



DoD Workforce Cost Realism Assessment

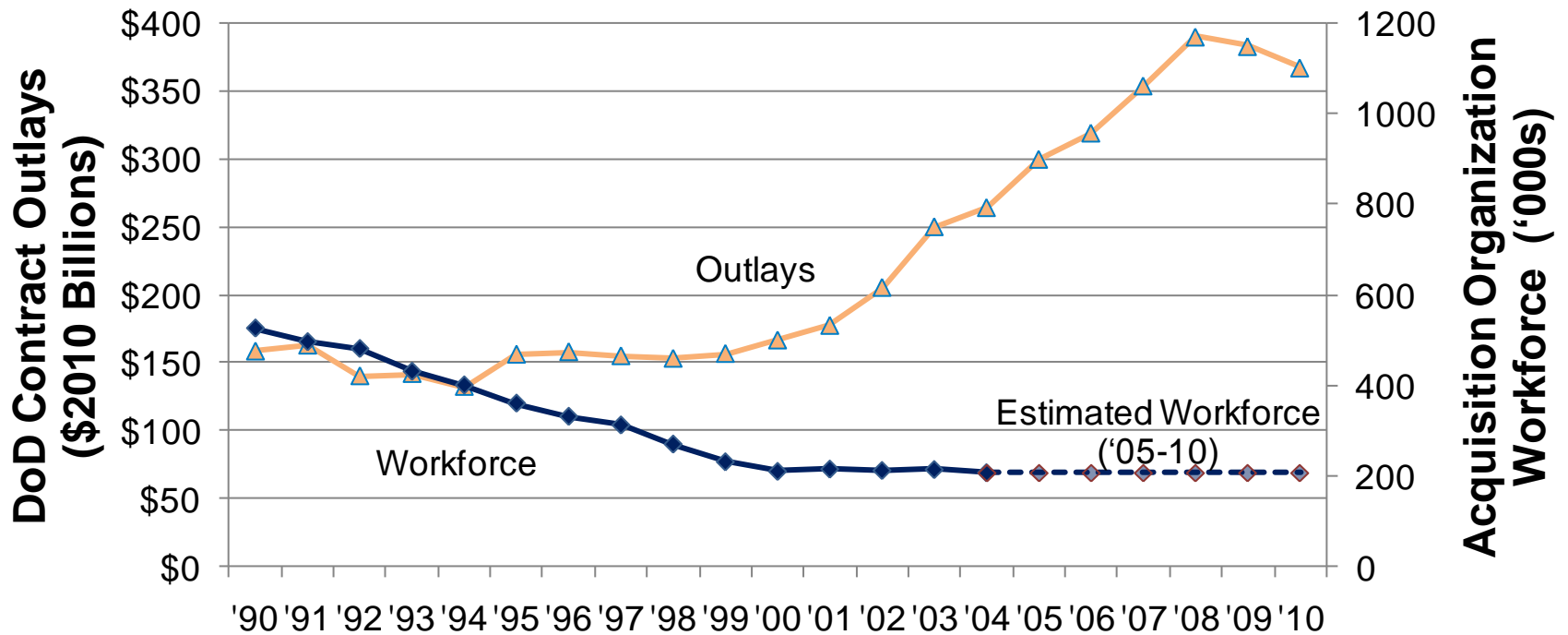
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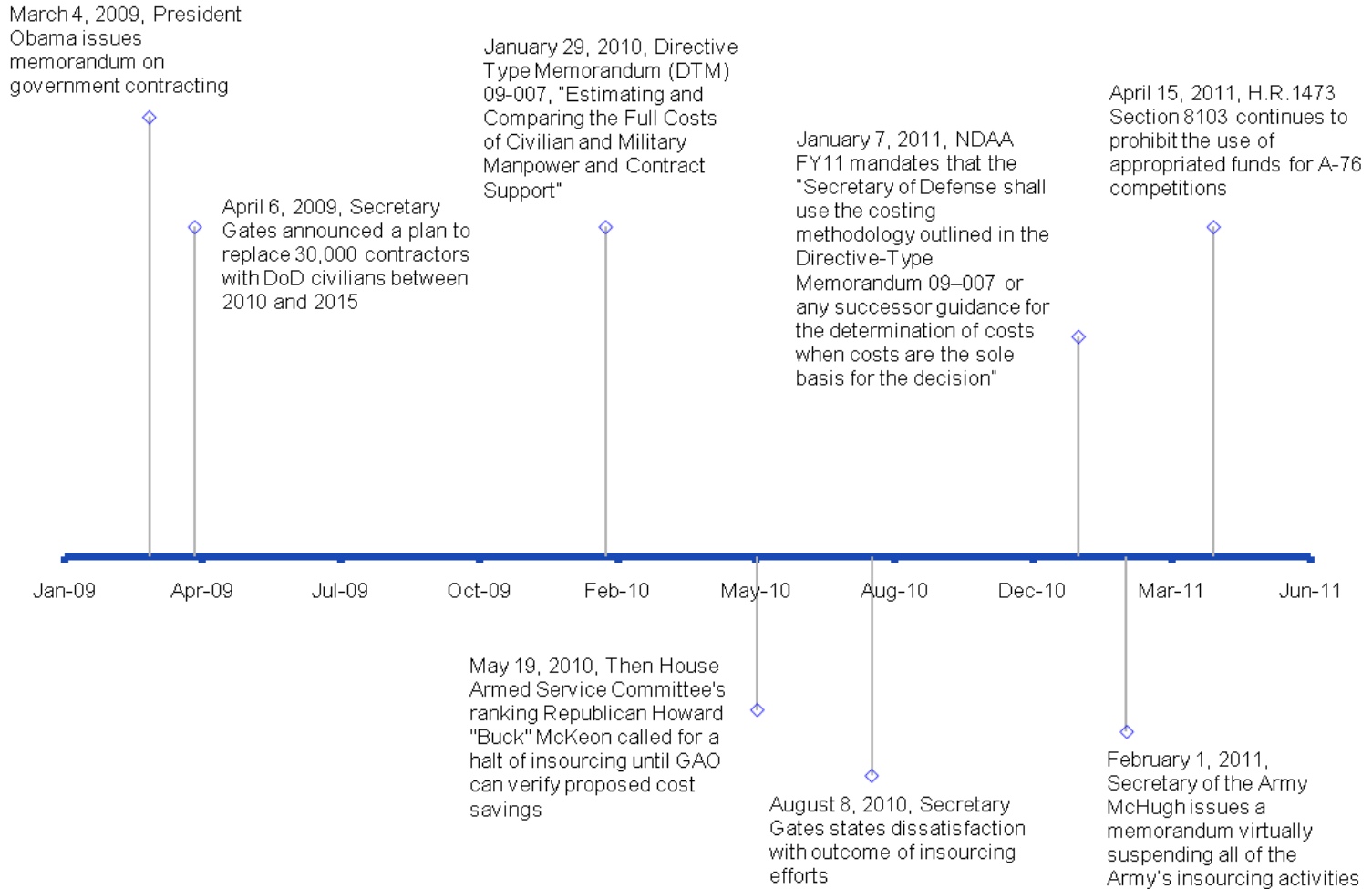
Defense-Industrial
Initiatives Group

Overall DoD Acquisition Workforce Declined As DoD Contract Outlays Increased, 1994-2010



Source: Acquisition organization workforce from DoD IG Report D-2000-088, Feb 29, 2000 & DoD IG Report D-2006-073, April 17, 2006. DoD Contract Outlays from the Federal Procurement Data System (available at <https://www.fdps.gov>).

DoD Insourcing Initiative



The Drive Toward Insourcing

March 4, 2009 - President Obama issues memorandum on government contracting:

- Directs OMB to review policies for contracting for services

April 6, 2009 - Secretary Gates announced a plan to replace 30,000 contractors with DoD civilians between 2010 and 2015:

- “Restore balance” to the workforce by returning the ratio of contractors to DoD civilians to its 2001 level
- Achieve budgetary savings equal to 40 percent of the cost of the contractors being replaced

Insourcing Guidance – the DTM

January 29, 2010 - Directive Type Memorandum (DTM) 09-007, “Estimating and Comparing the Full Costs of Civilian and Military Manpower and Contract Support”:

- DoD’s sole guidance for conducting cost comparisons and determining the budgetary impact of insourcing decisions
- Expected to be converted to a new DoD Instruction by September 1, 2011

Congress Reactions

May 19, 2010 - Then House Armed Service Committee's ranking Republican Howard "Buck" McKeon called for a halt of insourcing until GAO can verify proposed cost savings:

- Congressional concerns about unintended consequences of insourcing

January 7, 2011 - NDAA FY11 mandates that the “Secretary of Defense shall use the costing methodology outlined in the Directive-Type Memorandum 09–007 or any successor guidance for the determination of costs when costs are the sole basis for the decision”:

- Solidifies the DTM as the sole cost comparison methodology for DoD insourcing

April 15, 2011 – The President signs H.R.1473 into law, whose section 8103 continues to prohibit the use of appropriated funds for A-76 competitions:

- Bill language continues to prohibit A-76 competitions unless requirements of section 325 of the NDAA FY10 have been completed

DoD Reactions

August 8, 2010 - Secretary Gates states dissatisfaction with outcome of insourcing efforts:

- “Based on the data available after one year, I am not satisfied with the progress made to reduce our over-reliance on contractors.”
- “With regard to insourcing, other than changes planned for FY 10, no more full-time positions in these organizations [OSD, Defense Agency, and Combatant Commands] will be created after this fiscal year to replace contractors.”

February 1, 2011 - Secretary of the Army McHugh issues a memorandum virtually suspending all of the Army’s insourcing activities:

- “I reserve to myself the authority to approve any in-sourcing proposal, wherever generated across the Army. “

CSIS Insourcing Assessment

Wider governance:

- In a time of budgetary strain, the United States government must have repeatable, verifiable, and data driven mechanisms for making decisions and understanding their resource implications, including associated costs.

Insourcing specific:

- Proper cost estimating must be a core element of any insourcing decision, regardless of whether or not it is being made for budgetary reasons.
- The DTM's procedures of conducting cost comparison for making insourcing decisions have several significant gaps.
- No other DoD methodology has been officially approved for implementation.
- According to a February 15 conference call statement by DoD Comptroller Hale, out-year DoD budget "savings" still need to be accounted for.

The Directive Type Memorandum

Purpose:

- Establishes business rules for use in estimating and comparing the full costs of military and DoD civilian manpower and contract support

Claims to provide:

- A list of cost elements and methodologies for estimating and comparing the full costs of military and civilian manpower and contract support
- The data sources and calculations for direct labor cost elements for military and DoD civilian personnel
- A list of the kinds of goods, services, and benefits that should be considered when developing non-labor cost estimates
- An example of a cost comparison

Directive Type Memorandum: Key Shortcomings

- **Lacks consistent focus on fully burdened government wide costs**
- **Fails to account for the full cost of DoD-owned capital but includes those costs for contractors**
- **Fails to account for taxes forgone by the federal treasury or state or local governments**
- **Fails to account for the inherent risk of cost growth among public producers**
- **Overlooks the cumulative effect of multiple in-sourcing decisions**
- **Overlooks the imputed costs of insuring and indemnifying in-house producers**
- **Fails to account for non-cost factors, such as varying workload stability**
- **Fails to utilize a detailed Scope of Work as a basis for cost estimation**
- **Lacks specificity on how to calculate cost components**

An Alternative – the A-76 Process?

- **Included the cost of in-house production at a private sector rate of return on new investments**
- **Included forgone federal taxes as a cost element for in-house producers**
- **Required that in-house producers take into account what it would cost if they were required to purchase casualty and liability insurance**
- **Required a Performance Work Statement**
- **Offered high level of specificity for cost components**

The CSIS Cost Comparison Methodology

- **Emphasizes the usage of fully burdened costs to the federal government as the basis of the public sector's cost estimate**
- **Utilizes OMB Circular A-76 and the Directive Type Memorandum 09-007 as a foundation**
- **Enhances specific aspects of these pieces of guidance to correct for identified shortcomings**

The CSIS Cost Comparison Methodology (Continued)

- **Introduces a statement of work (SOW) as a common starting point for public-private competitions with uniform, clearly defined performance parameters upon which proposals will be evaluated**
- **Mandates more frequent updates for calculating personnel cost elements such as health care and retirement benefits to ensure as accurate a cost estimate for military and civilian employees as possible**
- **Provides a more robust overhead cost component**
- **Includes:**
 - Inherent risk of cost growth for both, the public and private sector
 - Expected transition costs in both directions - public to private and vice versa
 - Oversight and administration cost for both the public and private sector
 - Tax revenue generated by the private sector following the OMB Circular A-76 model
 - Effects of varying workload stability within a commercial activity
 - Effects of cumulative effects of multiple insourcing and outsourcing decisions on indirect cost structures within the public and private sector
 - Hypothetical costs for insuring and indemnifying of the public sector following the OMB Circular A-76 model

The CSIS Cost Comparison Components

Statement of Work

Public

- Personnel costs
- Material & Supply costs
- Facilities costs
- Capital costs
- Overhead costs
- Additional costs

Private

- Contract price
- Income tax adjustment
- Government contract administration and oversight costs
- Additional costs

The Problem of Definition and the 12 Percent Fallacy

- **There is no universally accepted definition on the components of overhead.**
- **Overhead calculated as a percentage of different baselines is making comparisons imprecise and potentially misleading.**
- **Without a common reference point, any comparison is methodologically suspect, and any decision is potentially unjustified.**
- **A-76's 12 percent figure was the product of negotiations between OMB, public-sector unions, and the private sector.**
- **Private sector overhead rates are commonly several times higher. Government is not that much more efficient.**
- **Private sector overhead rates vary significantly between different business sectors. Why use one common overhead factor for government?**

A New Approach – Overhead Line Items

- **Operational Overhead – Management & Oversight**
- **Information Technology**
- **HR/Personnel**
- **Legal support**
- **Accounting**
- **Payroll**
- **Headquarters management**
- **Miscellaneous**
- ***Note: As with A-76, facilities costs are broken out separately.***

The CSIS Public Cost Estimation Taxonomy

Personnel	Overhead	Facilities	Additional Costs
Direct Labor (Military & Civilian; including health care and retirement benefits)	Operational Overhead - Management & Oversight	Cost of Facility	Liability Insurance
Fringe	Information Technology	Rent	Travel
	HR/Personnel	Insurance	Subcontracts
	Legal Support	Maintenance & Repair	Nonrecurring Workloads
	Accounting	Utilities	Minor Items
	Payroll	Capital Improvements	Medical Exams
	Headquarters Management	Capital	Training
	Miscellaneous	Cost of Capital	Cost Growth
		Depreciation	Conversion Costs
Material & Supply			Administration & Oversight Costs
General			
Inflation			
Insurance			
Maintenance & Repair			

Way Forward for DoD

- **More transparency and access to data**
- **Engage relevant stakeholders**
- **Modify DTM to incorporate fully burdened costs**
- **Use modified DTM as basis for new DoD Instruction**

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H.R. 1473 Outsourcing Language

SEC. 8103. (a) PROHIBITION ON CONVERSION OF FUNCTIONS PERFORMED BY FEDERAL EMPLOYEES TO CONTRACTOR PERFORMANCE.—None of the funds appropriated by this Act or otherwise available to the Department of Defense may be used to begin or announce the competition to award to a contractor or convert to performance by a contractor any functions performed by Federal employees pursuant to a study conducted under Office of Management and Budget (OMB) Circular A–76.

(b) EXCEPTION.—The prohibition in subsection (a) shall not apply to the award of a function to a contractor or the conversion of a function to performance by a contractor pursuant to a study conducted under Office of Management and Budget (OMB) Circular A–76 once all reporting and certifications required by section 325 of the National Defense Authorization Act for Fiscal Year 2010 (Public Law 111–84) have been satisfactorily completed.

DTM Critique Cross-Reference

1) Lacks Consistent Focus on Fully Burdened Government-Wide Costs

- P. 5, 1.a.: “Manpower cost estimates normally address costs to the Department of Defense. However, in certain cases, analysts may be asked to report full manpower costs to the Federal Government.”
- P.7. 2.a.(1)(a)1.: “Direct labor costs for military and DoD civilian manpower can be divided into two categories: costs paid by the Department of Defense and costs paid by other Federal agencies.”
- P.11, 2.b.: “The costs of service contracts are variable costs in the short run paid by the Department of Defense.”
- P.12-13, 3.a.: “Manpower costs discussed in paragraph 2.a. of this attachment can be accounted for in four ways, each applicable in different situations.” The four ways listed are:
 - Base Pay with Locality Adjustments and Allowances
 - Programmed Amount
 - Full Cost to the Department of Defense
 - Full Cost to the Federal Government
- P.14, 3.c.: “When developing cost estimates for DoD manpower and service contracts, the full costs to the Department are considered and only common costs are excluded”

2) Fails to Account for Full Cost of DoD-Owned Capital

- P.21, Attachment 5, a: “Costs of capital assets valued at \$25,000 or more, plus the costs of depreciation, maintenance, and repair” is included in the list of goods, services, and benefits presented in attachment 5, which could provide a starting point when developing cost estimates. Beyond this the full cost of DoD-owned capital is not accounted for in the DTM.

3) Fails to Account for Foregone Taxes

- Not accounted for in the DTM

DTM Critique Cross-Reference (Continued)

4) Fails to account for the inherent risk of cost growth among public producers

- P.11, 2.b.(1): “Cost analysts should, where appropriate, take into account the inherent risk of cost growth after contract negotiation.” There exists no corresponding clause for the public cost estimation, leaving an assumption of no cost growth.

5) Overlooks the cumulative effect of multiple in-sourcing decisions

- Not accounted for; p.9, 2.a.(2) covers such indirect costs, but not in the context of cumulative insourcing activities.

6) Overlooks the imputed costs of insuring and indemnifying in-house producers

- P.12, 2.b.(2)(c)1.: “When military or DoD civilian personnel perform a function, their actions are covered by sovereign immunity. However, when a contractor performs a function, the contractor can be sued. To the extent the Government must indemnify or reimburse the contractor or its insurer, the Department of Defense incurs additional expenses and contingent liabilities that would not have to be paid if military or DoD civilian personnel performed the work.”
- P.12, 2.b.(2)(c)3.: “These costs are not common costs because they would not be incurred if Government personnel performed the work. If practical and if data are available, the DoD Components should incorporate these costs into their estimates.”

7) Fails to account for non-cost factors, such as varying workload stability

- Not accounted for in the DTM.