PUBLIC-PRIVATE PARTNERSHIPS
AND THE FUTURE OF THE ARMY INDUSTRIAL ENTERPRISE

Lexington Institute
EXECUTIVE SUMMARY

At the heart of the Department of Defense’s (DoD) acquisition and logistics transformation are Public-Private Partnerships (P3). This transformational effort recognizes the unique elements that both the organic base and private industry bring to the table — the organic base being known for unique industrial capabilities and a wealth of experience, and private industry acknowledged for its expertise in business practices, supply chain management and advanced design.

DoD is pursuing innovative Public-Private Partnerships to maintain and improve core competencies at organic depot facilities and to make its facilities and workforce available to partner in industry initiatives, for either military or industrial activities. The DoD is marketing these competencies, its reduced cost of labor and its renewed — and in some cases highly unique — industrial capabilities directly to industry as a means to keep industrial skills and facilities at the ready. As draw-down and reset occur from Operations Enduring Freedom and Iraqi Freedom, such partnerships will become even more critical in keeping the organic industrial enterprise at a high level of preparedness for future conflicts.

Why partner? Both the government and industry can benefit from each community’s skills, knowledge and approach to doing business. The types of P3s are diverse and flexible, ranging from work sharing, teaming, facility and equipment leasing, to Performance Based Logistics (PBL). To date there have been numerous successes with P3s, inclusive of PBLs such as the one between Anniston Army Depot and General Dynamics, and the highly effective partnership between Lake City Ammunition Plant and Alliant Techsystems. These partnerships have led to more advanced skills for depot workers and brought leading-edge repair technologies in-house.

Despite the fact that the organic and private sector bases have been working side-by-side for many years, there are difficulties based on laws and regulations that may need some reform to accommodate the transformation initiatives under Force-centric Logistics Enterprise, P3 and PBL. The single largest failure with this transformational effort is that the DoD is not being aggressive, imaginative or expansive enough.

It is ironic, however, that the government is seeking a closer relationship with the private sector to take advantage of precisely those skills and methods that can make industry difficult to work with. The government’s requirement to operate under established laws and regulations can make cooperation between the government and the private sector difficult.

The DoD and Congress must make efforts to rid the system of legislative, financial, cultural and educational impediments. Incentives must exist to entice the private industry to enter partnerships. Legislation needs to reform the accounting system, the working capital funds, the contract process and the debate over “colors of money.” Furthermore, the DoD must begin an education campaign for all the major stakeholders to highlight the value of P3s and the full scope of the law. These actions will fully transform the acquisition and logistics process and bring total life-cycle systems management to fruition.

The initial draft of this report was written by Ms. Carrie Hunter. Members of the Logistics Working Group had an opportunity to review and modify the final report.
INTRODUCTION

As part of transformation, the Department of Defense (DoD) has been engaged in a Department-wide effort to modernize its organic industrial base and align the overarching logistics enterprise. The DoD has looked to the private sector as a source of best business practices, benchmarking their innovative partnering approaches, while working through funding and downsizing pressures, process improvements and infrastructure reorganization (Lean, Six Sigma).

In terms of managing the National Technology and Industrial Base (NTIB), DoD’s strategic challenge is to meet the needs of national security in times of peace as well as anticipating and meeting these demands when at war. There is no absolute way to predict how much capacity and capability the DoD must maintain to achieve this balance. The critical issues of providing support for legacy systems as well as meeting surge demands of new conflicts are especially demanding under existing constructs. The Office of the Secretary of Defense has developed and enacted the Force-centric Logistics Enterprise to address these strategic needs, in ways that will provide best-value support for the warfighter. Public-Private Partnerships (P3) and Performance Based Logistics (PBL) are central to this Force-centric Logistics Enterprise concept. The idea is to leverage the best of the NTIB to support the warfighter through new levels of partnering that emphasize shared goals, risks and rewards with a focus on outcomes.

DoD is expanding P3s to make its organic facilities and workforce available to partner with industry on new business ventures, whether for military or industrial activities. Military depots maintain, repair, overhaul, engineer, manufacture, and in some cases, manage everything from parts of weapons to whole weapons systems or platforms. The DoD is marketing these industrial capabilities directly to industry as a means to keep industrial skills and facilities at the ready throughout the NTIB. As draw-down and reset occur from Operations Enduring Freedom and Iraqi Freedom, partnering will become even more critical in keeping the NTIB at a high level of preparedness for future conflicts in an era of shrinking program budgets, vanishing legacy systems, and jointness.
Why partner? Partnerships can contribute to more effective DoD maintenance operations, the introduction of innovative processes or technology, and the economical sustainment of organic capabilities. Most important, partnering is a cooperative effort, not a competitive engagement.

With this comes a shift in paradigm: the government’s need for control, oversight, information, and workload surety all work against the capitalistic character of private-sector firms. Despite the fact that the organic and private sector bases have actually been working side-by-side for many years, there is still some mistrust, misperception and bias.

A key issue is the difficulty private firms have making the business case for entering into or expanding their partnerships with DoD. One of the clearest examples of this is the ammunition sector. Companies that win contracts to manage the government-owned, contractor-operated facilities must still bid on production work. The length of the initial facilities contracts are often of insufficient duration to warrant the private firm investing much of its own money in the facilities, even though this would make the contract more profitable for the private firm and also save the government money. There is a great deal of uncertainty injected into the process.

These issues are amplified for the Army, which has the largest industrial base within DoD. It is also unique, including not only maintenance depots but also manufacturing arsenals, munitions centers, ammunition plants, and research and development facilities. The other services look to the Army’s industrial enterprise to meet a wide range of their needs from meals-ready-to-eat to arms and ammunition. As a result, the Army’s management challenges are more complex, and their mandate for P3 is far more expansive than that of DoD or the other services.

Public-Private Partnerships as defined by the military is new and evolving. DoD, the armed services and the Defense Logistics Agency, as well their commercial partners are all exploring what does and does not work best in these sorts of alliances. P3 is an evolutionary process. The private sector is much more accustomed to the incentive structures, transparency and collaboration that such partnerships require; this is less familiar territory for the government sector.

As part of a full DoD logistics transformation program, P3 with PBL would ideally drive a total life-cycle systems management support for weapons acquisition and sustainment. There is general agreement that P3 is the mechanism by which best value is attained for the warfighter, DoD and the industrial partners, and that depot maintenance partnerships can be an effective tool to implement PBL arrangements.

PUBLIC-PRIVATE PARTNERSHIPS DEFINED

DoD has defined Public-Private Partnerships at the depot level as:

…an agreement between an organic depot maintenance activity and one or more private industry or other entities to perform work or to utilize facilities and equipment. In general, depot maintenance public-private partnership arrangements include (but are not restricted to) one or more of the following forms:

• Use of public sector facilities, equipment, and employees to perform work or to produce goods for the private sector under certain defined circumstances;

• Private sector use of public sector equipment and facilities to perform work for the public sector; and

• Work-sharing agreements, using both public and private sector facilities and/or employees.
The Army has expanded this definition to include its entire organic industrial base. Unique among the services, the Army's organic base is comprised of depot maintenance facilities, manufacturing arsenals, ammunition plants and munitions centers. In addition, the Army maintains extensive maintenance capabilities at many of its class-one operating and training installations. Public-Private Partnerships, as defined by the Army, can be implemented at any of these 26 organic industrial facilities, whether government-owned, government-operated (GOGOs) or government-owned, contractor-operated (GOCOs) including offices, inventory control points and materiel/system logistics commands.

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Department of Defense Maintenance Depot Capabilities and Services, Office of the Secretary of Defense, August 2003.
The Army industrial facilities are organized within Life Cycle Management Commands and Major Subordinate Commands, a concept developed and implemented in 2004 to allow for continuity in warfighter support, from development through disposal. The Life Cycle Management Commands are:

- U.S. Army Aviation and Missile Life Cycle Management Command;
- U.S. Army Communications-Electronics Life Cycle Management Command;
- U.S. Army Tank-automotive and Armaments Life Cycle Management Command; and
- U.S. Army Field Support Command/Joint Munitions Command.

As of September 2005, the Army lists over 300 active P3s at GOGOs (192) and GOCOs (112). This number does not include active P3s at its research laboratories (which are known as Cooperative Research & Development Agreements) and other facilities. The objective of these partnerships is to enhance warfighter support through better synergies and improved effectiveness across the Army acquisition, technology and logistics community and providing better products faster while minimizing life-cycle costs.

Types of partnerships are diverse and flexible, including: workshare, teaming, sales of parts and services, facility and equipment leasing, Centers for Industrial and Technological Excellence partnering, Armament Retooling and Manufacturing Support Programs (ARMS), Arsenal Support Program Initiatives (ASPI), and Cooperative Research and Development Agreements.

Partnering agreements range from less formal Memorandums of Understanding to legal contracts under specific partnering authorities. P3s may differ from one to the next, but they all share a common element in that they must utilize some aspect of organic capability in support of the partnership. As stated earlier, P3s are enablers of PBL agreements, another key transformational tool.

**THE STATE OF PUBLIC-PRIVATE PARTNERSHIPS**

In fiscal year 2004, the military industrial base spent $25.4 billion, employed 70,000 civilian and military personnel and partnered with more than 1,000 private sector firms. Interestingly, P3s as currently defined still made up a very small percentage of total sustainment activities. The Defense Department traditionally partnered with industry in depot maintenance activities through work-share and facility-use agreements. These arrangements were not technically P3s. With depot P3s, the DoD is focused on finding private-sector partners to sustain and improve core depot maintenance activities, utilize excess capacity at facilities and provide facility capital investment. This is a wholly new approach to DoD relationships with the private sector, moving from the arm’s length nature of traditional contracts to the collaborative, longer-term relationships found in strategic alliances. The new policies and legal authorities for Public-Private Partnerships are fundamental elements in DoD’s transformational logistics initiatives.

The P3 structure creates opportunities, but requires significant change by both DoD and industrial partners to create the triple win: for the warfighter, the DoD program manager and the industrial partner. P3s are not limited to depot maintenance activities, but include all support and sustainment activities such as arsenals and ammunition plants. P3s and PBLs form a fundamental foundation of the DoD’s Force-centric Logistics Enterprise. As such, DoD seeks to expand and improve these initiatives and has instituted annual tracking mechanisms to measure progress.
DoD has P3s in place at 19 of 20 depot maintenance facilities across the services. As reported to the DoD by the services in October 2004, the current levels of depot partnerships and the various types of partnerships are noted below.

Table 1. Fiscal Year 2004 and Earlier Public-Private Partnerships by Service.

Table 2. Fiscal Year 2003 & 2004 Cumulative Public-Private Partnerships by Type.
Again, for the Army, P3 has been implemented across its organic base, in depot facilities as well as manufacturing arsenals and ammunition plants. For more than a decade, the Army has promoted commercial use of its ammunition plant facilities through the ARMS program, a P3 effort which promotes asset-based management and product diversification. There are currently 114 active ARMS agreements that sustain ammunition manufacturing capabilities while reducing GOCO ownership costs. Considered highly successful, Congress enacted a similar program for the manufacturing arsenals in 2001, the Arsenal Support Program Initiative. There are 14 active ASPI agreements at the three Army manufacturing arsenals. There are also over 90 active depot-level P3 agreements.

The Army has also taken some unique steps in implementing Public-Private Partnerships. At the Anniston Army Depot, General Dynamics is involved in a partnership to build the Stryker vehicles and refurbish Fox NBC Reconnaissance Vehicles. BAE Systems is cooperating with Anniston by taking some 600,000 hours of overflow work related to the reset of a large number of armored vehicles. At the Tobyhanna Army Depot, a multiyear partnership with Northrop Grumman is in place to support the design, manufacture, and installation of Blue Force Tracking equipment. Also at Anniston, Honeywell is initiating a major partnership program to build T1500 tank engines.

With its GOCOs, the Army has tested various partnerships to determine what works best in the Armament Retooling and Manufacturing Support Programs. The Lake City Ammunition Plant was an aging facility. Through an agreement with Alliant Techsystems, which also holds the contract to operate Lake City, scarce ammunition production capabilities have been relocated to that facility. Alliant Techsystems invested the funds to acquire critical technologies and redeploy them to government-owned facilities at Lake City. The ARMS program has also supported modernization of some vital operations at Lake City and the removal of production bottlenecks. As a result, the plant operates more efficiently, the government receives a better product at an extremely competitive price and Alliant Techsystems can make a profit.

With uncertain budgets and anticipated draw-down in Iraq, the Army is especially interested in exploring creative ideas from industry and the depots that will keep these core capabilities viable. The goal is 100-percent plant utilization, whether at war or in peace. Cost effectiveness is measured through high overhead offsets, a number which includes revenue streams and direct labor hours. Value indicators also include the number of repeat P3 customers, and the number of jobs and amounts of investment generated, whether private or public. To identify and facilitate additional P3s, the Army Materiel Command's Industrial Base Capabilities Directorate, Office of the Deputy Chief of Staff for Business Transformation, G-7 is coordinating and consolidating P3 data and information, and is developing “One-Stop Shopping” capabilities for business partners.

Local commands have explored business development through different approaches. The Watervliet Arsenal hired a broker and has focused on commercial manufacturing opportunities. Pine Bluff Arsenal developed an in-house office and has come up with creative “in kind” P3s such as swapping storage of excess rail cars for rail line maintenance throughout the base. Rock Island Arsenal also hired a broker to lease out excess office and warehouse space and, recently, to develop leases for the manufacturing plant and equipment.

The P3 opportunities however are not limited to what are currently being performed at these locations. For instance, P3s could include build-to-suit office or manufacturing facilities where industry partners or companies could lease already equipped research and testing labs to avoid expensive capital investments for initial research, design and development. The list of possibili-
ties is extensive, but not without challenges that range from financing and liability to managing risk and security. The Army is interested in exploring diverse possibilities for P3s, and is looking to industry for additional ideas and solutions.

Through their own initiative, DoD depots have earned new respect within industry for their skilled labor, upgraded facilities, and unique market posture. Well on their way to becoming lean, agile and more responsive, depots can offer a best value in skilled labor, access to testing facilities, utilization of specialized testing and support equipment, engineering expertise, and knowledge management. Arsenals and ammunition plants offer similar capabilities, as well as unique partnering opportunities in real estate and facility/plant/equipment leasing. Private sector partners can offer investment capital, marketing, technological and process expertise. There is general agreement that the P3 concept is the best mechanism to date by which the best value for the warfighter, DoD and the industrial partners will be achieved.

**P3 AND THE OTHER ARMED SERVICES**

The Army is certainly not alone in pursuing Public-Private Partnerships to enhance the operation of its supply chain. The Army has aggressively assessed the experiences of the Air Force, Navy and Marine Corps for best practices that can be imported into the Army system. The most effective partnerships are those that focus on enhancing performance of the supply chain while driving down costs.
The F/A-22 Support Partnerships break new ground for the Air Force. The Oklahoma Air Logistics Center at Tinker Air Force Base has created a unique set of procurement and sustainment partnerships with the prime contractor, Lockheed Martin, and with Pratt and Whitney, the engine vendor. Lockheed is the Product Support Integrator, and provides system integration and all logistics support management. Pratt and Whitney, as per agreement with the Oklahoma Air Logistics Center, provides all depot-level maintenance and ensures a guaranteed engine availability at a fixed price. But rather than send engines back to one of their sites, they use the facilities and touch labor at the base and provide an onsite management team.

Lockheed Martin is the prime vendor on the airframe and has developed five subsystem maintenance agreements with the original equipment manufacturers based at three Air Logistics Centers: Ogden, Warner Robins and Tinker. The depots provide touch labor and facilities, the Defense Logistics Agency provides consumables, and Lockheed Martin and Boeing manage unique items for the supply chain. Air Force teams will learn best business practices directly from the Original Equipment Manufacturers including shop management, production controls, computerized diagnostics and paperless maintenance, repair and operations. Follow-up contracts provide for performance based “agile” logistics support for additional F-22 sustainment. “Agile” refers to lean manufacturing, collaborative alliances and a transparent supply chain throughout the network of partners providing support to this weapons system.

At Warner Robins, Boeing works in partnership with the depot on C-17 maintenance. Northrop Grumman has a similar relationship at that same facility in support of the JSTARS surveillance aircraft. In both instances, the key to success is for the government to empower both parties to do what they do best. In particular, these activities allow the private sector to pursue profit by improving the overall performance of the supply chain.

One purpose the Air Force has for its pursuit of P3s is to take advantage of the skills and capabilities that commercial firms have developed outside the defense supply arena. For example, Standard Aero, a global engine maintenance, repair and overhaul company, was brought onto the team at the Oklahoma Air Logistics Center in large part because of its expertise in failure
analysis and parts reengineering. Similarly, Boeing supports the Air Force maintenance program for the C-17, seeking to identify defects, predict parts wear, improve parts performance and otherwise increase the number of operational aircraft. In 2001, Lockheed Martin and Warner Robins Air Logistics Center initiated an 8-year contract for maintenance of LANTIRN pods. Lockheed Martin guaranteed and delivered both a 90-percent availability of the pods and a significant cost avoidance to the Navy.

The Navy has made major strides forward in P3. Lockheed Martin and Sikorsky have teamed up on the H-60 Tip-to-Tail contract. This contract is intended to provide high availability at reduced cost. In both instances, a key to the success of these efforts has been the willingness of the organic base to alter their practices and procedures to fit with the routines established by the private sector.

The Navy and Marine Corps created a partnership between Honeywell and the Naval Depot at Cherry Point, North Carolina to repair auxiliary power units. The depot provides facilities and skilled labor and the private contractor provides parts, inventory control and management expertise. In addition, Honeywell brought Caterpillar Logistics on board because of that company’s proprietary distribution management capabilities. The depot not only allowed the private companies to make changes to its process and procedures but gave full access to its inventory control systems.

One of the largest and most complex P3s is the F-18 E/F FIRST program between the Navy and Boeing. The contractor team manages the process, provides parts, does engineering redesign to enhance availability and provides program management. The organic base provides repair services. This resulted in an improved availability from 67 percent to 85 percent along with enhanced reliability.

Finally, the activities surrounding military housing privatization offer empirical evidence to the potential success that partnerships have for the Army and other services. The National Defense Authorization Act for Fiscal Year 1996 authorized the DoD to work with the private sector to build and renovate military housing. Since then this program has obtained private capital to leverage government dollars, efficiently used the limited resources available, and used the market to offer service members better quality housing. Of importance was the ability of those in support of privatization to sway key stakeholders from their comfort zone, i.e. Congress, and show the value of allowing market forces to take shape. In the end, morale has increased, resources are expended more efficiently and the DoD has saved money.

**P3 DRIVERS**

As is the case with any business relationship, a Public-Private Partnership must meet the operational interests of both parties. In the past it was often the case that the interests of the organic base and those of the private sector did not coincide. This has now changed. The organic base has discovered the virtues of the know-how and advanced capabilities of the private sector. Similarly, the private sector has come to recognize the value of a division of labor with the organic base. Indeed, synergies have been discovered and exploited allowing the organic base to become more efficient and responsive and the private sector to increase its overall effectiveness. Objectives for DoD and industry partners, in general, align:

- Enhanced product support or product performance improvement;
- Improved business practices or technology;
• Best value in production, operations and maintenance;
• Total life-cycle systems management;
• Maximized facility utilization;
• Private investment in plant, equipment and technology development;
• Enhanced cooperation and trust among partners;
• Improved systems engineering and a smaller logistics footprint;
• Opportunities to better the warfighter;
• Leveraging public-private core competencies and best commercial practices;
• Longer term contracts, with multiyear funding and expectations for certain levels of returns on investments; and
• Viable business opportunities that return value to the shareholder.**

The DoD wants to slim down, speed up and make as effective as possible systems that support the warfighter. As draw-down occurs, resetting the Force will demand significant increases in budgeted maintenance, repair and operations to assure readiness for future combat or emergency need. Over the next 3-, 5- and 10-year outlook periods, there is only increasing demand for this approach to sustain the warfighter. To free up funds for procurement, DoD will want to achieve these objectives in the most cost effective way, i.e. through P3s and PBLs.

Additionally, the military industrial base faces a massive transformation as the labor force that supports this base begins to retire in large numbers. The organic agencies can better prepare for this through partnerships that help protect intellectual property, subject matter expertise, ensure a legacy system support capability, and train younger military employees in cutting-edge maintenance and manufacturing techniques and management.

A significant opportunity exists for “Make as Ordered” items. If depots were the source for non-current parts that are no longer stocked in commercial warehouses — the utilization of their workforce and tooling would be greatly enhanced. This would ensure industry of a source of parts for the long term and eliminate having to renegotiate each and every time a small job shop closed or was no longer supported.

In the private sector, P3 seeks to leverage advances in commercial markets such as smart products, embedded technologies for cradle-to-grave servicing, and enhanced logistics management capabilities. P3s create opportunities for longer-term relationships and longer business horizons, which is what industry seeks, especially in light of decreased government funding as the war winds down.

**THE REGULATORY AND OVERSIGHT ENVIRONMENTS**

To encourage public-private partnering throughout the organic base, various regulations and statutes exist. Chief among these is Title 10, Section 4544, which provides for Army industrial facilities to enter into cooperative activities with non-Army entities (contractors). Under these cooperative arrangements, a working-capital funded Army industrial facility may enter into a contract or other cooperative arrangement with a non-Army entity to carry out a military or commercial project. Supporting this is Title 10, Section 2474, which defines Centers of Industrial and Technical Excellence, or CITEs. Limited to depot-level maintenance and repairs, this directs the services to utilize collaborative P3s to reengineer depot maintenance activities, to adopt best practices as related to their “core competency requirements” and to test pilot
programs. Importantly, it allows for greater flexibility in work requirements allowing contractors to provide labor in core competency areas. Unfortunately, this exclusion for work performed at depots is temporary and only effective through September 30, 2009. CITEs also allows depots to lease underutilized facilities and equipment to contractors. The overall goal is to reduce total cost of ownership to the military for such industrial enterprise activities, while enhancing warfighter readiness through efficient and cost effective means. CITEs especially facilitates PBL agreements by providing greater flexibility in labor accounting. Again, this regulation applies only to depot maintenance activities to the exclusion of other P3 arenas: manufacturing arsenals, munitions plants, and research and development facilities.

While CITEs promotes P3s and PBLs, other regulations create constraints. “Core” and “50/50” work requirements can restrict the ability of depots and contractors to achieve greatest effectiveness in the ultimate goal of warfighter support. “Core” requires the military departments to own and operate a large enough depot maintenance industrial base to support the plans of the Joint Chiefs of Staff and to maintain its capability. The “50/50” rule requires that no more than 50 percent of Congressional appropriations for depot maintenance can be used for external contracting.

Other service and industry complaints lie in funding processes and policies. “Color of money” is a complaint generated from both private and public perspectives. What does it mean? Essentially, Congress stovepipes funding by budget categories, e.g. research and development funding is kept separate from production funds, which are kept separate from operations and maintenance funds. In P3 defense contracts, especially those that are performance-based, the partnership will need the freedom to do what is necessary in the fiduciary terms to meet conditions of the
contract. Under the current system, the “color of money” limits upgrades to weapons systems when they undergo standard maintenance.

For some platforms, program managers and contractors have found ways to meet performance goals despite this “color of money” constraint. Understanding how they’ve done this will better inform how funding mechanisms should be reformed to allow program managers and contractors the flexibility to meet cost-effective, performance-based standards.

There is also a general perception in the contractor community that there are inadequate incentives for government contractors and decisionmakers to push harder to achieve P3 relationships. It is nearly impossible to affect whole-scale change if individuals feel at greater risk for their job by pursuing new policies. Indeed it seems that there is lower-level management push back at command-level directives to engage in P3s and PBLs. With funding decreases and greater threats to jobs and bases, there may be an increase in this sort of resistance. Leadership needs to address this by taking on the challenge of cultural change in ways that align performance metrics with the new business practices.

Additional hurdles include inconsistent responses among and within the services, political turf battles, an adherence to adversarial positions (we/they) versus the collaborative integrative “us” of effective teams, legal and policy barriers, and issues of leadership and culture. There is tension between the competitive natures of some contracts with the collaborative goals of P3. Also, evidence of success in a P3 involving one service are not accepted as a prima facia case by another. The Navy has the C-130 APU on PBL. However, the Air Force refuses to acknowledge that a Navy program can do the job.

No doubt that Operations Enduring Freedom and Iraqi Freedom have added to the learning and, through the immediacy of warfighter need, significantly advanced P3 evolution in some programs. The Army’s Common Ground Station, the first P3 and PBL program, reported a near 99-percent operational availability in Iraq with significantly lower than historical program management costs reported at the depot level. To maintain a high level of readiness for the Common
Ground Station, the Tobyhanna Army Depot relies on a P3 with General Dynamics C4 Systems for system evolution engineering and modification projects.

The question now is where to go from here, given the consolidation that will occur in the next 3 to 5 years, in part as a result of the Base Realignment and Closure Commission, and the urgency this brings to those in charge of preserving the military organic base. Industry should examine potential business opportunities across the full sustainment spectrum, while the military needs to pay close attention to building and marketing the business case for potential partners.

ISSUES AND CHALLENGES

Public-Private Partnerships are very much in a nascent stage of development. As of April 2003, the Government Accountability Office concluded that depot P3s accounted for fewer than 2.2 percent of depot maintenance activities expenditures. As with any new and transformational initiative, there are significant issues and challenges to be addressed before P3s are a standard modus operandi. A 2003 survey of depot, arsenal and ammunition P3s by the National Defense Industry Association and the Aerospace Industries Association highlights a number of the barriers, finding that most P3s to date have been affected by “socio-political, cultural and public policy restrictions that, if not mitigated, will continue to inhibit the realization of ‘best value’ Public-Private ventures.”

The general themes of dissatisfaction on both sides include differences in opinion on objectives, enablers, impediments, metrics and results. The core tension seems to be in matching warfighter needs with business value (reduced risk, assured returns on investment) and DoD goals (sustaining organic infrastructure and productivity). Underlying challenges include issues of establishing mutual trust and respect, open communications, alignment of goals and shared purpose. In the 2003 Government Accountability Office report, a major finding was the difference in definitions of metrics for success, as well as the emphasis placed on teamwork and timeliness. Under lessons learned, industry placed significantly greater emphasis on goal setting, senior management involvement, and having the correct tools than did DoD respondents. DoD is still focused on formal, more prescriptive agreements as a means to define good partnerships while industry looks at creating common purpose and finding ways to share both risk and reward.

A key issue is the difficulty private firms have making the business case for entering into or expanding their partnerships with DoD. There is a great deal of uncertainty injected into the process. One of the clearest examples of this is the ammunition sector. Companies that win contracts to manage the GOCOs must still bid on production work. Industry complains that the time invested in designing and negotiating P3 contracts is excessive and costly, and can leave them vulnerable to loss of investment or contract income. A good example is the Lake City/Alliant Techsystems contract whereby the commander of Army Materiel Command (AMC) can terminate at will any of its agreements. To optimize their GOCO relationships, private partners will want assurances that their returns-on-investment are protected and cannot be terminated at will — subject to national security clauses written into virtually all contracts. They also seek greater use of multiyear agreements with equivalent funding predictability.

Industry is adamant that there needs to be greater predictability/stability in funding. As will be discussed below, multiyear contracts and a minimum purchase level are potential ways of achieving stability. All stakeholders recognize the importance of this goal while simultaneously recognizing its difficulty.
There is some movement in the direction of greater predictability with a new matrix system created by AMC to define the amount of expected yearly “reset.” Un-funded mandates, a baseline of repairs, etc. could be a way to create long-term contracts and the necessary conditions to appease the concerns of industry. Potentially there could be a way of legislating this “floor.”

Another important problem that must be recognized is the role of supplemental funding in supporting ongoing P3s. Supplemental funding will dry up at some point in the near future, which could result in increased competition to keep work within the organic base. Concerns regarding the depots’ continued willingness to partner with private industry will arise when money gets tighter.

And then there are the implications of the 2005 Base Realignment and Closure Commission recommendations as adopted. They transfer all depot-level repairable procurement management activities and management of all remaining consumable items to the Defense Logistics Agency. It is unclear what this will mean for depot maintenance management and the division of responsibility for programs and system platform sustainment. The Defense Logistics Agency has laid out an action plan that suggests increased ownership of the sustainment activities that are performed at these depots. P3s will succeed where there are consistent relationships among partners. The question is how the Agency will insert itself into this process. There is a major risk that this change will set the progress in P3 back. The Defense Logistics Agency faces a steep learning curve, one already successfully addressed by a number of the depots.

Some private sector sources contend that there is pushback to the expansion of P3s from lower levels within the bureaucracy. It is perceived by the private sector that the government is afraid of taking risks. Some government facilities are viewed as essentially opposed to the concept of P3s. There is also a concern among many private contractors that current interest by the depots in P3s may evaporate once there is a slowdown in the growth of defense spending.

What are the major issues and challenges to expanding the role of Public-Private Partnerships?

The Contracting Process. Contract duration is a significant problem area. The length of initial facilities contracts at GOCOs are often of insufficient duration to warrant the private concern investing much of its own money in the facilities, even though this would make the contract more profitable for the private firm and also save the government money.

Industry often expresses the opinion that its hands are tied, because the services are often enjoined by laws and regulations necessary to create a contracting and business environment conducive to private-sector investments. The government often seeks complete control of assets and footprint, which becomes an impediment for the industry to invest, modify and retool capabilities while also securing more external funding. In addition, the private sector believes that the termination clause in most government contracts can scare industry away. To be fair, the government is also concerned with the limited flexibility it would have with longer-term contracts.

The contracting process can often be long, tedious and expensive. This decreases the willingness of industry to compete when it could take 4 to 5 years to be awarded a contract. This is not only a result of the bureaucratic process, but also the turnover, change of command and lack of government personnel which results in the reworking of contracts and agreements. Several of the companies that have been part of very successful P3s said that if they had known how long it would take to get on contract they probably would not have begun the process. In addition, without adequate time to recoup capital investments, private companies are reluctant to spend their own money.
A big contracting hurdle is the failure of the contracting officer to insert language in the Request for Proposal (RFP) encouraging P3s. One possible answer is to move to the British system of letting the private sector control the logistics and sustainment processes. Another possible solution, in some instances, may be a new contracting model. One idea that has emerged is for a contractor-owned, government-operated facility. The government would rent the space, time on the machines, etc. and provide the labor. The contractor would actually own the facility, make investments in capabilities either in the interest of greater profitability or if the government provided the funding.

In essence, this could be viewed as a variant of the Army’s Armament Retooling and Manufacturing Support program. ARMS allows government-owned facilities to be used by commercial tenants. It also supports some investment in facilities. Although the government is reluctant to guarantee procurement funding, it should consider guaranteeing a return on any capital investments made by private companies in government facilities.

Another possible solution is to allow the depots to form exclusive partnerships, the same rights accorded to private industry. This will allow strategic alliances between depots and industry, permitting industry to make investments proactively, and for the depots to manage with the demands of the partnerships in mind. Under such strategic alliances, further changes in contracting could promulgate. Key to PBL is the business case analysis, indicating the best course of action for sustainment, which traditionally results in an RFP, the costly process that everyone wants to avoid. Why not use the business case analysis to establish a baseline for
requirements, and instead of an RFP issue an “Invitation to Negotiate”? The invitation to negotiate (ITN) is used when the agency determines that negotiations may be necessary for the Army to receive the best value. With strategic P3 alliances in place, and the AMC Industrial Base Office in advocacy, the Program Manager (or the originator of the business case analysis) could select one or more vendors, via an ITN, with which to commence negotiations for the procurement of commodities or contractual services.

**Funding.** A common theme in any discussion of P3s is the need for predictability/stability in funding. Multiyear contracts are one way of achieving stability. Another is a minimum purchase level. This “floor” has helped in the ammunition sector. Government representatives acknowledge the importance of stability in funding but point out the difficulties achieving this goal.

A legislative solution is needed to address the problem with using operations and maintenance money to fund product improvements as part of a PBL. One clear virtue of P3 is the incentives for the contractor to improve the products/processes in order to become more efficient and profitable.
Paragraph 2.a. of the AMC Partnership Program, dated April 21, 2006 states: “We must remove barriers to partnerships by shaping legislation, creating supportive regulations and policies, and using common business rules for evaluating partnership proposals.” Supporting this ideal, the Army can now use their Army Working Capital Funds (AWCF) to establish PBL contracts, allowing for long-term contracts. The Army could better align with industry best business practices and remove barriers to partnerships by changing Army policy to align the organic business practices with the private-sector. This is not an issue of selecting a product support integrator versus a product support provider under PBL. This is solely about funding PBL for secondary items using AWCF. To avoid any such confusion and potential mis-management of these funds, a product support activity group working capital fund could be established to identify and manage AWCF funds for PBL.

Legislative and Policy Concerns. As previously discussed, the regulatory environment has a significant impact on the ability and willingness of both parties to engage in P3s. It is crucial to take steps now in reforming acquisition policy, legislation and regulations if P3s are to become more common and useful. Legislative or policy changes are needed in order to allow for a more streamlined contracting process, flexibility of funding, more complex P3s and longer contract periods.

There needs to be recognition in legislation that the private sector may need to recoup their costs over a number of years. As a result, it is necessary that P3 arrangements provide this time. Congress is not keen to authorize and appropriate long-term, multiyear contracts because it binds their hands. However, the ARMS program has recently written some contracts for 25-year occupancy of government facilities.

The aforementioned legislative issues must be addressed, especially as they relate to operations and maintenance funding. One clear virtue of P3 is the incentives for the contractor to improve the products/processes in order to become more efficient and profitable. Perhaps some P3s — those designed to pursue performance-based goals — need to be given a special designation/exemption that would permit a broader range of industrial activities to take place under a single contract.

Lack of Education in Public-Private Partnerships. The DoD has done a great job of educating government players, e.g. courses at Defense Acquisition University, on PBLs and their value. However the same does not exist for P3s. For P3, AMC has undertaken a “road show” to educate the Program Managers and the entire AMC community. However, there is more that needs to be done; the education also needs to exist for potential industry partners. Because of uncertainties regarding the nature, purpose, value and limits of P3, both government officials and industry partners remain timid in initiating its full potential. (Army Logistics Management College is a great source that benchmarks industry and teaches these findings. It is often overlooked in the process.)

The education process should go beyond lessons learned from projects involving the government. Private industry continues to make advances in managing the supply chain in support of their commercial customers. Companies such as Maersk, UPS, Boeing, Caterpillar and C.H. Robinson are setting the standards for supply chain management in the commercial arena. When AMC, the Defense Logistics Agency or other DoD elements seek to benchmark their supply chain initiatives to a “gold standard,” that standard must include commercial practices.

In this area and in PBL, it is important to experiment. AMC needs to pursue pilot projects that test the theories about P3 and PBL. These cases need to be followed closely and documented.
However, AMC should not wait for a 100-percent solution. Successful initiatives should be modeled and tweaked while continuing to improve.

**Marketing.** There is a lack of marketing by the services for P3s and generally a lack of information explaining how industry should go about tapping these programs. Marketing should include working with the local Chamber of Commerce and other similar organizations to expand the partnerships and investment potential.

There is an erroneous impression that only the private sector can market P3s. Some depots, notably Anniston Army Depot, have aggressively sought new P3 opportunities in relatively low-margin areas such as equipment repair and painting.

It is no longer enough for the members of a particular sector — e.g. ammunition, shipbuilding, engine repair — to work with and look within its own disciplines to acquire ideas for improving performance. Instead, the services must utilize the full potential of the DoD. Army Materiel Command has aggressively surveyed the entire logistics and support community, and its leadership has visited depots and supply installations run by or for the other services. Key commercial supply chain managers have been consulted. Examples from one service can be used to encourage the contracting officers and acquisition specialists in another to be more aggressive about pursuing or allowing P3s.

**INCREASING THE LEVEL OF PUBLIC-PRIVATE PARTNERSHIPS**

The Department of Defense is interested in accelerating the number of P3s while improving P3 outcomes, making them better and smarter with enhanced value to the warfighter, industry partners and program managers. They would like to work closely with industry to understand how partnership outcomes can be improved for the private sector, to identify the barriers to improvement and to increase the number of P3s. The Army seeks more effective outreach to and feedback from partners to drive the learning curve and enhance partnership opportunities.

To achieve these goals, there are several areas that need to be addressed. Chief among these is funding. As discussed earlier, a pilot program(s) on alignment of funding regulations and practices with P3 and PBL goals would identify the ways in which program managers and contractors have addressed, or would like to see changed, funding constraints, including the “color of money.” The AMC should direct each Life Cycle Management Command to establish a Public/Private Support Strategy Integrated Product Team. These IPTs will ensure consideration, throughout support strategy design and development, of all factors and criteria necessary to achieve an optimum PBL strategy that utilizes the best capabilities of the public and private sectors in a cost effective manner. The results of the pilot program(s) would be a critical output of these IPTs, sharing better management practices throughout the Army, as well as discovering possible new funding mechanisms and considerations for regulatory changes. Through such exchanges among benchmarked facilities, a series of guidelines would be established for managing the Army Industrial Enterprise.

Making the case for P3s and for regulatory and legislative reform should be based on data that has been collected or compiled; to date this data is lacking. Acquiring that data necessitates, in turn, case studies to prove the value of P3s to Congress and any critics. Creation of a library of case studies would be valuable both within the acquisition community and among decision makers. In this way, it might be possible to identify the inhibitors and causes for successful P3s.
The AMC needs to pursue pilot projects that test the theories about P3s and PBL. These cases need to be followed closely and documented.

In this area and in PBL, it is important to establish goals that will drive success in partnerships. AMC needs to develop a plan of actions and milestones for pilot projects that test the theories set about in this paper. Under a plan of actions and milestones these cases can be followed closely and documented for the benefit of all AMC. Each Life Cycle Management Command should select two initial partnership projects, which test both public and private partners in leader and follower relationships.

In the private sector, complex, dynamic management circumstances are effectively addressed through distributed leadership models. Creating a pilot project that builds distributed leadership business capabilities at command levels would test various methods to improve P3 and PBL contract training, set consistent principles for interacting with the private sector in these new partnerships, test appropriate incentive systems for both military and contractor employees, and align risk and reward accordingly. Through exchanges among benchmarked facilities, a series of guidelines would be established for managing the defense industrial and logistics enterprise.
END NOTES

1 The Army Industrial Enterprise and Performance-Based Logistics, Lexington Institute: Arlington, VA, April 2006.
2 Ibid.
7 Ibid.
11 Ibid.
14 Public Private Partnering Survey Report.
15 With the exception of design unstable items.
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