housing privatization pilot program involves four major Army installations, more than 16,000 housing units, total value of over $6 billion, and cost savings to the government of nearly $1 billion. Yet we recently spent over 100 hours of executive and staff time responding to questions about an $11,000 expense. The expense was justified, but it had to be researched, explained verbally and in writing several times, and even wound up among the questions for the record in my recent Congressional hearings. The $700 hammer and the $3,000 telephone are legendary military procurement embarrassments. But privatization has produced a business service equivalent — the simple $1,000 analysis that became a complicated $10,000 bill because of this "excessive oversight" factor.

An additional obstacle is closely related to micro-management: the military specification, or "milspec." While the present Administration has been calling for change, the military has a long history of defining its requirements from whole cloth — as if no other institution had ever met the same or similar needs before — and then specifying the products or services required to meet those

original requirements. Even tradition-bound corporations know they can't indulge in this sort of luxury. One of the axioms in business policy is that an organization's needs should first be defined in terms of products and services that are already available in the marketplace. The art of management and innovation lies in using stock items whenever possible in new and better ways — not inventing new stock. Custom-tailoring is simply too expensive for all but unique or esoteric requirements — and if a military support service requirement is so unique or esoteric that it requires customized solutions, one must question whether its proponent has applied good, disciplined business judgment and a strong dose of common sense!

In grappling with "military unique" standards and specifications, we face two core issues: first, is the "milspec" truly unique to the military, or simply the military version of an otherwise commercial product or service?; and, second, is it essential to apply the "milspec" globally, or can it be adapted and sourced in the local market? Specializing an asset or restricting its potential uses diminishes its value. In other words, milspecs promote an "artificial" micro-market for defense — with its attendant price premiums — instead of the broad, competitive "real" market of the wider economy. Thus, the ideal military support facility or service is a generic facility or service so it can be used by anyone with a similar need.

The next obstacle resides in our own organization and skills. Our defense work force is aging; we will lose about 60 percent of our civilian employees in the next five years. With attrition comes loss of know-how and institutional memory. Where will we find replacements for these valuable workers? This problem, of course, is also a potential opportunity to replace people who may have hindered innovation. How will we compete with the private sector for skills? Smart procurement requires "smart clients." When negotiating with private firms for privatization, we must have both management and technical skills on our side of the table. Army lawyers acknowledge that they need help in structuring privatization deals and facilitating working agreements, in addition to opining on broad legal issues. We have already begun addressing this issue in the Residential Communities Initiative, or RCI, with a number of proposed changes that will help us acquire the skills we need.

On the other hand, privatization will necessarily bring about reductions in civilian staff, and this creates new problems in terms of due process for personnel actions, working with professional unions, and ensuring that we keep severance costs as low as possible. Lack of hard information on these costs makes planning more difficult. Our information systems themselves constitute another obstacle. We collect and array a mind-numbing amount of data on installation management and base operations, devoting an enormous amount of time gathering it and debating its accuracy. But we often lack a strategic view of our data as it applies to base operations, services, and facilities — that is, we do not have a clear view of what information is really important, and how to get it to the right people at the right time. Strategic information, and the information technology required to collect, disseminate, and use it, would be a significant enabler of privatization, flattening our hierarchical organizations, involving

stakeholders more quickly, and helping leaders achieve the rapid buy-in that is critical to organizational change.

A final obstacle to privatization is our decentralized, stovepiped management structure. This structure makes it difficult to establish strategic goals for the Army's overall privatization effort. Issues are resolved slowly and weakened by excessive compromise. Progress is impeded not only by bureaucracy, but also by lack of appropriate training at executive as well as staff levels. Our practice of giving commanders autonomy results in a culture that prizes the "can-do" attitude, but often balks at asking for help, especially from those outside the military.

Toward Privatization: Some Recent Army Initiatives

Despite these obstacles, the White House and DoD have become advocates of privatization and outsourcing, to reduce support costs and increase value for money. A number of you here today have helped to pioneer several major U.S. Army initiatives that parallel the U.K.'s more expansive strategy. The U.K. experience and some of the lessons learned for the U.S. are profiled in the RAND and PricewaterhouseCoopers background papers. A few of these are highlighted below, from adapting "best business practices" to direct private-sector involvement.

Best Business Practices

One of the most fruitful areas of improvement has come simply from adapting some of the private-sector's best business practices.

For example, DoD is producing auditable financial statements for the first time, and is also making extensive use of Working Capital Funds — similar to "trading funds" in the UK — which require supplier organizations to cover their costs through charges to their internal customers, and make customer organizations more aware of the costs of these services.

The weapons-systems organization has reduced the use of military specifications, increased purchases of commercial off-the-shelf items, and rewritten our Federal Acquisition Regulations to make use of commercial contracting practices. However, these regulations are still geared mainly to contracting for "goods" rather than services. Similar changes are sorely needed in military base support operations, services, and facilities, where our hidden overheads and operating costs appear to substantially exceed those of the private sector.

Procurement reform has been a consistent theme throughout the 1990s in DoD, and shares many features with MoD's "Smart Procurement" program. It is an essential ingredient of privatization because current contracting methods deter many qualified firms from partnering with us. For privatization to work, we need to make government contracting easier, cheaper, and less risky. Then we need to involve our private partners in planning, as well as executing, our programs and projects.

We faced this challenge in the Army's housing privatization program. Industry leaders told me that our procurement system was a major obstacle to



their participation. To streamline it, we designed a slimmed down Request for Qualifications, or RFQ. This contrasts markedly with the traditional, weighty Request for Proposal, or RFP, where contractors bid on a plan that the Army has described in exhaustive detail. RFPs are costly and time-consuming for both the Army and the bidders. And significantly, they preclude contractors from applying their ingenuity to redefining the project concept and plan during the bidding process.

The RFQ, on the other hand, focuses on track records instead of bids. We seek leading developers who have actually built and operated outstanding facilities. The RFQ template defines the qualifications we are seeking in prospective partners, lists the selection criteria, and lays out background information about the installation and the needs to be met. The qualification statement asks the applicant for a preliminary concept and business approach to the project; documentation of financial resources, management, and organizational capabilities; and — most important — demonstrated experience in projects of comparable scope and complexity. Once the partner is selected, the Army and the partner jointly prepare a Community Development and Management Plan (CDMP), which sets forth the terms of the partner's relationship with the government over the life of each project. The agreement includes incentives and sanctions to assure performance.

We have recently launched an initiative known as the Value Improvement Program, or VIP. Its objective is to reduce both front-end capital costs and ongoing maintenance and operating costs of government facilities. This program seeks to apply best practices that are at the core of successful private real estate businesses and corporate real estate management. In large, complex private-sector projects — such as apartment and office buildings, hotels, hospitals, and schools — significant savings have been achieved both from fresh insights about

the project concept and rigorous analysis of trade-offs among the preferences of customers and engineers.

Value analysis differs from value engineering — a traditional method used widely in construction — because it requires executives and technical specialists alike to rethink the entire end-to-end process of planning, developing, and managing buildings, from their initial concept and definition of requirements to their ongoing use — and even reuse — over time. From initial discussions with MoD, I understand that you have a similar initiative underway.

Housing and Facilities Management

Turning to specific privatization initiatives in the three areas of consideration for this conference, housing privatization is a major U.S. Army priority, as I have already mentioned. Our traditional methods of funding and operating housing cannot meet the critical housing needs of America's soldiers and their families. Over three-quarters of our existing housing stock is inadequate, and funding is insufficient either to revitalize and maintain it or to replace it with new housing. While we have added more than $250 million to the Army's military construction program for the next five years, we have concluded that we simply cannot solve this acute problem without privatization.

Under the 1996 Military Housing Privatization Initiative Act (MHPI), Congress authorized the Army and other Services to turn over the design, construction, maintenance, and management of entire residential neighborhoods on Army posts to private developers. In the Army's RCI, we will partner with homebuilders and developers to build, manage, and maintain residential communities on Army posts. RCI encompasses not only housing but also the amenities and support services that most Americans enjoy in their neighborhoods and communities. The program uses a new set of tools provided under MHPI to attract homebuilders and real estate developers as partners in our long-term, "whole-post" community development and management program. These tools include various financing features, incentives, and guarantees; the ability to design and build to local market standards; and the opportunity for the developer to provide a limited array of support facilities such as mini-parks and community centers to enhance the housing.

RCI projects do not commit Army resources beyond soldiers' housing allowances and any guarantees we might offer to ameliorate unique military risks. The Army leases its land to the developer and regulates its terms. We negotiate the housing designs and standards with the developer based on comparable properties available in the local community. Soldiers pay rent to the developer, so if the privatized houses don't meet the market test — acceptance by soldiers — soldiers can choose to live elsewhere off-post and receive their housing allowance. The developer has a clear incentive to provide value for money.

Our first major housing privatization project is at Fort Carson, Colorado. The contract calls for the developer to renovate the existing inventory of 1,823 units, build 840 new units, and operate and maintain the total inventory for the term of the contract, including periodic upgrades. The contract is for 50 years with a 25-year renewal option. The premise is that this large-scale, long-term arrangement will motivate the contractor to renovate and build quality housing,

because it is responsible for maintaining and continuing to revitalize what it builds over the project's entire life cycle. The developer will invest about $220 million in renovation and new construction in the first five years.

In the first two months of the Fort Carson contract, the developer doubled the maintenance force and opened more than 200 unoccupied housing units. Such strong initial outcomes pave the way to significantly more and better on-post housing within a few years. We are working closely with Congress to test RCI through pilot projects at three additional posts: Fort Hood, Texas; Fort Lewis, Washington; and Fort Meade, Maryland. These three projects involve the stripped-down RFQ procurement system and CDMP process I discussed earlier. This gives us the opportunity to evaluate the merits of traditional and alternative procurement systems operating in roughly similar situations. By 2010, we anticipate that 16,000 quality housing units in attractive neighborhoods will be provided under RCI. The pilot program alone will help us save over $800 million and avoid $1.1 billion in new funding, while leveraging public capital 10:1 — that is, every dollar of government funding will produce ten dollars of private capital over the 50-year project life.

Historic properties present another challenge that we hope will benefit from public-private partnerships. The Army holds one of our Nation's largest portfolios of historic properties, including 12 National Historic Landmarks — such as Fort Sam Houston, Texas and West Point, New York — and more than 12,000 historic buildings that are listed on, or are eligible for, the National Register of Historic Places. During the next 30 years, more than 70,000 additional buildings on Army posts will reach 50 years of age and will need to be evaluated for their historic significance in accordance with the National Historic Preservation Act. These properties cover a broad spectrum of historic eras, architectural styles, building types, and land uses. They are more than bricks and mortar — they are an important part of our national heritage and the Army's heritage, telling the story of America one Army post at a time. We intend that the most significant properties should be preserved to inspire tomorrow's generations. We also know that thousands of World War II-era buildings with no redeeming architectural or historic value should be demolished. But we obviously need a systemic solution and a long-term strategy to use and polish the "jewels" as we eliminate the "junk."

The age, size, and diversity of the properties make this an especially difficult portfolio to manage. Yet it also presents significant opportunities for creative ways to reuse old buildings. For example, we are partnering with a private developer to convert the abandoned Brooke Army Medical Center at Fort Sam Houston for commercial use on a long-term lease. And the non-profit Friends of Historic Fort Sam Houston have restored that post's historic Stillwell House. Their improvements were a gift to the Army, and the property is now available for both Army and community functions. At the portfolio level, we are exploring the possibility of an Army Historic Properties Trust Fund and other mechanisms to recapitalize our historic real estate. With the help of the National Trust for Historic Preservation and leading private historic property developers, we want to mirror the substantial leverage of public capital that has resulted from the rehabilitation tax credits and other incentives for private enterprise. Our

challenge is to design policies and management processes that encourage full utilization of these unique assets and make economic sense.

Base Operations

U.S. Army posts — like our Air Force and Marine Corps bases — are small cities: in addition to housing, they have office buildings, maintenance facilities, shops, restaurants, schools, hospitals, roads, utilities, police and fire protection, and — of course — motor pools, firing ranges, training facilities, and other military-unique facilities. Even temporary bases like our camps in Kosovo are also surprisingly complex. In management terms, military bases are more intricate than most sophisticated weapons systems — mainly because they are human communities, not just facilities. Yet we do not devote to them the same high level of management sophistication in organization, information, institutional systems and support.

Privatization and outsourcing offer opportunities to relinquish the day-to-day management of base operations and activities that are not core competencies. The Army has launched several innovative programs for in-garrison and deployed base operations. For example, Brown and Root Services has been providing base operations, support, and logistics services in the Balkans since 1995. These include construction of temporary housing, food services, road repair, waste management, power generation, and transportation.

In the early 1980s, the Army hired a civilian contractor to establish the National Training Center, or NTC, on Army-owned property. The initial contract covered a variety of functions, including traditional base operations, maintenance of a large pre-positioned fleet of training vehicles, and other logistics functions to support visiting maneuver brigades. However, NTC decided that the scope of this umbrella contract was too broad, and divided it into two separate contracts for base operations and fleet maintenance to improve performance and to provide better management information to customers. Contract management costs increased initially due to this change, but both contracts are now cost-efficient.

As in the U.K., we are in the process of privatizing or contracting out management of water, sewer, natural gas, and electric utilities by transferring ownership, operation, and maintenance to private firms or special local authorities. In fact, this was one of our Army's earliest privatization initiatives. To date, we have privatized, or exempted for security reasons, 45 systems, and we plan to evaluate 275 additional systems for privatization in the next three years. A powerful tool in this transition is the Energy Savings Performance Contract, in which private firms invest capital and provide equipment for infrastructure improvements such as high-efficiency boilers, heat pumps, and lighting.

In telecommunications and IT, we face a requirement of nearly $2 billion to upgrade the outmoded "information infrastructure" on our posts. This is an ideal opportunity to transform the existing patchwork system by privatizing the delivery of advanced communications services — combining software, bandwidth communications, and e-service solutions — through a consistent and unified approach from the start, with minimal investment of public funds.

A new environmental tool — the "early transfer authority" or ETA — has helped us clean up and reuse contaminated land. In the past, the Army traditionally has performed the cleanup before transferring properties to local communities for redevelopment. The ETA encourages private investment and entrepreneurship by shifting responsibility from the Army to the purchaser. For example, at the Sunflower Army Ammunition Plant in Kansas, where a shrewd wizard named OZ wants to develop a theme park on Army property. The OZ Entertainment Corporation has offered to carry out the site cleanup in exchange for a credit against the property's purchase price, using the ETA. Another incentive for the developer is tax-exempt revenue bond financing. Under this arrangement, the Army will avoid substantial spending on environmental cleanup — a win-win for both parties.

At the Army's Rocky Mountain Arsenal, or ARMA, we are using another novel management concept — called "pay for performance" — to accomplish DoD's largest cleanup effort. The Army, the U.S. Fish and Wildlife Service, and Shell Oil Company have joined forces to transform ARMA into the nation's largest urban wildlife refuge. All money set aside for fees is at risk and subject to the Army's assessment of the partner's performance. The prime contractor does not directly perform the cleanup, but designs the projects and manages a cadre of sub-contractors, with responsibility for ensuring that the cleanup schedule is met and stays within cost guidelines. Savings in the first year of the ARMA contract are already being applied to meet other needs in the Army budget. Secretary of Defense Cohen has declared this partnership a "national model."

Logistics

Over the past 20 years, most major corporations have transformed their logistics systems from massive, "just-in-case" inventories, to lean, "just-in-time" inventories, based on faster, more frequent deliveries of supplies as required. The Army is now beginning to operationalize this fundamental change.

We outsource approximately one-third of our depot-level component repairs, and have some contractor-operated Directorates of Logistics on our posts. In 1992, the Army implemented working capital funding of depot-level reparables that resulted in a 20 percent reduction in demand for spare parts and DoD-wide savings of about $500 million per year. Army units and installations began repairing more items and redistributing some items that received low credit in the supply system. Return rates increased significantly as support activities reduced inventories or returned items to wholesalers for repair.

These activities reduce spending by logistics customers, but it isn't clear that they reduce overall Army costs because the prices and credits we charge do not always correspond with actual repair and replacement costs. This can result in customers establishing their own repair and redistribution systems. To address this problem, the Army is planning to reduce the financial incentives customers may have to set up alternative systems.

The Army is also adopting innovations that have proven successful in private sector logistics. To create a more effective supply chain, we adopted Velocity Management — a systems approach to delivering products and services. It requires the Army to overcome functional and organizational limitations both internally and externally.

Making Privatization Work: Some Current Hypotheses

Our privatization efforts are not progressing at the same rate as those in the U.K. But it's fair to say that both the U.S. and U.K. privatization experiences to date point toward some broad hypotheses that I hope will be tested at this conference.

First, broad-based support for the concept of privatization must be built among key civilian and military officials and legislative leaders. We must find more effective ways to demonstrate the benefits of privatization and contrast this with the costs of maintaining the status quo.

To ensure the success of privatization initiatives, we also need talented staff, adaptable structures, and a process for sharing lessons learned across functions and organizations.

Third, we must rewrite the rules. The U.K. did this by setting up a task force with two teams: a policy team of a dozen civil servants, backed by external consultants; and a projects team headed by a creative financier and staffed by a dozen "best-in-class" private sector professionals. They not only rewrote policy and guidelines for public-private partnerships but championed the "change management" program in MoD and throughout government. We in the U.S. could save years by adopting this model.

Next, we must recognize that real estate, facilities and support services are what we use, not what we do. The more we can move from being a provider to being a procurer and client, the better off we are likely to be. For every function, we need to ask ourselves, "Why are we doing this in the first place?", "Do we need it?", and "Can someone else do it better, cheaper, or faster?"

In negotiating with private sector partners, we should control outcomes by setting standards and service levels, not by focusing on inputs. We need to become smart clients and customers for the private sector, ensuring that we do business in a way that attracts and retains quality providers.

Finally, a strategic view is imperative. Privatization requires a long-term view of resource management that must be focused on, and aligned with, war-fighting objectives. Strategic planning should be applied to real estate and support services for several reasons. First, it ensures that such investments are aligned with the Army's mission, focusing specifically on core sites and personnel. Next, it permits the Army to take into account full life-cycle costs. And last, it allows the Army, DoD and Congress to match the total requirement for funds with the potential sources of funds, including self-generating sources from monetizing our real estate.

This strategy needs to be developed at the top of the organization, with a minimum 20-year view of the needs and opportunities. But until we develop that long-term view, we must find innovative ways to work within the existing system to begin achieving our privatization goals.



Issues for Consideration and Discussion

As we turn to the conference group discussions, I hope you all will contribute your knowledge, experience and ideas — especially those that can be implemented quickly, as well as those that are longer-term solutions. Here are six key issues for consideration during the conference:

1. How can we facilitate a strategic approach to public-private partnerships? How can we balance privatization, outsourcing, and process reengineering as we plan support functions and facilities to ensure that military needs are met? How can we integrate "stovepiped" projects at individual posts in a way that best serves the Army as a whole? And how can commanders be motivated to take an installation-wide perspective that yields the right mix of privatization, outsourcing, and internal process reengineering? The Army Planning Guidance document and the projections that stem from it are a basis for addressing major issues at Army policy level. Fundamental questions on privatization and contracting are appropriate topics to address at this level. The Planning, Programming, Budgeting and Execution System, or PPBES, could be amended to raise key issues for the Army Leadership, the Office of the Secretary of Defense (OSD), the Office of Management and Budget (OMB) and Congress. As we already have the structures to put strategy-based policy-making into effect, we should use them.

2. How shall we identify and prioritize opportunities for public-private partnerships? How should we define the scope of the activity, determine whether contractors should own and/or operate the assets and services, and allocate risks between the customer and the supplier? What sequence of

opportunities will best meet high-priority installation needs while minimizing potential opposition? How should posts that are less attractive to private enterprise be prioritized with the most attractive locations? The U.K. has achieved an active market for the purchasing and supply of military assets and support services over a 20-year period. If the U.S. were to adopt a similar approach — for example, letting long-term contracts to the private sector for the supply of whole-base accommodation and support services — could we do it any more quickly?

3. What are the best ways to attract, select, and work with highly qualified partners? Can we achieve excellence and "best value" for the soldier and the taxpayer in a system that dictates "fair and open" competition? Many of the privatization approaches being adopted in the U.K. and elsewhere lead to a high level of reliance on a few private sector suppliers who in turn subcontract with a wide array of specialized businesses — large and small. Is this an obstacle or a benefit? How can we create true "partnerships" with our suppliers and avoid the traditional "them" and "us" relationships? How can we align the goals and incentives of buyers and suppliers, resolve disputes, and establish productive long-term relationships with contractors?

4. How do we ensure that the Army receives full value from its public-private partnerships? Successful contract management depends on the quality of our contractors, the design of our contracts, and the skills of our contract managers. We must be well represented in negotiations — supported by the skills, expertise, training, and experience that are appropriate for complex, high level, outcome-based contracts. After negotiations, we need to have equally skilled contract managers to implement agreements for the benefit of Army units and ultimately our soldiers. Success will also depend on our ability to identify and manage acceptable risks. To be successful innovators, we must learn to be successful risk-takers and risk-managers, encouraging leaders to develop and apply sound risk management techniques. Policy makers must also understand the nature of risk in new proposals, and recognize that risk and frequent course corrections are inherent in privatization as they are in any innovation.

5. How should we establish standards for product, facility, and service quality? In the U.S., achieving quality will require Army leaders, OSD, and Congress to commit to clear standards and maintain them over the long-term. What impedes this commitment? And how do we find robust linkages between service levels and factors like military capability, motivation, and recruitment and retention levels? Furthermore, how do we leverage the knowledge and capabilities of private enterprise, design performance measurements and contract incentives, and monitor our private sector partners to make sure we're getting what our soldiers need, not necessarily what our administrators, contracting officers, and technicians want?

6. And finally, given the potential advantages of public-private partnerships, how can we achieve broad-based support for a more

proactive approach? To reduce the cost of support activities, how should we gain the support of senior military and civilian personnel, legislators, and soldiers who ultimately are the primary beneficiaries? What legislative, organizational, and cultural changes need to occur? What experimental initiatives, such as pilot projects and "reinvention labs," will jump-start a new strategy? And what aspects — if any — require an all-out, Army-wide "campaign plan" such as that now underway to drive Army Transformation?

Our efforts here in the next two days should benefit our respective countries and their armed services. The cross-pollination of ideas for privatizing military assets, operations, and services should provide us with renewed vigor for increased efficiency and effectiveness when we return home. We have much to learn from each other. And as I said at the outset, I hope we might establish an ongoing forum to help institutionalize the policies and practices about this critical subject in our respective defense establishments.

Thank you.

PWC REPRESENTATIVE: MR. MARTIN KITTERICK

I have acted as a financial advisor on privatization to the U.K. MoD since the early 1990s. I am currently leading a U.K.-U.S. PwC team that has developed background material for the conference on the U.K. experience with defense privatization, the U.S. Army's real estate portfolio, and potential privatization approaches for U.S. Army real estate and supporting services.

Although the MoD has been very progressive in its attitude toward involving the private sector in its activities, some parts of the MoD have less willingly embraced the initiatives they have been asked to implement. On the whole, the track record is impressive, and for the most part, successful. However, U.S. participants should understand that the process has been a 20-year evolution, and not a revolution, despite the political imperatives that initially underlaid the process. This evolution has encompassed asset and business sales, various outsourcing initiatives, and most recently, the Private Finance Initiative (PFI). Although the PFI was slow to take off, both philosophically and practically, it is now a major plank of U.K. government and MoD policy.

PFI is rooted in two major principles: first, that in many cases, there is a compelling argument for the public sector to be a procurer of services rather than a provider of services; and second, that in any enterprise or project, risks should lie where they are best managed. If these principles are accepted, it is logical for the public sector to consider buying a required output, rather than specifying the inputs. Specifying output allows the private sector to apply its skills and capital to delivering that output most effectively, and transfers risk and responsibility to the private sector, but only the risk that can be better quantified and managed by the private sector than by the government.

PFI also places greater emphasis on life-cycle costing. The MoD has to consider both the capital cost of the project, and the cost of maintaining assets in

good condition over 20 to 30 years. This combination must be considered realistically, or there is a danger of making the wrong investment decision. Although it is important to emphasize value for money rather than lowest cost when comparing different procurement options, the MoD has achieved savings of 30 to 40 percent of the total net present value of project costs using PFI.

In Britain today, PFI is considered an option for almost all significant support expenditures in the MoD, including some of its most vital assets. It has been applied to a wide range of activities, such as training facilities, married quarters housing, and logistics support. It has even included secure and sensitive facilities, such as the MoD Main Building and the government's communication headquarters. As an example, I would like to discuss the PFI project for the MoD Main Building, on which I have been an advisor to the MoD.

Those of you who have visited or worked in the MoD Main Building know that it is an outdated building which is not geared to the working practices of the 21st century. The MoD decided to adopt a PFI approach to provide new office accommodation on the existing site. As an historical building, the shell will be gutted and redeveloped while activity continues in parts of the existing building. A private sector consortium will provide office accommodation and services under a thirty-year contract. The consortium will design, build, finance, and operate the building and provide a range of services, from office support to catering. The capital value of the project is greater than £400 million, and the consortium will raise over £500 million in debt and equity to finance the redevelopment. They will be responsible for the maintenance of the building over the 30-year contract term. At the end of the contract, the building will revert to MoD.

The consortium will ensure that the building works properly and that it meets the needs of its users. The packaging of many related supporting services into a single contract and the integrated approach to the design of the building and its life-cycle maintenance ensure that responsibility and risk are not split among many different parties. A single contractor will be responsible for the whole project. In return, the contractor will receive annual payments for the term of the contract, but these payments will be subject to deductions for poor performance. The PFI project also has the advantage of smoothing the capital expenditure profile that the MoD would otherwise have to fund in the next three to five years.

This contract is expected to provide a greatly enhanced, flexible, working environment to MoD headquarters personnel. It is important to emphasize that management control is not lost under these arrangements. It is exercised through the terms of the contract. Military and civilian users will be able to communicate their day-to-day needs to a responsive service provider whose payment depends upon the availability and the quality of the services provided.

In addition to real estate, the PFI model is being expanded to important logistics functions, including such major equipment projects as the Future Strategic Tanker Aircraft and the Heavy Equipment Transporter. These projects are pushing back the boundaries of PFI and raising difficult issues for the MoD, the armed services, and the private sector, including questions about the

respective roles of the public and private sectors, and the impact of PFI contracts on readiness levels and long-term operational integrity.

There are many other activities ongoing in the MoD that involve close cooperation and partnership with the private sector, and harness private sector skills and innovation, although not always private sector finance. Examples include the Smart Procurement initiative in the Defence Procurement Agency and the Prime Contracting initiative in Defence Estates. These initiatives show how the best of both public and private sectors can be brought together to deliver results that are in the best interest of both parties.

The U.K. MoD continues to face many drivers to change: the changing shape and scale of conflicts under its peace-keeping role; change driven by resource-based accounting; change driven by new technologies and e-business; and change driven by new ways of doing business, such as Smart Procurement and its integrated project teams. Involving the private sector is often a component of implementing such change. It is important that these changes are grounded in robust business processes and a long-term strategic plan specifying what the organization is trying to achieve. In the defense environment, these strategies include solving real business challenges, delivering a better working life and environment for military and civilian personnel, and achieving more within constrained resources. The latter is one of the primary drivers behind PFI.

Concerns are often expressed about potential reductions in long-term flexibility resulting from the implementation of privatization. This could be the case, unless the defense customer identifies and commits to robust, long-term requirements that are supported by its diverse stakeholders. Defense customers should also consider that the price of budget flexibility is often the deferral of necessary maintenance and ultimately, service deterioration. Funds originally budgeted for maintenance are frequently reallocated to other purposes during the annual expenditure process. A contract that prevents the deferral of necessary maintenance expenditures can therefore be beneficial to the long-term health of the armed services. In some cases, long-term spending priorities can change due to technological change or major and unforeseen changes in future demand. These types of changes can be accommodated in a flexible partnership contract.

I would like to emphasize three points raised by Mr. Apgar in his opening remarks. First, I wholly endorse the concept of implementing privatization in conjunction with a strategic approach to real estate and other defense support activities. The U.K. has learned that a piecemeal or stovepiped approach can lead to major inefficiencies, complex and costly interface problems between separate initiatives, and even dysfunctional behavior. Very little sustainable benefit can be obtained from a privatization initiative unless it is viewed as part of a longer-term strategy for organizational reform. The decisions made about the defense customer's needs and the options for meeting those needs must be grounded in a vision that defines the long-term shape and function of the armed services. Privatization contracts tend to be long-term, and therefore the organization must think through the long-term need for the contracted output.

The MoD has recognized that strategic planning is vital in the real estate context, and is putting the initiatives in place to deliver a coherent strategy. This

is important not only to the military customer, but also to the private sector partners who are investing their resources to help the MoD implement its strategy. A centrally driven, strategic approach that sets out priorities for capital investment should not have a detrimental effect on military effectiveness or the ability of base commanders to run their bases from day to day.

Second, and another important theme in Mr. Apgar's address, is the need for clear leadership and commitment from key stakeholders. If there isn't a strong push from the top, privatization initiatives will not be successful, or they will be implemented in a lackluster fashion. The most successful projects in the U.K. have strong team leaders and project managers, clear and sustainable objectives, and strong sponsorship by senior military and civilian leadership.

Third, I would like to stress the importance of creating true partnerships between the public and private sectors. Partnership involves the creation of open and honest relationships between purchasers and providers who each have clear goals, underpinned by a contract that is designed to make the partnership work better, not to be used as a weapon in an adversarial relationship. Partnerships are easy to describe, but difficult to implement. But they have wide-ranging implications for the way services are procured, competitions are run, bids are evaluated, and contractual negotiations are conducted. We must implement change in each of these areas before we reach the promised land of true partnership.

RAND REPRESENTATIVE: DR. DAVID CHU

As I looked at the papers prepared as background materials for this conference, I was struck by three broad themes that resonate through them, either directly or indirectly.

First, there is an extraordinary degree of faith in the excellence of the private sector, both in the U.K. and the U.S., in providing defense support services. More effective use of the private sector is seen as a source of better quality services, a way to save money, a way to get superior access to capital, and a solution to some of the political constraints and excessive regulation under which government agencies sometimes have to function.

Second, while the U.S. has an older history of using the private sector to provide defense services, going back to the Cold War and Vietnam, and possibly even now a wider base of private sector defense activity, in recent years the U.K. has taken bolder and more imaginative steps. Two of the most innovative examples are the PFI project to renovate the MoD headquarters building, in contrast to the U.S. approach to renovating the Pentagon, and the MoD's plans to contract for the provision of aircraft tanker services. This suggests that the United States has a great deal to learn from recent U.K. experiences.

And third, the forms of privatization vary widely, both within each country and between the two. The term privatization has somewhat different meanings on the two sides of the Atlantic, and each country is exploring its options to determine which approaches best fit its needs. However, there may still be unifying principles or preferred forms of privatization that work better then other approaches.

As we think about these issues, there are four particularly compelling questions that the conference should consider. First, when is the private sector a better provider than the public sector? Mr. Apgar argued in his remarks that there may be little, if anything, that is inherently governmental. If there is a good private market, we should use it. However, not everyone who considers public administration issues would agree with that contention. As one examines the literature on this subject, there is a dearth of long-term quantitative evaluations of the effectiveness of outsourcing and privatization. Such studies would be very useful in determining whether there are any general principles indicating when the private sector is likely to do a better job than the public sector. Furthermore, most of the examples involve peacetime operations. Although Brown & Root has some experience in providing services in deployed operations, the military may face more difficult conflicts in the future.

The second issue that I find intriguing is, why is the private sector better? Are there ideas that the public sector could emulate in activities that we choose to provide in-house for political or operational reasons?

Third, how can the military get the best outcomes, regardless of which sector is selected to provide services? When the government turns to the private sector, how can we get the best suppliers to put their ideas forward and bid on projects? How do we devise the appropriate sharing of responsibility and risk? How can we determine the right contract incentives ex ante, instead of ex post, after we discover that they have dysfunctional effects? How do we become smart customers? The identity of the government "customer" may be ambiguous. The government has many parts, and in some areas, such as housing, one may ask whether the government should be involved in the market at all. Perhaps the government should simply give the money to the ultimate customers, i.e., the service members who are going to live in the houses, and let them deal with the private market directly.

The final issue is, how do we secure political support for these initiatives? The public issue that ultimately concerns the U.S. Congress and other legislative bodies is the distributional effect of choosing the private sector versus the public sector.

3. Housing Working Group

The Housing Working Group brought together senior U.S. and U.K. civilian and military defense officials with private developers, financiers, and analysts. Each group member had past experience or current involvement with government privatization efforts, and most had dealt directly with privatization efforts involving military housing. Both countries have experimented with efforts to privatize military housing over several decades, with varying degrees of success. The working group discussed housing privatization in light of past experiences and the two major initiatives now ongoing –- the U.K. MoD's Private Finance Initiative (PFI) and the U.S. Army's Residential Communities Initiatives (RCI). The group also considered other novel approaches to housing privatization.

For many of its U.S. participants, the working group provided the first opportunity for developers and Army leaders to meet face-to-face to discuss strategies to promote housing privatization. The four-way dialogue – between U.S. and U.K. military representatives and U.S. and U.K. developers – provided fertile ground for discussion, and promoted new understandings on all sides.

Discussion among the Housing Privatization Working Group focused on several topics:

- Determining the appropriateness of private sector involvement in housing
- Comparing U.S. and U.K. reasons and strategies for recapitalizing military housing stock
- Analyzing the pros and cons of transferring ownership and management of housing facilities
- Forging successful partnerships with industry
- Exploring the roles of tenants and local communities
- Identifying and overcoming barriers to privatization
- Sharing new ideas

The Working Group's discussions and debates ultimately coalesced around a major conclusion: successfully privatizing military housing requires changing cultural attitudes. Improving education for all players –- public and private sector –- is essential to effect that change.

DETERMINING THE APPROPRIATENESS OF PRIVATE SECTOR INVOLVEMENT IN HOUSING

Working group participants agreed that housing privatization is clearly an appropriate area for private sector involvement. The private sector has sophisticated and efficient systems for financing, designing, building, and managing residential housing units. Unlike other functions under discussion at the Ditchley Park conference, housing is not complicated by stovepipes, nor is it an essential element of the military's core function –- war fighting.



Increasingly, U.K. military housing is being merged into the private sector, and base housing is being phased out of existence. In the U.S., housing privatization refers primarily to efforts to repair and revitalize housing on military installations. The unique location of U.S. Army housing, combined with the distinctive military culture, does present challenges to developers who are accustomed to building private sector residential housing. However, irrespective of culture and location, the technical details of building and maintaining houses are the same in the public and private sectors.

COMPARING REASONS AND STRATEGIES FOR RECAPITALIZING HOUSING STOCK

The U.S. and the U.K. share some basic military housing problems. Approximately 78 percent of the military housing stock in both countries needs to be repaired or replaced, and the military budgets for operations and management are not adequate to remedy the situation. In both countries, deteriorating housing facilities are directly linked to increased attrition of service personnel.

During the 1990s, the defense leadership in both countries crafted initiatives designed to leverage private sector capital to facilitate housing improvements. In the U.K., the PFI is an initiative –- driven directly by the Prime Minister's office -– that attempts to move the MoD out of the housing business altogether. A 1994 PFI deal transferred ownership of approximately 55,000 married quarters to a private developer. Subsequent large PFI projects have leveraged private capital to build new married quarters and to renovate barracks accommodations. Thus, PFI projects help the MoD upgrade its housing stock without requiring up-front

public sector investment. They give the military immediate access to private sector expertise while transferring much of the risk to the private sector.

Two initiatives designed to harness private sector capital and expertise are also underway in the U.S. Army. Under the Community Ventures Initiative, 1,823 sets of on-base quarters at Fort Carson, Colorado, are undergoing extensive renovation, and an additional 840 new sets of quarters are slated for construction during the next four years. The related Residential Communities Initiative (RCI) aims to renovate or build approximately 12,000 sets of quarters at three additional installations in the U.S. The total revenue stream from Basic Allowance for Housing (BAH) for these four projects is approximately $100 million per year.

ANALYZING THE PROS AND CONS OF TRANSFERRING OWNERSHIP AND MANAGEMENT OF HOUSING FACILITIES

When the working group began to discuss the details of privatizing military housing, it quickly became apparent that U.S. and U.K. military leadership differ sharply on the very definition of "privatization." The U.K. leaders begin with the premise that since the private sector can own and operate residential property more efficiently, the government should privatize housing in the most literal sense – by completely removing itself from the housing business. This means moving military housing off installations and integrating service personnel into the greater civilian community. In keeping with this philosophy, recent PFI projects aspire to transfer as much asset ownership as possible to the private sector. In doing so, they also transfer much of the associated risk to their private sector partners.

The U.S. Army, on the other hand, views owning on-base housing units as a fundamental military requirement, and its leaders have no intention of removing housing from installations. When U.S. Army leaders talk about privatization, therefore, they are referring to broad-based service contracts with private sector partners for constructing and maintaining buildings, rather than arrangements for transferring property or land. Accordingly, the Army's RCI aspires to leverage private capital in order to vastly improve military housing, but to do so without relinquishing ownership of the assets. Rather than moving military personnel into the community, RCI is designed to help military communities function more like civilian ones.

This stark difference in attitude informed much of the group's discussion about the merits of transferring ownership and management of residential housing facilities.

Because U.S. Army homes are often located in the center of installations, the Army is unwilling to consider U.K.-style "true" privatization. Rather, the Army retains its property but transfers the associated income stream to its private partners via a long-term (maximum 50-year) lease. One U.S. group member suggested that property in the center of military installations is particularly unsuitable for private mortgages, noting, "most banks don't like the idea of showing up to reclaim or foreclose on a mortgage when a guy at the front gate [has] a tank."



One developer in the group, pointing to the downside of this type of arrangement, noted that a residential developer normally anticipates three sources of return on his investment: cash flow, tax savings, and appreciation. In a lease-holding arrangement, appreciation is eliminated as part of this equation. Also, although no assets are transferred, contractors who are operating government activities are sometimes subject to state and local taxes. Still, countered an Army representative, these partnerships potentially provide substantial tax advantages to contractors, and they guarantee a steady income stream in the form of rent. That income stream is an especially valuable asset to developers because it is guaranteed by the federal government.

In the past, long leaseholds have posed difficult problems for the U.S. Army. For instance, in the final five years of one 50-year lease, the Army watched helplessly as a contractor allowed property to deteriorate drastically. If a developer has no future stake in property, how can the Army prevent the developer's interests from diverging with its own toward the end of a lease? Industry and U.K. group members offered concrete advice about building contracts with incentives that reach all the way through the lease. For instance, the developer could be required to establish a capital reserve fund for improvements, a cache of money that stays with the property when the lease expires. If the fund is not depleted at the end of the lease, the developer loses his investment in the fund.

FORGING SUCCESSFUL PARTNERSHIPS WITH INDUSTRY

Members of the Housing Working Group were especially interested in sharing ideas about forming workable partnerships. MoD and U.S. Army

representatives found the forum particularly useful for comparing partnership models for their major privatization efforts. Since successful partnerships require well-structured contracts, group members devoted considerable time and attention to sharing ideas about structuring contracts.

The U.K.'s PFI and the U.S. Army's RCI are designed to create true partnerships with the private sector. In both cases, ideal partnerships will last for many decades, and will involve a shared vision by the public and private sector partners. The U.K. and the U.S. initiatives achieve this end through somewhat different means. In both cases, potential private sector partners are engaged very early in the process.

In the U.K., the housing PFI process creates a special purpose vehicle that consists of a prime contractor and all the other major players required for the project, including the construction company, the bank, the facilities management company, etc. As the competition goes forward, these players contribute to the design of the project. As the nature of the project crystallizes, quite often the players change. By the time the contract is ready to be bid, the public and private sector partners have already established a working relationship and, ideally, all partners are already invested in the project's outcome.

In the U.S., the RCI model employs a "Request For Qualifications" (RFQ) mechanism to bring potential partners into the process very early. In an RFQ, the Army asks potential partners to describe their qualifications in seven broad areas. By basing its selection on these general criteria, the Army brings a development partner into the process long before the details of the contract have been refined, and the partner participates in developing the plan's broad outlines and details. As in the U.K., by the time the contract takes shape, the partnership is firmly established.

The participants agreed that successful partnerships require a combination of mutual trust and excellent contracts. In discussing the issue, the group discovered three important issues that contracts must take into consideration: sharing risks and profits, encouraging innovation, and overcoming personnel changes.

In both countries, housing privatization plans include a detailed analysis of who assumes which risk. Generally, the contractor assumes most of the risks, but some are explicitly assumed by the government, and others are shared. Sharing the benefits, however, appears to be more difficult. In the U.S., in particular, developers are highly motivated to take risks because the benefits reaped by refinancing a project's income stream can be exceptionally valuable. In some cases, developers reap more return in a single event of financing and refinancing than they have the potential to earn in rent and management fees over the full term of the contract. However, the U.S. Army has not yet developed contracts that allow it to fully share this benefit.

Encouraging innovation is a second important element for contracts. In both countries, procedures to involve developers early in a project's life are designed



to tap into private sector expertise and promote new ways of thinking. However, both countries' efforts have been stymied by regulations that detail construction specifications. In the U.K., these regulations have been, as one group member put it, "thrown in the bin" because they were antiquated and unnecessary. When MoD talked to soldiers about the types of houses they wanted to live in, they learned that they wanted exactly the same things as British civilians. In housing, as in other areas of military privatization, the MoD has demonstrated the value of specifying outputs in contracts, rather than inputs. In the U.S., said frustrated Army group members, specifications continue to hamper innovation in military housing.

Real estate is a fast-paced business, the goal of which is to quickly create value and realize profits –- even the largest and most reliable developers "flip," or sell, their assets. Consequently, the prospect of establishing long-term relationships with the real estate industry is very challenging. Given the situation, advised private sector group members, the military must develop contractual agreements that survive partnership changes. Specifically, contracts should specify measurable performance standards, and tie the revenue stream to those measurements. If the contractor is not sustaining the standards over time, the contract should allow for his removal. From the perspective of the developers in the group, the best way to guarantee high performance over a long contract is to put the Basic Allowance for Housing (BAH) into tenants' hands, and let them "vote with their feet."

Officials involved in housing privatization initiatives in both countries report that their current public-private partnerships appear to be successful, but they acknowledge that the contracts are too young to know for sure.

EXPLORING THE ROLES OF TENANTS AND LOCAL COMMUNITIES

Throughout their discussions, members of the Housing Working Group tried to keep their gaze on the purpose of their efforts: to provide a better quality of life for military families. Unless potential tenants can see how these projects will improve their lives, they are unlikely to support them. Thus, public-private partnerships in both countries stress the importance of giving these stakeholders a voice early in the process. In the U.K., tenants are included in planning even before a private sector partner is selected. At Fort Carson, site of the U.S. Army's Community Venture Initiative, tenants were invited to meet with developers early in the process, and housing requirements were built around their input.

Involving members of the surrounding community is more difficult, group members agreed, but it is essential to securing political support for these projects, particularly in the U.S. RCI is based on a vision of delivering community services –- including retail services –- to families living on military installations. As such, it ideally includes a robust commercial component, which potentially provides an additional revenue source for the Army's private sector partner. In the Fort Carson project, this commercial component was deleted in the plan authorized by Congress, partly because it was perceived as potentially damaging to the economy of the local community. The architects of the Fort Carson plan, who believed their project actually presented new opportunities for local businesses, are attempting to identify a role for civic leaders earlier in the process for future projects. Their U.K. colleagues supported this effort, noting that if the Army could first coordinate plans with adjacent communities, it could present a fully supported plan to Congress, potentially circumventing opposition.

IDENTIFYING AND OVERCOMING BARRIERS TO PRIVATIZATION

Working group discussions focused on two types of persistent barriers to privatization efforts. The first type encompasses political opposition and institutional resistance to change. The second type of barrier involves the cultural divide and knowledge gap between the public and private sectors. Group members explored both types of barriers, and proposed strategies for overcoming them and increasing momentum for change.

Congressional opposition to aspects of RCI has been frustrating for its proponents. Still, when the working group systematically examined sources of support and opposition to privatization plans, they discovered broad-based support at many political levels. Senior DoD officials –- including the U.S. Secretary of Defense –- support privatization efforts, as do many senior Army leaders. Military tenants support the goals of privatization, without much regard to the means. Installation commanders, who will ultimately be held accountable for the success or failure of housing on their bases, are reluctant to rush into privatization efforts. And Congress, while demonstrating some support, has not wholeheartedly endorsed the RCI plan.

U.K. group members noted that in their case, the privatization effort was driven from the very top level of government. Change has been incremental but steady, and the best tool for enlisting support has been the ability to demonstrate

good results. U.S. Army leaders are confident that the success of the Fort Carson project will also translate into increased support in the long run. The group agreed that in the short term, combating Congressional opposition will require consolidated lobbying efforts by industry and the Army. In particular, the Army needs to demonstrate to Congress that the people who stand to benefit most from housing privatization are the same people that the nation counts on during wartime and crisis. To this end, senior war fighters need to be enlisted in the battle for political support.

The second type of barrier –- the cultural gap –- was particularly evident to working group members during their discussions. Industry and military group members agreed that, in general, the U.S. military does not understand the language and customs of the world of finance. Each side recognizes that the other misunderstands its culture. Bridging this divide requires education on both sides, but particularly on the military side. U.S. military group members acknowledge that until the Pentagon fully understands issues like the cost of money, debt and equity ratios, and the checks and balances that exist in the commercial marketplace, the public sector is likely to miss some benefits of private sector partnerships. Current efforts are aimed at formally educating the next generation of military leaders in the basics of private sector finance. Likewise, industry group members noted that their limited knowledge of military culture inhibits the process. MoD officials noted that in the U.K., private sector partners routinely employ former military personnel to help bridge this cultural divide.

SHARING NEW IDEAS

Throughout the course of its discussions, the housing privatization working group generated a series of novel suggestions about how private sector involvement can improve the quality of life for military families. In particular, group members brainstormed about methods for giving military personnel equity in their homes. Two models for doing this were proposed, one by the U.S. private sector contingent, and one by U.K. military group members.

The idea floated by U.S. developers is to devise a military home ownership plan based on the resort time-sharing model. Under this scheme, military personnel would not own their homes, but would own contracts that represent the income stream generated by those homes. As service members transfer from base to base, their time-share ownership would transfer with them. Over time they would acquire real equity in their homes. Critics in the group argued that the benefits of this scheme may be difficult to convey to the people it is intended to benefit. After all, they noted, the American Dream is about owning a home, not a piece of paper.

The U.K. group members noted that owning a home is also the British Dream. In fact, MoD research indicates that 86 percent of U.K. service families aspire to own homes. As a consequence, the U.K. military has experienced a trend in which personnel take "premature voluntary retirement," i.e., they use their military pensions as down payments for homes, and find employment in the private sector. To counter this trend, the U.K. services have crafted plans that



allow service personnel to borrow against their future pay to finance home ownership. The zero-interest loan program has proven so popular for service personnel in their 30s that the Royal Navy has lowered the eligibility age to 23. The Air Force and Army are considering following suit. Once they own their homes, service personnel who are transferred tend to rent them to other military families, which ultimately benefits MoD.

HOUSING GROUP REPORT

The Housing Working Group's report is shown in Appendix D. In the closing plenary session, the group's chairman and rapporteur emphasized the two main questions discussed by the group. First, what is privatization? Group members from the private sector thought the military should simply give housing allowances to service members and allow them to choose housing in the private sector. However, military representatives wanted to maintain communities that nurture military values and provide amenities equivalent to the private sector. Second, how can progress toward privatization be made? The Army's Residential Communities Initiative is a good start, but some stakeholders do not fully support the program. Congress is uncertain, military leaders are taking a "wait and see" attitude, and industry is largely silent. To make progress, industry must understand the needs of military customers, and military leaders must become better customers by defining and communicating their needs, improving contracting methods, and establishing partnerships with the private sector.

The group chairman stressed that the ultimate question for military housing is whether the money currently being spent on it is helping retain and sustain

service families. Could this money be better spent on something else, or should it be given to the families themselves?

4. Base Operations Working Group

The Base Operations Working Group used the U.K. experience as a springboard to discuss strategies and opportunities for private sector involvement in U.S. Army base operations. Over the course of four sessions the group talked through a full spectrum of issues related to private sector involvement. Ultimately, the group concluded that the U.S. Army must apply creative strategies before the infrastructure on its bases –- which is badly in need of improvement -– deteriorates further. Group discussion centered on six themes:

- Acknowledging the scope of infrastructure decay
- Determining which functions and services are appropriate for private sector involvement
- Clarifying incentives for base commanders to contract out for services
- Creating appropriate and flexible partnerships with the private sector
- Implementing cost accounting measures
- Managing political challenges

In the end, the Base Operations Working Group considered alternatives for the future and devised a deliberately provocative group report designed to challenge the Army to change.

ACKNOWLEDGING THE SCOPE OF INFRASTRUCTURE DECAY

Military budgets have been shrinking precipitously for a decade, and because the U.S. Army's primary mission is to be ready for war and not to manage real estate, base infrastructure is suffering. Despite diminishing resources, the Army culture will remain can-do; base commanders will allocate shortages so the Army can continue to put an adequate share of its resources into missions.

While Base Operations Working Group members disagreed about whether the current situation constitutes a crisis, they agreed that if it is not, it soon will be. The Army is managing to maintain mission readiness despite downsizing, but it is mortgaging its future by letting the infrastructure deteriorate. Base commanders are forced to spread thin and diminishing resources over the infrastructure from year to year, in effect playing around the edges of the problem rather than instituting policies to fundamentally change it.

The Army must acknowledge that meeting its core mission depends on maintaining intact housing and infrastructure. It cannot afford to ignore this fact when planning for the future. Poor living conditions on installations are the second leading cause of attrition for Army personnel. The leadership needs to consider the cost of retraining new military personnel as part of the total cost of blocked pipes and crumbling buildings. One group member noted that the maintenance and repair backlog at just 17 of the U.S. Army's installations will total $8 billion by 2005.

The political situation in the U.S. inhibits radical rationalization measures, as well as further Base Realignment and Closure (BRAC) rounds, at least in the short term. With no reasonable likelihood of major additional funding for Army base operations in the foreseeable future, the Army will continue to face suboptimal operating conditions and resources.

Despite the gravity of the situation, U.S. base commanders remain reluctant to enter into contracts with the private sector. This is because commanders are frequently forced to divert funds to prepare for new missions, and they believe fixed contracts take away their flexibility to do so.

U.K. and private sector representatives in the Base Operations Working Group urged the U.S. Army to recognize the issue as a fundamental business problem, and to think strategically about how private sector involvement might ameliorate the crisis. The private sector will not solve all the problems, they noted, but they can help manage some of the horrors that are waiting to happen.

DETERMINING WHICH FUNCTIONS AND SERVICES ARE APPROPRIATE FOR PRIVATE SECTOR INVOLVEMENT

Group members agreed that private sector involvement can be a good way to improve value for money, as long as it does not interfere with military mission requirements. However, deciding which functions and services are candidates for private sector involvement is a complicated issue.

There was absolute agreement on one thing: under no circumstances should the military outsource or privatize its core functions. Everything else is a candidate for contracting out. But what constitutes the core function of the military? The gray area that falls between "military core competencies" and "functions better handled by the private sector" is vast. Group discussion centered on how to define military core competencies.

Recent involvement with the private sector has been more varied in the U.K. military than in the U.S., and British group members urged the Americans to "be brutal" when paring down the list of core military competencies. One British group member –- who admitted playing devil's advocate –- suggested that there are no military core competencies, and that all functions (including combat) are candidates for private sector involvement. This radical suggestion posed a challenge to group members to look at all base operations and identify areas of clear core competencies, gray areas, and areas in which contractors are likely to have better expertise and values.

Group members agreed that war fighting is a core military competency. They also agreed that the preservation of the unique military culture, or ethos, cannot be accomplished by an outside contractor. However, agreement dissolved as soon as the group considered functions outside this essential core.

For one thing, core competencies in deployment differ from those on base. The Army might contract out for cooks on base, for example, but when units deploy they need cooks who are soldiers. The same is true for mechanics, truck drivers, police, and other professional functions that appear to be targets for private sector involvement. U.K. group members noted that this dilemma is surmountable. The British military routinely contracts out part of a profession.



For example, two-thirds of military cooks are civilians and the other third are deployable service personnel.

Conversely, some functions that are crucial to the core mission of war fighting are dependent on private sector involvement, both in the U.K. and the U.S. For example, both countries contract for the design and manufacture of strategic nuclear weapons. Similarly, some airplane and helicopter training programs are handled stem-to-stern by outside contractors. The U.K. military is currently pushing the concept even further by investigating privatizing tanker aircraft service.

Because the military is filled with talented people who are competent in a wide range of areas –- from munitions manufacture to child care –- defining primary core competencies is essential. Given the scope of gray areas and the natural tendency for individuals to protect their own functional areas of expertise, U.K. group members suggested that these decisions be made at the strategic level of command.

CLARIFYING INCENTIVES FOR BASE COMMANDERS TO CONTRACT OUT FOR SERVICES

U.S. Army group members asked their industry and U.K. military colleagues to help clarify incentives for contracting with the private sector. U.S. Army commanders, they explained, are loath to tie up their limited funds in contracts and thereby relinquish the small amount of budget flexibility they have. In addition, the Army's long-term budgeting process reduces base commanders' future budgets in anticipation of savings generated by public-private competitions, eliminating the opportunity for commanders to feed the savings

back into their own operations. Given these circumstances, what incentives exist for base commanders to enter into contracts?

The emphatic answer to this question was, bluntly, "your incentive is, 'change or die.'" Already, base commanders are allocating shortages and trying to accomplish more than they can afford. Don't think about saving money, U.K. group members urged, but about accomplishing more for the same money. Making base operations "less unaffordable" creates some relief for base commanders, and that, they note, should provide powerful incentive.

Public-private enterprises can also potentially generate profits. For example, a privately owned carwash on base at Fort Carson, Colorado, required no military investment. The contractor owns the assets and assumes the risk, and the military receives 10% of the profits generated. This arrangement provides an obvious incentive for base commanders.

CREATING APPROPRIATE AND FLEXIBLE PARTNERSHIPS WITH THE PRIVATE SECTOR

Much of the group's discussion focused on the nuts and bolts of contracting with private sector providers for support services. Representatives from both countries shared stories about their experiences. Since the U.K. MoD has had more varied experience with private sector contracts, the British representatives offered valuable advice to their U.S. colleagues about setting standards, designing flexible contracts, and establishing solid partnerships.

Setting Standards

One critical barrier to private sector involvement in U.S. military functions is a lack of codified standards for base operations. While the U.S. Army has absolutely clear measurements for war fighting skills, it lacks similar standards for running installations. As a result, tight budgets cause standards to default to whatever available resources allow, and installation infrastructure continues to deteriorate.

The group discussed whether standards should be defined service-wide or locally. Group members from the U.K. military advised that because what is appropriate locally is not always apparent at a high level of command, standards should not be set at the top unless local commanders retain some measure of control. This is the key to making the local installation commander an integral member of the intelligent customer team that must be in place if contracts are to be successful.

Further, successful contracts require measurable performance standards. The military partner in such contracts must define performance criteria and make the provider accountable for delivering them. Because the process of measuring performance influences outcomes and behaviors, the intelligent military customer needs to be sure that the right performance indicators are being measured. This difficult task is essential to successful contracts.



Designing Flexible Contracts

U.S. Army installation commanders express deep reservations about committing significant portions of their budgets to contracts because doing so limits their flexibility to apply funds to emergent budget requirements. For instance, a garrison commander may be told to provide troops for hurricane relief, an action that might require ramping up from 5-day to 7-day weeks. The commander would not receive additional funds for the operation. A contractor could certainly accommodate this change, but not without additional payment, which the commander would be unable to supply.

To counter this anxiety, other group members offered valuable advice about building contracts for maximum flexibility. They also warned that unless the Army can commit money to contracts aimed at infrastructure improvements, the situation on its U.S. installations will go from serious to critical. They urged the Army to make a strategic decision to pursue every available efficiency option, recognizing that this will probably compromise flexibility.

After much trial-and-error, the U.K. MoD has learned some basic lessons about creating successful contracts. According to U.K. group members, the single most important aspect of building flexibility and value for money into contracts is to specify outputs rather than inputs. This requires a dramatic shift in thinking and demands a planning process in which the customer makes difficult choices up-front. Defining outputs allows the customer to tap into contractors' expertise and incorporate best practice methods into military functions. For instance, a contract for grounds maintenance that requires the contractor to cut the grass every two weeks defines inputs and limits the scope of innovation. If the contract proposal specifies the outputs instead –- in this case, nice-looking grass –- the contractor may have a method that accomplishes the

task cheaper and better. The same principle works in larger, more complex projects, including one now underway for wastewater treatment for all MoD facilities in the U.K. Such contracts require the military to establish reliable partnerships with contractors and to remain involved, intelligent customers throughout the length of the contract.

Military customers can retain flexibility by designing large, multifunction contracts. Single-function contracts perpetuate stovepipes, while multifunction contracts eliminate them. For instance, by contracting with one prime contractor for all base maintenance, an installation commander unloads the burden of overseeing every detail and paying for each individual service. With the right contract, the base commander can step out of the way and give the contractor latitude to manage within the umbrella of his multifunction contract to help the commander achieve his or her aims.

Such contracts should contain provisions for annual changes to deal with problems and accommodate new aims. They should also contain clear provisions for termination if the contractor fails to live up to specified performance standards or the customer requires it for some other reason. The U.K. military aims to make contracts as output-oriented and multifunction as possible. In fact, the U.K. goal is to contract with a single supplier organization to manage a network of regional prime contractors and deliver a fully serviced estate to MoD users.

For such contracts to work, the military must be an intelligent customer and establish close, long-term relationships with contractors. In many cases, U.K. military customers involve contractors very early in the planning process, sometimes soliciting "outline proposals" even before outcomes are specified. Experience has taught MoD not to try to outthink the private sector, but to involve it in its thinking process. Sometimes this requires recruiting private sector representatives onto advisory boards, and sometimes it requires collaborating with a narrow field of contractor candidates to develop output specifications. Bringing contractors in as early as possible fosters partnerships, which is the ultimate goal of private sector contracts.

Establishing Solid Partnerships

Creative, flexible contracts will only work if executed within partnerships in which the customer and the contractor share objectives, risks, and rewards. U.K. military customers routinely strive to eliminate arm's-length relationships with a multitude of contractors and replace them with close relationships with a few prime contractors. Successful partnerships require the customer and contractor to talk through issues of cost and risk, and to make intelligent choices together. The best contractor, therefore, is often not the one who submits the lowest bid, but the one who demonstrates that he has considered the risks and is willing to establish an open partnership.

In addition to sharing management responsibilities and risks, U.K. military customers demand open-book accounting from their contractors. This eliminates many potential contractors, but U.K. group members insist that any contractor who is unwilling to share accounting information is unlikely to be a good

partner. A foundation of trust, they emphasize, underpins all successful partnerships.

Another important factor in choosing a partner is to investigate potential contractors' experience, expertise, and investment in the field. Partnering with a contractor who is investing money and fostering innovation puts the military customer on the cutting edge and frequently provides the best value for money.

Close partnerships and careful contracts with specified, measurable standards go a long way toward eliminating concerns about the military's ability to control functions for which they contract with the private sector. Still, the U.S. Army group members expressed doubts that contractors can deliver services during wartime. Their U.K. colleagues were less concerned about this issue, but noted that strategic assets –- those needed for war fighting –- may be too closely related to the military's core function to be considered for privatization.

IMPLEMENTING COST ACCOUNTING MEASURES

One thorny area that needs to be addressed in discussions of privatizing military functions is how to compare the cost of in-house and outsourced services. Large, bureaucratic entities like the military traditionally lack robust cost accounting systems. Indeed, such measures were unnecessary in the era of flush military budgets. Today, however, diminished budgets and private sector competition provide strong incentives for the military to fully understand costs.

One Base Operations Working Group member, a former U.S. Army base commander, confessed that although he rigorously maintained a budget and kept sight of cash flows to and from the base, he never seemed to be able to get his arms around the real costs of base operations. His U.K. colleagues in the group suggested that the commander's perception persisted because he only had a view of cash flow. Full resource accounting, they pointed out, also considers capital and assets. Without this, a base commander will never be able to truly grasp the real cost of service provision.

To address this problem, the U.K. MoD has made a substantial monetary investment over the past five years to implement a new system of resource accounting and budgeting. In doing so, military leaders discovered exactly where money is going and gained valuable insight into the cost-effectiveness of the services that they provide and the true cost of the resources they use. When information about the real costs of services was made public, demand evaporated for the less cost-effective ones. As a result, services that might have been considered candidates for private sector involvement were simply eliminated. The British group members advised their U.S. counterparts that investment in resource accounting is not only worthwhile, but is crucial to effectively design and evaluate private sector contracts.

One effect of the new cost accounting measures in the U.K. was a shift from a "landlord" to a "tenant" mentality. In other words, once the military executive understood the real cost of "owning" support services, it was better able to appreciate the advantages of "renting" them.



MANAGING POLITICAL CHALLENGES

While comparing U.K. and U.S. military experience with private sector involvement is a valuable exercise, importing U.K. successes to the U.S. is difficult because the two countries' governments operate differently. Privatization efforts in the U.K. have been driven from the top down by a succession of Prime Ministers. Before, during, and after contracts are awarded, parallel bottom-up processes occur, with local political and union leaders working with Parliament to enact laws that protect people who could potentially be harmed by privatization actions. It is, reported U.K. group members, a very successful political process.

Congress plays a very different role than Parliament, and U.S. Army leaders are doubtful about the likelihood of enlisting broad-based Congressional support for privatization efforts. Congress has more leeway than Parliament to limit the scope of Army plans, as well as a much greater capacity to affect base operations. For instance, Congress can mandate the centralization of services, or pass laws requiring construction on individual bases.

More than anything else, group members who represent the U.S. Army reported being stung by Congressional opposition to the Army's BRAC plans. Designed to consolidate bases and alleviate the Army's excess real estate overhead, BRAC was stopped in its tracks by members of Congress representing regions where bases were slated for closure. U.S. Army group members said they are resigned to the current situation and expect to be supporting excess overhead for a long time. Their U.K. counterparts expressed surprise that the situation seems so intractable. Group members from both sides of the Atlantic agreed that the U.S. legislative system poses unique challenges.

LOOKING AHEAD

Responding to the frustration of their U.S. counterparts, the U.K. contractors and defense officials suggested that the Americans embark on a campaign to educate legislators about the scope of the problem facing the Army. If a crisis is looming, they asked, shouldn't the government and the Army find some shared goals? Further, they suggested that U.S. Army officials put the bitterness of BRAC behind them and consider taking a fresh approach to the excess capacity problem. For instance, the Army could generate revenues and reduce the real estate burden by retaining ownership of the redundant bases and working with private partners to exploit their commercial potential. One U.S. group member noted that long before BRAC, the U.S. government privatized parts of some ammunition and manufacturing facilities –- retaining the right to recover them –- and rented other sections of those facilities to private users in exchange for infrastructure upkeep or environmental remediation. In all cases, these projects generated revenue.

Another suggestion from the U.K. was to adopt the British "Trading into Wider Markets" strategy when possible. The U.S. Army provides excellent day care services, for instance, that could easily compete for non-military users. In Britain, such successful in-house services are sometimes converted to independent agencies. The military gets the same service by contracting with the enterprise, but overhead costs are shared with outside customers.

Before closing their discussions, the U.S. Army group members asked for general advice about how their U.K. colleagues would proceed if their positions were reversed. They received the following counsel:

- Think about this as a long-term process. Your confidence will increase, you'll gain clearer insight into how to do things, and you'll capture best practice as you move along.
- Have a clear strategic view of what the future is going to be like. Identify your core bases and invest in those.
- Start moving toward full cost accounting. It takes time, but you have to start somewhere.
- Start pilot programs. If you can demonstrate effectiveness, you can rally political support to expand them.
- Think of yourself as a business. Start with zero-based budgeting, look at every function, and decide if it's necessary. If you tackle this problem before you contract out, you eliminate some of the cost basis from the very start.
- Look at this as an exciting opportunity. Engage decision-makers, form alliances with the private sector and environmental groups, and forge ahead.

BASE OPERATIONS GROUP REPORT

The Base Operations Working Group's report is shown in Appendix D. In the closing plenary session, the group rapporteur reflected the impending crisis of deteriorating infrastructure at U.S. Army bases due to underfunding, and the

need for new approaches. If the Army does not have the resources to finance improvements internally, then programs such as the U.K.'s Private Finance Initiative or Public-Private Partnerships can be used to leverage private-sector capital. As Mrs. Thatcher would have said, "There Is No Alternative."

The group chairman argued that three essential components are needed to resolve the crisis in U.S. Army base operations. First is "command by negation." If someone hasn't told you not to do it, then move ahead. Second, the Army must determine what bases and functions are absolutely essential to the Chief of Staff's vision of a 21st century Army, and which of these functions must be performed by military personnel. Third, the Army needs a full cost accounting system so that savings can be measured and fed back into commanders' budgets to enhance the support base and ultimately, the Army's warfighting capability.

5. Logistics Working Group

The Logistics Working Group compared experiences with outsourcing and privatization of logistics support functions in the U.S. and U.K., and discussed a strategic vision for integrating contractors into the military supply chain and integrating new logistics support concepts into the acquisition process to reduce the life cycle costs of weapons systems. Achieving this strategic vision will require the development of long-term partnerships with contractors that allow both sides to share in the benefits of reduced costs and improved performance, and may require new organizational structures, such as government corporations, to overcome political obstacles and objections from senior military leaders in the U.S.

The discussion centered on several related themes:

- Defining logistics and privatization
- Identifying candidates for privatization
- Developing a strategic vision for privatization
- Creating internal incentives for privatization
- Organizing new military-industry structures
- Attracting and selecting the best contractors
- Managing and monitoring contracts

The Logistics Working Group report reflected the consensus that the goal of the logistics system is to provide seamless, reliable support for combat commanders. Integrating contractors into this system requires a strategic vision, top-level political and military commitment, and a new approach to contracting.

DEFINING LOGISTICS AND PRIVATIZATION

The Logistics Working Group began its discussion by comparing the U.S. and U.K. definitions of logistics. Both definitions include maintaining equipment, managing the supply chain, and providing field services (such as showers and latrines) and some construction engineering. The U.K. definition also includes the real estate and facilities used to provide these services. The group agreed that a broader definition was more appropriate, since privatization could encompass any of the resources used to provide logistics services.

The group also noted the links between logistics and acquisition, because the design of new equipment and the reliability of components affect supply and maintenance procedures and life-cycle support costs. When designing new equipment, the military has greater flexibility to incorporate innovative forms of private sector support than it does for existing, "legacy" systems. However, legacy systems can also provide opportunities for privatization.

In the U.K., the term "privatization" normally refers to selling government assets and contracting with the new owner to provide services. However, the group agreed to accept a broad definition of privatization, including outsourcing (where the government retains ownership of assets), private finance initiatives



(where the contractor invests in assets used to provide a service), and other forms of public-private partnerships that engage the private sector to perform military support services.

IDENTIFYING CANDIDATES FOR PRIVATIZATION

The Logistics Working Group took two approaches to identifying candidates for privatization. First, it attempted to identify inherently military functions that could not be provided by civilians or contractors, leaving all other functions as potentially open to privatization. Second, it identified characteristics of functions that would make them good candidates for privatization.

One group member initiated the discussion of inherently military functions by noting that military manpower is a scarce resource that is becoming more expensive and more difficult to recruit for demographic and economic reasons. Therefore, the activities of military personnel should be focused on the core capabilities that are unique to the military, such as legitimate taking of life and the capacity to operate under fire.

The group then attempted to define the area of operations that should be limited to military personnel in wartime or other deployed contingencies. However, the "bullet line" proved to be a vague concept, because it changes as the military campaign evolves. As military personnel redeploy to front lines, contractor personnel could be used to backfill their positions, but it would be a challenge to ensure that such a system could provide seamless support to combat commanders.

Concepts such as Sponsored Reserves in the U.K. and contractor technical representatives in the U.S. also blur the line between military and contractor

personnel. U.K. legislation allows for Sponsored Reserves, contractor employees who are trained as military reserves and can be put on active military duty during a deployment. The U.S. services have deployed contractor technical representatives to perform complex maintenance tasks on Navy aircraft carriers and with other types of units. Thus, it became difficult to specify which functions should be excluded from contractor involvement.

The group then began to discuss the characteristics of functions currently performed in-house that would make them good candidates for privatization. These characteristics included:

- Functions where the military lags behind civilian technology, such as management information systems;
- Functions with a strong civilian market, particularly when the private sector shows better performance or more expertise than the current in-house providers;
- Functions that can be well-defined in terms of output, performance, risk, and interfaces with related functions; and
- Functions controlled by a decisionmaker who has the budget and responsibility for the function, and the authority to make a decision.

In-house functions that could benefit from the particular strengths of the private sector should also be candidates for privatization. These strengths include the abilities to absorb some types of risk, raise financial capital to make investments that reduce costs or improve performance in the future, provide expertise in specialties where it is difficult for the government to recruit personnel because of Civil Service restrictions, and create organizational incentives for employees to improve performance.

DEVELOPING A STRATEGIC VISION FOR PRIVATIZATION

The Logistics Working Group came to a consensus that a strategic vision for privatization of logistics functions must begin with an architecture for the supply chain, particularly in wartime. The output of this supply chain is available equipment and supplies that the warfighting commander can rely upon. Although the MoD or DoD bears responsibility for the supply chain architecture, it does not necessarily need to own it or even to design it. Internal and external providers must be integrated into the supply chain in order to optimize the total process rather than each of its component parts. For example, the architecture must specify how far forward contractors' supply lines will extend into a theater of operations.

Both the U.S. Army and the U.K. MoD have made progress toward a new supply chain architecture. The U.S. Army is reducing massive inventories and speeding up deliveries to customers through its Velocity Management initiative. The U.K. MoD has combined its separate service logistics commands into a single joint Defense Logistics Organisation. However, some of their contracts for spare parts and repairs do not contribute to optimizing the total process. When contractors are paid for each repair or spare part, they do not have an incentive



to improve reliability. Integrating spare parts and repair contracts into "power by the hour" contracts creates an incentive to invest in improved reliability.

Ultimately, the group agreed that MoD and DoD need to integrate reliability, maintainability, and resupply considerations into the acquisition process. For example, increasing the fuel economy of military vehicles and aircraft could greatly reduce the requirements for fuel delivery into a theater of operations. Current acquisition processes rarely consider such issues. Furthermore, the lack of communication between personnel who set "requirements" for equipment and the acquisition community frequently prevents adequate consideration of cost-vs.-performance tradeoffs. Smart Procurement in the U.K. and Acquisition Reform in the U.S. are establishing integrated project teams to help take these issues into account. Incentives to integrate logistics and acquisition might be further improved if the output of the acquisition process were thought of as "available equipment" rather than just the equipment itself.

The group also discussed how internal and external defense functions should be organized to contribute to the supply chain architecture. There is a tradeoff between focusing organizations on activities and creating interfaces that must be managed, vs. removing the interfaces and getting an unfocused organization. Organizational boundaries must be defined so that responsibilities can be delegated. Only then can good performance be rewarded and bad performance punished.

A well-designed supply chain architecture will also help eliminate duplication of activities, both in internal and external organizations. British participants stressed that maintaining output on a decreasing budget requires avoiding duplication. Although some American participants expressed concern about becoming dependent on sole-source contractors for support, British

participants pointed out that paying for duplication means giving up something else, such as force size or training exercises.

CREATING INTERNAL INCENTIVES FOR PRIVATIZATION

The Logistics Working Group discussed some of the internal obstacles to outsourcing and privatization and how they might be overcome. One of the industry representatives pointed out that in the private sector, managers are responsible for the costs of all the assets and other resources they use, whereas in the public sector, resources such as real estate, facilities, or even military personnel are regarded as "free goods" if the manager does not have to pay for them from his or her budget.

The U.K. MoD is introducing a new system of accrual accounting to help identify inefficiencies and reduce incentives to delay repairs and maintenance. However, a U.S. defense representative pointed out that the DoD has had accrual accounting for military and civilian personnel for several years, but it doesn't seem to have changed behavior.

Some military commanders object to privatization because of an unwillingness to give up control or doubts that the contractor will perform, particularly at times of crucial need. Other objections sometimes include safety, security, or environmental issues. One of the British participants stated that "Ownership is the refuge of the intellectually idle," i.e., that privatization can provide equal or greater control if commanders specify outputs and design contracts appropriately. Objections like these can be overcome by using pilot projects as learning tools, sharing best practices, and moving toward more complex and innovative privatization projects as experience increases. Another participant observed that giving commanders the ability to reinvest saved resources — rather than having savings taken out of their budgets — would provide a strong financial incentive for privatization.

Government civilian employees may object to privatization if it threatens their jobs. Providing adequate protections or incentives may help overcome these obstacles. Under European Union regulations, U.K. MoD employees have a right to transfer to a contractor who takes over their activity. Employees can also be assuaged by the guarantee of equal or better pay and benefits.

CREATING NEW MILITARY-INDUSTRY STRUCTURES

The Logistics Working Group discussed how current military-industry structures might need to change to accommodate new outputs and new forms of partnerships. The defense industry is currently geared toward procurement rather than supply chain management. However, one participant pointed out that a contractor who is given the responsibility and the risk of providing a service will put together a team with the necessary skills to do the work.

The group discussed how to strike a balance between partnership and competition. On one hand, long-term contracts are needed to provide incentives for contractors to invest, but on the other hand, competition allows the customer



to test the efficiency of the provider against the market. Noncompetitive contract renewals might be a way to reward good performance, whereas underperforming contractors might be subjected to competition for contract renewal. Benchmarking against commercial market best practices could provide a basis for noncompetitive contract renewals or extensions.

The group also discussed a number of different hybrid military-industry structures that could potentially serve as stepping stones toward full privatization. The American participants raised the possibility of setting up government corporations for politically sensitive functions such as housing or health benefits. Government corporations are exempted from some of the normal operating rules of the government, particularly in areas such as procurement, raising capital, and employee pay and benefits. However, the government still owns the underlying assets, and senior military leaders can be represented on boards of directors.

The U.K. MoD has used trading funds to put some internal organizations, such as the Defense Evaluation and Research Agency, onto a more business-like footing, and it plans to convert its Army base repair organization and aviation repair agency into trading funds. Trading fund agencies receive their income from customers rather than from a budget, so they are sensitive to customer requirements and have an incentive to work more efficiently. In some cases, they can also sell their services to outside customers or accept subcontracts from private-sector prime contractors. When the agency has demonstrated its ability to operate as a trading fund, it can become a candidate for privatization.

The DoD has a similar concept called working capital funds, but it has not led to privatization. The U.S. has found it difficult to reduce overcapacity in its depots, arsenals, and shipyards because of political sensitivities about

government job losses. However, working capital funding does allow Army activities to act as subcontractors to defense prime contractors or bring in outside tenants to use excess capacity.

Some participants questioned whether these intermediate solutions should be pursued. They argued that the government should be able to create contractual or regulatory mechanisms to overcome concerns about monopoly power and satisfy government objectives. They also asked what would happen if one of these hybrid organizations got into financial trouble. Although agency heads could be fired, or government corporations required to raise debt to repay their losses, the government would be ultimately responsible for their debt. Similar issues could arise if trading funds enter into joint ventures or external contracts with private sector firms.

ATTRACTING AND SELECTING THE BEST CONTRACTORS

British and American participants in the Logistics Working Group compared their methods of attracting and selecting contractors. One British participant described the U.K. source selection process as being "like a funnel." It normally begins with a request for comments on the requirement to determine whether it conforms to market capabilities. The scope or allocation of risk is often adjusted in response to these comments. The provisional requirement is advertised, and respondents are asked to fill out a prequalification questionnaire. Depending on the number of potential bidders, there might be a stage where a short list of bidders is asked to submit outline proposals. Two to five bidders are then given Invitations to Negotiate. These negotiations proceed in parallel until a preferred bidder is selected. The shape of the deal and the way the risk is identified, allocated, and sold between the parties can change during the negotiation process.

The U.S. source selection process tends to be based on a Request for Proposals (RFP), which specifies in great detail the requirement and the criteria that will be used to assess it. It is usually described in terms of inputs or tasks to be performed instead of outputs or outcomes. This source selection method tends to preclude innovative proposals by contractors, and blurs the accountability for outcomes. The use of military specifications can also increase costs and production lead times. However, there are pockets of innovation in various parts of the U.S. Army. The Army's housing privatization program is using a Request for Qualifications (RFQ) to assess contractor capabilities and select a partner to draft a community development plan in collaboration with Army personnel. Contracts to operate Army ammunition plants have been awarded following a process similar to the MoD's, with a market survey prior to advertising a requirement, prequalification, outline proposals, and negotiations with two or three short-listed bidders.

The allocation of risk between the government and the contractor is an important part of the negotiation process. An industry representative said that his company's technique would be to pass the risk back to the customer, insure it, or identify it and manage it with an active risk management program. His company always limits its exposed risks to its profit margin on a contract to

avoid the possibility of being bankrupted. U.S. Army industrial operations uses two approaches to handle the risk of varying workload. If demand is very uncertain, it can use a cost plus incentive fee contract. In other cases, it uses firm fixed price contract, and allows for different terms and conditions for different levels of workload.

The group discussed whether in-house employees should be allowed to bid for contracts. Earlier outsourcing initiatives in the U.K., such as Market Testing, allowed internal employees to bid, but did not require it. More recently, the MoD has moved away from public sector bids because the bids were not usually competitive with the private sector, they were expensive, and it was difficult to create a level playing field. U.S. legislation requires an in-house bid for most functions employing government civilians. In many cases, the in-house team wins, but the competitive pressure often fundamentally changes the way it performs the function.

Both British and American participants agreed that they faced pressure to accept the lowest bidder in contract competitions, but were trying to move toward "best value." When the lowest bidder wins, contractors tend to underbid and then ask for contract modifications to improve their profits. If contracts are going to be awarded based on best value, the criteria have to be clearly specified in order to justify choosing a higher bid. The MoD is developing a questionnaire and weighting system for "soft" criteria, such as attitudes to change, attitudes to people, risk management, and strategic objectives.

MANAGING AND MONITORING CONTRACTS

The Logistics Working Group discussed how contract design affects the contractor's incentives to improve performance and reduce costs during the contract period. The DoD tends to use cost plus incentive fee contracts for situations in which a lot of risk is involved or the requirement is not well defined, and fixed price contracts with an award fee for well defined requirements. The award fee is administered if the contractor performs well, at the discretion of the contracting officer and the functional employees who oversee the contract.

The MoD has moved away from fixed prices toward pricing mechanisms that share the gains from reduced costs or improved performance. Under these contracts, both parties have an incentive to contribute toward process improvement. As contract length has been extended to give contractors an incentive to invest in assets, it is difficult to specify fixed prices for the entire length of the contract. Furthermore, under firm fixed price contracts, the contractor may be able to keep any savings from cost reduction rather than sharing them with the government. These gain-sharing mechanisms require the contractor to share information about its costs and performance.

Contract extensions can also be used to reward good performance, but they are used less often because they are more difficult to administer unless option years are built into the original contract. However, it is difficult to determine whether the contractor is performing well relative to the market if the contract is



not recompeted. It might be possible to include benchmarking in the terms of the contract as a basis for deciding whether to recompete.

Both British and American participants agreed that there were weaknesses in their systems for monitoring contracts. The government often has poor data management systems for monitoring contractor or internal costs and performance. When the government doesn't understand its internal costs or performance, it is difficult to determine whether it is getting a good deal from a contractor. Often, contracts are not monitored after the initial award unless something is clearly going wrong, so the government does not know whether costs and performance are going up or down. Better data collection and performance metrics can be built into contracts to improve the information available to the government. Performance metrics should be clearly specified and measurable, such as reliability of assets and turnaround times for maintenance operations.

LOGISTICS GROUP REPORT

The Logistics Working Group report is shown in Appendix D. In the closing plenary session, the group's chairman and rapporteur reflected the group's consensus that the goal of the logistics system should be providing seamless support to combat commanders. Achieving this goal requires trust between government civilian leaders, military commanders, and contractors. This trust can only be achieved with new contracting methods that emphasize openness, shared objectives, and continuous improvement. Although the U.S. procurement system does not currently operate in this way, procurement regulations allow for

considerable flexibility. In any case, unless the procurement culture is changed, altering the statutes by themselves is unlikely to improve the situation.

Strategic direction and top-level commitment are needed to make progress in privatization. "The process of redefining the boundary between the public and private sector … can be a torturous and uncertain road," the group chairman stated. "We need to provide a clear map to those who journey along it."

6. Concluding Remarks

In the concluding sessions of the conference, participants raised common issues and themes across the three areas of interest: housing, base operations, and logistics. These common issues can be grouped under four broad questions:

- Why do we need privatization?
- What are appropriate activities for privatization?
- How can public-private partnerships be established?
- How can we create incentives for privatization?

WHY DO WE NEED PRIVATIZATION?

Defense budgets are unlikely to increase significantly unless the threat environment changes. Therefore, logistics, base operations, and housing infrastructure must be provided by the most cost-effective means. If these support costs cannot be reduced from their current levels, the military will either have to reduce its force structure or slow down modernization. Furthermore, some housing and other base facilities have been allowed to deteriorate as funding has migrated to more urgent priorities, which is likely to lead to higher maintenance costs and to affect recruiting and retention of military personnel in the future.

Under annual government budgets, it is difficult to make the investments required to renovate housing and other base facilities and improve the reliability of military equipment. However, such investment is needed today to lower support costs and improve living and working environments tomorrow. Privatization can help solve this problem, because a private sector provider with a well-designed, long-term contract has the financial incentive and the ability to borrow against a future income stream and invest today to reduce costs tomorrow. The private sector can also absorb some risks, contribute expertise in better business processes and practices, and provide organizational incentives to improve performance.

One participant challenged those who opposed privatization to answer a series of questions. First, "Is the present system working?" If the answer is no, then the next question is, "Is it likely to get better or worse in the future?" And if things are likely to get worse, then "Do you want to manage decline or embrace a new way of doing business?"

WHAT ARE APPROPRIATE ACTIVITIES FOR PRIVATIZATION?

Each of the three working groups attempted to define military core competencies that should be excluded from privatization, leaving all other areas open to potential privatization. However, each of the three groups had difficulty drawing a clear dividing line between activities that must be performed by

military personnel and those that could be performed by civilian or contractor personnel.

In the housing group, some participants argued that the military should get out of the housing business entirely, and simply provide housing allowances to service members and allow them to choose among private sector housing options; others argued that it was important to create a sense of military community, whether on-base housing was owned and managed by the government or the private sector. In base operations, some participants argued that functions that could be provided by civilians in peacetime might be needed as a rotation base for military personnel who would perform them in deployment; others argued that these same functions had been performed by contractors during deployments in Bosnia, Somalia, and Haiti, for example. In logistics, concepts such as Sponsored Reserves (contractor employees who would be trained as reserves and could be activated during deployments) and contractor technical representatives who perform maintenance tasks in deployed operations blurred the line between military and contractor functions.

Although it proved difficult to draw a dividing line between military, civilian, and contractor functions, each group agreed that a strategic approach was needed to integrate contractor, civilian, and military operations, particularly in deployed environments. In logistics, for example, contractor operations must be integrated into an overall supply chain architecture for a deployed theater that can deliver reliable, timely support to combat commanders.

HOW CAN PUBLIC-PRIVATE PARTNERSHIPS BE ESTABLISHED?

To make effective use of private sector providers, adversarial contracting relationships must be replaced by long-term partnerships based on common goals. Conference participants emphasized three aspects of contract design that helped foster partnerships and create common goals:

- Defining contract requirements in terms of outcomes or outputs rather than inputs, based on consultation with potential providers about what is available in the market;
- Establishing performance metrics, including measures of customer satisfaction, and linking them to contract incentives, such as higher profits or contract extensions; and
- Sharing gains associated with cost reductions and performance improvements between the government and the contractor.

Participants disagreed about whether U.S. procurement regulations must change in order to write contracts with these characteristics. Some argued that wide-ranging reforms are needed, whereas others argued that existing contracting rules provide a great deal of flexibility, but cultural change is needed to persuade contracting officers to adopt more innovative approaches. The U.K. MoD adopted the slogan "Deals Not Rules" to encourage cultural change. Contracting officers are encouraged to design a deal that makes sense first, then to see whether it can be done within existing procurement regulations, or if the rules need to be changed.

HOW CAN WE CREATE INCENTIVES FOR PRIVATIZATION?

Conference participants explored some of the reasons why the U.K. has recently made more progress than the U.S. in privatizing military support functions. Many felt that the DoD leadership had not yet secured the full support of senior military leaders, government civilian employees, and political leaders in Congress to proceed with innovative privatization deals. Suggestions for increasing support and creating internal organizational incentives in favor of privatization included the following:

- Introducing improved management information and accounting systems, such as accrual accounting in the U.K. MoD, to make managers more aware of in-house costs and provide more accurate comparisons with contract costs;
- Using capital charges and trading funds/working capital funds to create financial incentives to privatize infrastructure and reduce costs;
- Allowing commanders to keep some of the savings from privatization;
- Designing pilot projects to test new contracting methods, demonstrate successes, and learn from mistakes;
- Sharing best practices and lessons learned across installations and commands; and
- Educating commanders and contracting officers about how to design and manage innovative contracts to get their desired outcomes.

One participant summed up this theme by saying, "At the end of the day, the much greater value for money -- and it's taxpayers' money -- that can be achieved through the intelligent application of these new processes must surely start to speak for itself."

NEXT STEPS

Participants agreed that the conference had been a valuable forum for exchanging ideas, learning from each other's experience, and discussing common problems. Many felt that a useful next step would be to arrange visits to sites where innovative contracts had been implemented so that they could be observed and evaluated in action. Both U.S. and U.K. participants thought that they still had a lot to learn about how to make more effective use of private sector sources of support.

Based on their interactions with MoD and industry representatives, U.S. Army participants resolved to pursue the following action plan:

1. **Establish a permanent, ongoing forum**, such as this Conference, for continued U.S.-U.K. exchanges. The forum should meet at least annually, and organize visits to installations in the U.K. and U.S. where public - private partnerships are in force.
2. **Develop new forms of contracting for privatization** that focus on "public – private partnerships" and aim to institutionalize this concept in the Army's mainstream planning, budgeting, and operations.
3. **Engage former U.S. Secretaries of Defense** Richard Cheney, Frank Carlucci, and William Perry to support and work for the advancement of

privatization efforts in the U.S., particularly through informal dialogues with DoD and congressional leadership.

4. **Seek policy statements in support of privatization** efforts from Secretary of Defense Cohen and the White House.
5. **Develop a strategic vision** for the military's privatization efforts, with the assistance of private-sector experts.
6. **Work with the Office of Management & Budget, Members of Congress, and their staffs** to ensure a thorough understanding of the programs proposed and gain their commitments to the Residential Communities Initiative, reforms to OMB Circular A-76, which governs public-private competitions for defense support services, and other key initiatives.
7. **Gain key military commanders' support** for privatization, including their cooperation in producing a strategic vision for privatization, and their assistance in gaining support in Congress.

Appendix A: Conference Participants

U.S. PARTICIPANTS Name	Title	Location
The Honorable Mahlon Apgar IV, Conference Host	Assistant Secretary of the Army (Installations and Environment)	Washington, DC
The Honorable Richard B. Cheney, Conference Co-Chair	Chairman and Chief Executive Officer, Halliburton Company; former U.S. Secretary of Defense	Dallas, Texas
Major General Joseph W. Arbuckle	Commanding General, U.S. Army Industrial Operations Command	Rock Island, Illinois
Mr. Michael Bayer	Chairman, Army Science Board	Potomac, Maryland
Mr. Douglas P. Bennett	Managing Partner, Hudson River Partners	Washington, DC
Dr. David S.C. Chu	Director, Arroyo Center, RAND	Washington, DC
Mr. Jean S. Friedberg, Jr.	Managing Partner plc, Choptank Group	Columbia, Maryland
Brigadier General Robert H. Griffin	Commanding General, U.S. Army Engineer Division, Great Lakes and Ohio River	Cincinnati, Ohio
General Richard D. Hearney (USMC Ret)	President, Business Executives for National Security	Washington, DC
Mr. John A. Kelley	Special Assistant for Asset Management, Office of the Assistant Secretary of the Army (Installations and Environment)	Washington, DC
Mr. James T. Lipham	Program Director, Residential Communities Initiative, Office of the Assistant Secretary of the Army (Installations and Environment)	Washington, DC
Admiral T. Joseph Lopez (USN Ret)	Chief Operating Officer for North and South America, Brown and Root Corporation	Arlington, Virginia
Lieutenant General Lawson W. Magruder, III	Deputy Commanding General/Chief of Staff, United States Army Forces Command	Fort McPherson, Georgia
The Honorable Bernard D. Rostker	Under Secretary of the Army	Washington, DC
Colonel Michael C. Ryan	Army Attaché, American Embassy	London, England
Mr. Donovan D. Rypkema	Real Estate Services Group, National Trust for Historic Preservation	Washington, DC
Mr. Richard P. Shields	Managing Director, Mesirow Stein Real Estate, Inc.	Chicago, Illinois

Mr. Stan Z. Soloway	Deputy Under Secretary of Defense (Acquisition Reform)	Washington, D.C.
Major General Charles W. Thomas	Chief of Staff, United States Army Training and Doctrine Command	Fort Monroe, Virginia
Brigadier General Craig B. Whelden	Commanding General, United States Army Community and Family Support Center	Alexandria, Virginia
Mr. Randall A. Yim	Deputy Under Secretary of Defense (Installations)	Washington, DC

U.K. PARTICIPANTS **Name**	**Title**	**Location**
Sir Nigel Broomfield, Conference Host	Director, the Ditchley Foundation	Oxfordshire, England
Field Marshall The Lord Vincent, Conference Co-Chair	Chairman, Hunting Defence Limited; former Chief of Defence Staff for the U.K. Ministry of Defence	Bedford, England
Mr. Ian C.F. Andrews	Chief Executive, Defence Estate Agency	West Midlands, England
Mr. Colin Balmer	Principal Finance Officer, MoD	London, England
Mr. Alistair Bell	Principal Director Commercial, Defence Logistics Organization	Bath, England
The Hon. Elizabeth Anne Crowther-Hunt	Director, The Prince's Trust	London, England
Mr. Steve M. Cuthill	Managing Director, Serco Defence Limited	Hampshire, England
Lieutenant General Sir Scott Grant (Ret)	Quartermaster General, British Army; Chief Royal Engineer	Wiltshire, England
Mr. Brian W. Hendry	Director, Taylor Woodrow Construction Limited	Middlesex, England
Major General G. Malcolm Hutchinson (Ret)	Chairman, Atomic Weapons Establishment Management Limited	Hants, England
Mr. Martin J. Kitterick	Partner, PricewaterhouseCoopers	London, England
Mr. Christopher Littmoden	Chairman, Easier plc	Surrey, England
Mr. Peter Ryan	Director, Public-Private Partnership Unit, Ministry of Defence	London, England
Mr. John Spellar	Minister of State for the Armed Forces, Ministry of Defence	London, England

Mr. Roger J. Whysall	Chief Executive, Hunting Defence Lmited	Bedford, England
Mr. John R. Wilson	Chief Executive, Defence Housing Executive	London, England

RESEARCH STAFF **Name**	**Title**	**Location**
Dr. Jonathan Cave	Senior Economist, RAND Europe	Leiden, The Netherlands
Dr. Ellen M. Pint	Senior Economist, RAND	Santa Monica, California
Dr. James C. Wendt	Special Assistant for Privatization Research, Office of the Assistant Secretary of the Army (Installations and Environment)	Washington, DC

MILITARY STAFF **Name**	**Title**	**Location**
Lieutenant Colonel Donald Chrans	Military Assistant, Office of the Assistant Secretary of the Army (Installations and Environment)	Washington, DC
Lieutenant Colonel Timothy S. O'Rourke	Special Assistant, Office of the Assistant Secretary of the Army (Installations and Environment)	Washington, DC
Major Preston Thompson	Military Assistant (Special Events), Office of the Assistant Secretary of the Army (Installations and Environment)	Washington, DC

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Appendix B: Biographical Sketches

Mr. Ian C.F. Andrews, CBE, TD. Chief Executive, Defence Estates. Former Managing Director, Defence Evaluation and Research Agency; Civil Secretary with British Army of the Rhine and United Kingdom Support Command (Germany); Head of Resources and Programmes (Army); and Head of Defense Lands in Chessington. Awarded Commander of the Order of the British Empire.

The Honorable Mahlon Apgar, IV, AB, MBA, FInstD, FRSA. Assistant Secretary of the Army for Installations and Environment. Former Principal, Apgar and Company, Inc.; Partner, McKinsey and Company, Inc.; Special Assistant to James W. Rouse. Member, Chancellor's Court, Oxford University. Fellow, Institute of Directors and Royal Society of Arts. Former Trustee, Urban Land Institute and National Building Museum. Editor/Author, "New Perspectives on Community Development" and numerous other publications. Former Captain, US Army Reserve.

Major General Joseph W. Arbuckle, BA, MS. Commanding General, US Army Industrial Operations Command. Former Commanding General, Armament Research, Development and Engineering Center, Picatinny Arsenal; Deputy Chief of Staff for Ammunition, Army Materiel Command. CSA Strategic Fellow, Army War College. Awarded the Legion of Merit.

Mr. Colin Balmer. Principal Finance Officer, Ministry of Defence. Responsible for all financial matters within the Ministry of Defence, including the Private Finance Initiative. Previous assignments include several positions in the finance area, such as resource allocation for the Army, the Royal Air Force, and the Procurement Executive; central coordination of the Defence Budget; general financial rules; guidance in handling public funds; and the delivery of resource accounting and budgeting.

Mr. Michael J. Bayer, BS, MBA, JD. Chairman, Army Science Board. Board Member, The Association of the US Army. Former Associate Deputy Secretary, US Department of Commerce; Deputy Assistant Secretary for Congressional Affairs, US Department of Energy. Former Member, Board of Visitors, United States Military Academy.

Mr. Alistair J. Bell. Principal Director Commercial, Defence Logistics Organization. Responsible for privatization initiatives within the Ministry of Defence Logistics agency. Former Director of Commercial Policy, Defence Procurement Agency, at the time of the Strategic Defence Review and

development of the Smart Procurement Initiative, and Director of Contracts for Naval Support.

Mr. Douglas P. Bennett, BS, MBA, JD. Founder and General Partner, Hudson River Partners, developers of Hotel Thayer, West Point. Former Legislative Assistant, US Congress; Assistant to the Secretary of the Treasury; Assistant to the President. Served on federal advisory boards in the White House, Department of State, Department of Education, and private sector boards. Member of the Disabled American Veterans. Former Chairman, Board of Visitors and Trustee, United States Military Academy.

Sir Nigel Broomfield, KCMG, BA Hons (Cantab). Director, The Ditchley Foundation. Former UK Ambassador to Germany. Retired Major, 17/21 Lancers. Board Member, the Dresden Trust; Advisor, Arthur Andersen (UK); non-Executive Director, TI Group, plc; Chairman, Konigswinter Conference. Awarded Knight Commander of the Order of St. Michael and St. George.

The Honorable Richard B. Cheney, BA, MA. Chairman of the Board and Chief Executive Officer, Halliburton Company. Former US Secretary of Defense; Assistant to the President; White House Chief of Staff; Chairman, the Republican Conference; Member and Minority Whip, US House of Representatives; Senior Fellow, American Enterprise Institute. Director, Procter & Gamble, Union Pacific, EDS, and American Petroleum Institute. Awarded the Presidential Medal of Freedom.

Dr. David S.C. Chu, BA, PhD. Vice President, RAND Corporation. Responsible for RAND's Army Research Division and Director, the Arroyo Center. Former Assistant Secretary of Defense; Director for Program Analysis and Evaluation; and Assistant Director of the Congressional Budget Office for National Security and International Affairs. Fellow and Board Chairman, the National Academy of Public Administration. Awarded the DoD Distinguished Public Service Medal.

The Honorable Elizabeth A. Crowther-Hunt, MA Dip Soc Admin. Director, The Prince's Trust Volunteers. Responsible for the management and development of the organization across the UK, delivering personal training for 10,500 youth annually. Associate of Newnham College, Cambridge. Former Division Director, The Industrial Society; Chief Executive, South East Training; Co-Founder, Chief Executive of a voluntary organization in Southwark. Author, "Inner Cities – Inner Strengths."

Mr. Steve M. Cuthill. Managing Director, Serco Defence Limited, one of the largest suppliers of services to MoD, including Public Finance Initiative contracts. Former Managing Director for Serco's joint venture Aerospace Company and Marketing Director for Serco's Defence Business; and responsible for the Royal Air Force's outsourcing program.

Mr. Jean S. Friedberg, Jr., BS, MBA. Managing Partner, Choptank Group, LLP, consultants in strategic, financial and marketing management. Strategic Advisor on Community Development to the Army's Residential Communities Initiative. Former Senior Engagement Manager, McKinsey and Company, Inc.; Strategic Planner, The Rouse Company. Former Infantry Officer, US Army National Guard.

Lieutenant General Sir Scott Grant (Ret), KCB. Quartermaster General, British Army. Chief Royal Engineer. Former Commandant of the Royal College of Defence Studies; General Officer Commanding, United Kingdom Support Command (Germany); Director General of Army Training; Colonel Commandant of the Royal Engineers and the King's Division; and Colonel of The Queen's Lancashire Regiment. Awarded Knight Commander of the Order of the Bath.

Brigadier General Robert H. Griffin, BS, MS, MBA. Commanding General and Division Engineer, US Army Corps of Engineers, Great Lakes and Ohio River Division. Responsible for all military construction in five-state area; and water resource development, environmental protection and disaster assistance in 17-state area. Former Commanding General and Division Engineer, Northwestern Division, Oregon; Chief of Staff, US Army Corps of Engineers; and Engineer District in Alabama. Registered professional engineer. Awarded the Legion of Merit.

General Richard D. Hearney (USMC Ret), BA, MA. President and Chief Executive Officer, Business Executives for National Security. Former Assistant Commandant, US Marine Corps; Deputy Director for Operations, US European Command; Vice President, Military Aircraft and Missile Systems Group, The Boeing Company; Regional Vice President, Business Development — Western Europe, McDonnell Douglas.

Mr. Brian W. Hendry. Director, Taylor Woodrow Construction Limited. Responsible to the Main Board for Business Services, including Supply Chain Management, Legal Services, Project Finance, and privatised infrastructure projects. Experience in TWC's operating territories in Asia Pacific, Middle East, Africa, North America, UK.

Major General G. Malcolm Hutchinson (Ret), CB, MA, CEng, FRSA, FIEE. Chairman, Atomic Weapons Establishment Management, Ltd; Director, Serco Technology; Director, Altram Manchester, Ltd. Former Managing Director, Docklands Light Railway (privatised Railway Operation and Maintenance, contracted Private Finance Initiative for new railway extension). Former British Army Liaison Officer to US Army Materiel Command.

Mr. John A. Kelley, BS, MA. Special Assistant for Asset Management, Office of the Assistant Secretary of the Army for Installations and Environment. Senior Executive Service. American Management Association, American

Association for Budget and Program Analysis, International Personnel Management Association. Chairman, Commonwealth of Virginia Board for Waste Management Facility Operators. Former President, Peterson/Gaston Associates. Director, River Farms Conservancy, Inc.

Mr. Martin J. Kitterick, LLB Hons, CA. Partner, International Project Finance and Privatisation Group, PricewaterhouseCoopers (PwC). Member of the PwC Public Private Partnerships Board. Specialist in Public Private Partnerships (PPP) in the UK. Responsible for PwC's financial advisory services to Ministry of Defence and international PPP projects in the Defence sector. Advises on privatisation feasibility, financial structure and concession arrangements in the UK and internationally in Defence, Construction and Transport.

Mr. James T. Lipham, BS, BA. Program Director, US Army Residential Communities Initiative (RCI), Office of the Secretary of the Army for Installations and Environment. Senior Executive Service. Former Chief, Housing Privatization Team, Office of the Assistant Chief of Staff for Installation Management; Chief, Unaccompanied Personnel Housing Branch, Army Housing Division; Chairman, Tri-Service and Army Unaccompanied Personnel Housing Standards Subcommittees. Member of Executive Board and Comptroller, Professional Housing Management Association, International.

Mr. Christopher Littmoden, CBE, FCA. Chairman, Easier plc, a UK-based residential real estate web site. Former Group Financial Controller and Main Board Member of international retailer, Marks and Spencer (M&S) plc, and President and CEO for North America. Former Member, Prospect Team and Advisor, Competing for Quality Programme Team, Ministry of Defence. Special Advisor to the Ministry of Defence Efficiency Steering Group. Board Member, British-American Chamber of Commerce. Awarded Commander of the Order of the British Empire for services to Defence.

Admiral T. Joseph Lopez (USN Ret), BA, MS, Hon PhD. Chief Operating Officer for North and South America, Brown and Root Corporation. Former Commander-in-Chief, US Naval Forces Europe and Allied Forces, Southern Europe; Commander, US and Allied Bosnia Peace Forces. Member, Department of Defense Policy Board and Senior Military Advisory Board for US Commission on National Security. Awarded the Department of Defense and Navy Distinguished Service Medals.

Lieutenant General Lawson W. Magruder, III, BS, MA. Deputy Commanding General and Chief of Staff, US Army Forces Command. Former Deputy Chief of Staff for Operations, Forces Command; Commanding General, 10th Mountain Division (Light) and Fort Drum; Commanding General, Joint Readiness Training Center and Fort Polk; and Commander, US Army South and Joint Task Force-Panama. Awarded the Distinguished Service Medal.

Mr. Anthony Francis Pryor, BA (Cantab), PEng (Ont). Chairman, Devonport Royal Dockyard Limited; Director, Business Acquisitions, Brown and Root Services Europe and Africa Region. Former Managing Director, Vickers Group. Director, Hunting-BRAE Limited. Chairman, Joint Trade Association Working Group on the Competing for Quality programme. Former Chairman, Brown and Root Ealing Technical Services Limited; Chairman, Defence Manufacturers Association.

Sir Michael Quinlan, GCB. Former Permanent Under Secretary of State, Ministry of Defence; Former Director, The Ditchley Foundation; Defence Counsellor, UK Delegation to the North Atlantic Treaty Organization and Secretary, Eurogroup; Policy Director, Ministry of Defence. Member, International Institute for Strategic Studies. Author on international security issues. Awarded Knight Grand Cross of the Order of the Bath.

The Honorable Bernard D. Rostker, BS, MS, PhD. Under Secretary of the Army. Special Assistant to the Secretary of Defense for Gulf War Illnesses. Former Assistant Secretary of the Navy for Manpower and Reserve Affairs; Deputy Director, Army Studies and Analysis Center, and Director, Defense Manpower Research Center, RAND Corporation; Director, Selective Service System. Author, "Assessing the Structure and Mix of Future Active and Reserve Forces" and numerous other publications.

Colonel Michael C. Ryan, BS, MS, PhD. US Army Attaché to the United Kingdom. Former Army Attaché to the Kingdom of Spain; Brigade Executive Officer, 2nd Armored Division; White House Fellow; Associate Professor and Executive Officer, United States Military Academy; Executive Assistant to the Secretary of Defense. Awarded the Defense Superior Service Medal.

Mr. Peter Ryan. Head of the Public-Private Partnership Unit, Ministry of Defence. Responsible for Ministry of Defence privatisation projects, including market testing for outsourcing, Private Finance Initiative, strategic partnerships, and market initiatives. Former UK Air Defence Representative and Deputy Representative on Armaments Cooperation, North Atlantic Treaty Organization; Director for Central and Eastern Europe, Private Office of the Minister of Defence; Staff member, RAND Corporation.

Mr. Donovan D. Rypkema, BS, MS. Principal, Real Estate Services Group. Specialist in neighborhood and commercial district revitalization and adaptive reuse of historic buildings. Consultant, US Army Historic Property Advisory Group, the National Trust for Historic Preservation. Former Member, Board of Advisors, the National Trust for Historic Preservation. Member, Board of Directors, North Capital Neighborhood Development Corporation, Washington, DC. Author, "The Economics of Historic Preservation."

Mr. Richard P. Shields, BA. President, Mesirow Stein Real Estate, Inc. Responsible for $1.5 billion in current development projects, including the historic preservation and redevelopment of the Historic Landmark District at former US Army Post, Fort Sheridan, Illinois. Development Advisor, Orlando Naval Training Center and Glenview Naval Air Station. Member, US Army Historic Property Advisory Group, the National Trust for Historic Preservation; Reinventing Government Commission; US Courts Design/Build Task Force. Former President, The Quest Group; senior officer, ICF Kaiser Engineers.

Mr. Stan Z. Soloway, BA. Deputy Under Secretary of Defense for Acquisition Reform and Director, Defense Reform Office. Specialist in government contracting, acquisition policies, and outsourcing/privatization issues. Former Advisor, Contract Services Association. Founding Member, Acquisition Reform Working Group, Council of Defense and Space Industry Associations; Founder, Government Competition Coalition; Chairman, Industry Depot Coalition.

Mr. John Spellar, MP, BA (Oxon). Minister of State for the Armed Forces, Ministry of Defence. Member of Parliament for Warley West. Former Opposition Whip for Employment, Trade and Industry, and the Defence Committee; Opposition Spokesman on Northern Ireland and on Defence. Member, Trade Union Committee for European and Transatlantic Understanding; National Officer, the Electrical, Electronic, Telecommunications and Plumbing Union.

Major General Charles W. Thomas, BS, MS. Chief of Staff, US Army Training and Doctrine Command. Former Commanding General, US Army Intelligence Center and Fort Huachuca; Deputy Chief of Staff, Intelligence, Headquarters, US Army Europe and Seventh Army; Deputy Director, Current Intelligence, Defense Intelligence Agency; Director, US Central Command Joint Intelligence Center, Saudi Arabia. Awarded the Distinguished Service Medal.

Field Marshal The Lord Vincent of Coleshill, GBE, KCB, DSO, DSc. Chairman, Hunting Defence Ltd. Chancellor, Cranfield University. Chairman, Imperial College of Science, Technology and Medicine. Former Chief of Defence Staff; Chairman, Military Committee, North Atlantic Treaty Organization. Fellow, Institution of Mechanical Engineers; Royal Aeronautical Society; Imperial College, London. Vice President, Defence Manufacturers Association. Governor, The Ditchley Foundation. Freeman, City of London. Life Peer. Awarded Knight Grand Cross of the British Empire, Knight Commander of the Order of the Bath, and the Legion of Merit.

Brigadier General Craig B. Whelden, BA, MA. Commanding General, US Army Community and Family Support Center. Former Deputy Director for Operations, National Military Command Center; Chief of Staff, 3rd Infantry Division; and Commander, 98th Area Support Group (Germany). Awarded the Defense Superior Service Medal.

Mr. Roger J. Whysall, BSc (Hons), FRAeS, CEng. Chief Executive, Hunting Defence Limited. Chairman, the Irvin Group; Director, Hunting PLC and Hunting-BRAE; Chairman, Hunting Contract Services and Hunting Technical Support. Member, Board of Pera International; Fellow, The Royal Aeronautical Society; Member, the SBAC Council.

Mr. John R. Wilson. Chief Executive, Defence Housing Executive. Former Finance Director and Deputy Chief Executive, DHE. Responsible for £500 million programme to modernize family housing for the Ministry of Defence. Delivered four Private Finance Initiative projects with two more underway. Experienced in project management, finance, personnel, training and administration.

Mr. Randall A. Yim, BA, JD. Deputy Under Secretary of Defense for Installations. Former Principal Deputy Assistant Secretary of the Army for Installations, Logistics, and Environment; Deputy Director, Sacramento County Department of Military Base Conversion. Founding member and past president, Asian-American Bar Association of Sacramento. Former editor and publisher, "The Military Base Reuse Forum;" contributing editor, "The Base Reuse Report."

RESEARCH STAFF

Dr. Ellen M. Pint, BA, MA (Oxon), PhD. US-UK Privatization Conference Research Team Leader. Senior Economist, RAND Corporation. Rhodes Scholar. Specialist in Financial Management, Outsourcing, Regulation, Privatization. Participant in evaluation of US Army Single Stock Fund Initiative and financial management processes for logistics; study of outsourcing options for US Air Force acquisition reform; and analysis of the effects of British privatization and nationalized industry policy on corporate objectives. Member, American Economics Association; Econometric Society; Royal Economic Society; and Western Economic Association International. Author, "Applying the Velocity Management Approach to Logistics" and numerous other publications.

Dr. Jonathan Cave, BS, MA (Cantab), PhD. Senior Economist, RAND Corporation Europe. Specialist in program evaluation, industrial organization and international policy. Senior Lecturer, Department of Economics, University of Warwick. Member, American Economic Association; Econometric Society; European Network for Industrial Policy; Operations Research Society of America; UK Law and Economics, Public Economic Networks. Author, "Smart Procurement: Report on Procurement Reform in the United Kingdom" and numerous other publications.

Dr. James C. Wendt, BS, MS, PhD. Special Assistant for Privatization Research to the Assistant Secretary of the Army for Installations and Environment. Responsible for US-UK Privatization Conference administration. Senior Analyst, RAND Corporation. Specialist in international strategic defense

research. Former Assistant Professor, Columbia University. Member, International Institute for Strategic Studies. Author, "Innovation and Defense Organization: Implementing the Revolution in Military Affairs" and numerous other publications.

Appendix C: Conference Agenda

FRIDAY, 14 APRIL

1530 Arrival at Ditchley Park

1600 Tea

1630-1800 **PLENARY SESSION I**

Opening Remarks by **The Honorable Richard B. Cheney**
Field Marshal The Lord Vincent

Introduction by The Honorable Mahlon Apgar, IV

Responses by Dr. David S. C. Chu and Mr. Martin J. Kitterick

1800-1815 Coffee

1800 Group Chairmen and Rapporteurs (Organizational Meeting)

1815-1930 **DISCUSSION GROUP SESSION I**

Discussion Group A – Housing and Facilities Management

- Recapitalizing the housing stock
- Transferring "ownership" and management
- Working with tenants and local communities
- Forging new partnerships with industry
- Designing "Smart Client" strategies

Discussion Group B – Base Operations and Services

- Ensuring military control
- Gaining political support
- Maintaining desired levels of performance
- Providing new services in non-traditional ways

Discussion Group C – Logistics

- Identifying candidates for privatization
- Organizing a new military-industry structure
- Determining the appropriate scope
- Ensuring sustainable support

1930 Reception

2015 Dinner

SATURDAY, 15 APRIL

0830-0915 Breakfast

0930-1100 **DISCUSSION GROUP SESSION II**

1100-1115 Break

1115-1230 **DISCUSSION GROUP SESSION III**

1230-1300 Pre-lunch gathering

1300-1345 Lunch

1345 Transport departs for Oxford and Broughton Castle

1530 Return to Ditchley

1600 Tea

1630-1800 **DISCUSSION GROUP SESSION IV**

1800 Group Rapporteurs, in consultation with their Group Chairmen, prepare brief reports for circulation to the plenary session on Sunday morning. Secretaries will be on hand to assist with this.

1930 Group Photo on Main Entrance steps

1945 Reception

2015 Dinner (Black Tie, Army Blue Mess)

SUNDAY, 16 APRIL

0815-0900 Breakfast

0915-1000 **PLENARY SESSION II**
Presentation and discussion of Group A's report

1000-1045	**PLENARY SESSION III** Presentation and discussion of Group B's report	
1045	Coffee	
1115-1200	**PLENARY SESSION IV** Presentation and discussion of Group C's report	
1200-1300	**PLENARY SESSION V**	
	Final Discussion	
	Closing Remarks by	**The Honorable Dr. Bernard D. Rostker and Field Marshal The Lord Vincent**
1300	Pre-lunch gathering	
1315-1400	Lunch	
1400	Departure	



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Appendix D: Group Reports

DISCUSSION GROUP A: HOUSING

SITUATION
- Shortage of affordable housing
- Unacceptable housing quality

GOALS
- Support the Army's mission
- Retain and sustain soldiers and their families

MEANS
- Involve local commanders and soldier in process
- Construct new units; renovate existing units
- Engage the private sector
- Generate funds by selling the income stream while transferring risk
- Rationalize capital allocation through accounting reform
- Define and attain "value for money"
- Focus on core installations
- Establish new creative structures for rewards and incentives: condo model, time share, time shift
- Develop sound business arrangements — with self-adjusting mechanisms and incentives

STATUS
- Generally we see a positive attitude toward privatization; part of broad trend
- Ft. Carson has achieved initial success; U.K. experience confirms viability
- RCI has big pilot program: 4 sites with 16,000 units
- But military leaders are in a wait-and-see mode; deep concerns about a 50-year relationship and what happens if it doesn't hold up
- Congress apparently conflicted
- Industry voice mute

ISSUES
- What strategy should we employ to deal with stovepipes?
- Will government-style accountability discourage the private sector? What can/should be done about it?
- How can we capitalize on potential for commercial development?
- Should we be aiming for "real" privatization, rather than just another form of contracting?
- Can we build equity for soldiers through time-sharing?
- Should we package multiple installations for privatization?

DISCUSSION GROUP B: BASE OPERATIONS

INTRODUCTION

The U.S. Army faces a fundamental crisis. It is under-resourced and no relief is in sight — indeed it faces potential dangers in the next QDR. Current efforts to address the problems are piecemeal and insufficient. Political climate for BRAC-like solutions likely to remain very difficult.

There are no easy solutions. But some obvious things can and must be done.

LOOKING OUTSIDE THE BOX

Avoid temptation to navel-gaze. U.S. economy undergoing dramatic and speedy changes in business practices. By working with the private sector, a dedicated and forward-looking Army leadership can identify ways to deliver radical change quickly, even within existing constraints.

U.S. experience of contractorization in Bosnia, etc., proof that private sector does deliver. Introducing private sector efficiencies in CONUS and in overseas bases can release funds to help underpin Army's modernization program — without endangering the mission.

Countries such as the U.K. have pushed the envelope, e.g., the U.K. MoD has spent $400 million on introducing resource accounting and budgeting. U.K. MoD is also attracting billions of dollars of private sector investment and enabling delivery by the private sector of a wide range of services which until recently were regarded as core military business.

WAY AHEAD

Recognize that there is a crisis and that current approach will not deliver a solution.

Meaningful and accurate resource/cost information is essential to inform key decisions at all levels. Introducing a system will take time and money and be painful, but this has to be done. Meanwhile, make every effort to utilize insights from activity-based costing.

Develop a top-level business vision, drawing upon relevant evidence from best-in-class private sector and other institutions world-wide.

Put together implementation strategy to be delivered by top team.

Find ways to rationalize state/infrastructure — take every available opportunity, scoring quick wins wherever possible.

Press on with experiments such as RCI.

Educate key decision-makers at all levels on gravity of crisis, range of options available, and need to deliver results.

Incentivize those decision-makers by enabling them to reinvest significant portion of efficiency gains in their business area.

Devote major effort towards becoming a truly intelligent customer, recognizing what private sector has to offer.

Inaugurate radical and ruthless review of what are key functions that need to be delivered by uniformed personnel and DoD staff. Work with private sector partners to identify what can be outsourced or done in partnership with the private sector.

Develop key meaningful performance indicators. Incorporate them in commercial contracts. Concentrate on outputs.

Work to attract private sector partners to develop/exploit all commercialization options, thus generating revenue and reducing real estate burden.

Question assumption that outsourcing necessarily means only constraints; emphasize improved flexibility that the right contract can offer.

SUMMARY

There is now convincing evidence that the private sector can deliver effective performance through innovative business practices, fully meeting the Army's requirements while releasing resources for essential (and currently unfunded) equipment modernization. Army needs to develop game plan and to implement it bottom up as well as top down.

DISCUSSION GROUP C: LOGISTICS

1. DEFINITIONS

    1.1. Logistics: supply, maintenance, transportation, field services, construction engineering, together with the facilities that support them.

    1.2. Privatization: a range of possibilities for engaging the private sector in providing services to the government that could include simply the provision of services in government-owned facilities, or could extend to the sale of government assets or encouragement by the private sector to provide new capital assets.

2. IDENTIFYING CANDIDATES FOR PRIVATIZATION

    2.1. Define those activities which can only be performed by scarce, trained military personnel. Remainder are candidates for privatization.

    2.2. Assess the ability of the private sector versus the public sector to provide the service.

    2.3. Define function/operation, its outputs, its success criteria, its boundaries — BASED UPON STRATEGIC VIEW OF BUSINESS. Top-level (including political) support will be essential to success.

    2.4. Establish a clear owner, with authority, and hold accountable.

    Caveats

    i. Robustness of privatized arrangement
    ii. Effect on the market. Can we live with the effect on future competition?
    iii. Need adequate data for comparisons, including current cost of outputs. U.K. decision to adopt accrual accounting will improve the basis for decision-making.

3. DETERMINING THE APPROPRIATE SCOPE

    3.1. Responsibility for the architecture of the supply chain is the Government's, optimizing the capabilities of what the in-house system can provide and what the private sector can do best. Its objective is to provide responsive support to combat elements, who should not have to worry about where their support is coming from, or whether it is going to arrive on time.

3.2. To achieve this, it is essential that decisions be taken on a strategic view of business. Ultimately, for example, this would involve packaging support with the original acquisition of equipment or equipment services — "power by the hour."

3.3. Focus on outputs, not inputs. CUSTOMER FOCUS AT ALL TIMES.

4. ORGANIZING A NEW MILITARY-INDUSTRY STRUCTURE/ENSURING SUSTAINABLE SUPPORT

4.1. Two broad approaches: public corporations versus contractual relationships that link the public and private sectors.

4.2. Objective is long-term sustainable support capability. This leads to using longer-term contracts, and perhaps not setting all prices in advance. Emphasis shifting to selection of partner rather than selection of bid.

4.3. But there is a trade-off between long-term partnerships and maintaining competition.

4.4. Place greater emphasis on whole life (life cycle) costing and link it to the acquisition decision.

4.5. A sub-objective should be to eliminate unnecessary duplication between government and private facilities. Identify and optimize complementary capability in public and private sectors.

4.6. Selecting a contractor is like using a funnel. But a lengthy or expensive funnel will drive away applicants. Need clear criteria for evaluation set at the start of the process.

4.7. Performance and reward should be closely linked. Gains should be shared between the contractor and the government. Increasing performance targets are the aim. A strong performance evaluation capability is needed, but at the moment both the U.K. and U.S. are "better at making contracts than managing them."

4.8. Openness and transparency as a basis for management of a contract and incentivization. "DEALS NOT RULES."