

Competitive sourcing appears to generate personnel cost savings: In this study, the expected annual personnel cost savings ranged between 34 percent and 59 percent of baseline costs. Moreover, costs for private contractors and government MEOs did not escalate from expected levels except where observed cost increases could be attributed to expansion in mission at the installation.

The personnel cost savings we observed were achieved primarily by using fewer people and downgrading positions. Contrary to expectations, substituting capital for labor or lower wage and benefit costs did not appear to be important sources of personnel cost savings in the competitions we examined. To accomplish work with fewer people, both contractors and government managers employed a wide variety of techniques—multiskilling, organizational restructuring, civilianization, increasing labor availability, increasing labor intensity, and reducing the scope of work. Most of these personnel cost saving techniques were used by both contractors and in-house managers. This finding suggests that neither contractors nor in-house managers have an inherent advantage when reducing personnel costs.

APPLYING LESSONS LEARNED

Our finding that both contractors and in-house managers generate savings in similar ways lends encouragement to the hypothesis that the techniques used to generate labor cost savings during an A-76 competition could be applied more broadly to generate government efficiency improvements. However, we also observed that there are

strong structural incentives in place that deter managers from making such changes if they are not involved in an A-76 competition. An A-76 competition fundamentally changes the choices available to managers. Rather than comparing potentially painful reforms to the status quo, the manager must compare those reforms to the possibility of the entire function being outsourced. Competition, or more precisely the credible threat of losing everything in the competitive process, induces managers to make efficiency-enhancing changes they might otherwise resist. We conclude that comprehensive reforms, reducing the negative incentives and improving the positive incentives, would be needed to encourage DoD managers to reduce personnel costs voluntarily. In addition, training is needed to assist functional managers in identifying and implementing personnel cost savings opportunities.

TRADE-OFFS ARE INHERENT IN MANY PERSONNEL MANAGEMENT POLICIES AND PRACTICES

Management of the DoD civil service workforce is controlled by a variety of rules, regulations, policies, and practices from several entities, including Congress, OMB, OPM, OSD, and the components. Many rules are well-intended and help the entity in question achieve important goals. For example:

- The PPP reflects a commitment to current workers that might make DoD civil service more attractive to prospective workers and help maintain morale during a general downsizing.
- Veterans' hiring preferences make military service more attractive and represent a form of social payback to individuals who have made personal sacrifices to provide for the common defense of the nation.
- A centralized examining and certification process, run by OPM for most initial competitive appointments in the civil service, assures fairness and consistency in federal hiring practices.¹
- Classification policies for multiskilled positions promote comparable pay for comparable work.

¹In some cases, OPM delegates examining authority to agencies.

At the same time, many policies and procedures have important efficiency implications. These programs may introduce delays in hiring or result in the hiring of workers who are less qualified or more expensive than others in the available pool. We see no way to eliminate these trade-offs. We would like to point out, however, that such trade-offs will tend to have a more significant impact on more efficient, streamlined organizations with little or no slack resources than in other areas. In view of such consequences, it might be important to review current policies in terms of their compatibility with DoD's initiatives to create high-efficiency, high-performance organizations.

POLICY RECOMMENDATIONS

The A-76 process generates a wealth of knowledge regarding how to improve efficiency in government-run organizations. Many functional areas, particularly inherently governmental activities, could benefit from the exchange of information on cost-saving techniques. The methods through which savings are achieved could be documented and disseminated DoD-wide. However, the exchange of information is not sufficient to promote efficiency-enhancing changes.

Improving Efficiency Without Competition

Several reforms to DoD's internal management system would be required to generate personnel cost savings outside the A-76 process. First, OSD, Military Departments, and Defense Agencies need to provide more positive incentives to local commanders and managers. Local commanders and local functional managers have the detailed process knowledge required to identify opportunities for cost savings. They also face the strongest disincentives to undertake change. To improve this scenario, DoD could turn to both individual and organizational rewards. DoD performance evaluations could explicitly consider the extent to which managers have identified and implemented cost savings. Managers and their workforces also could have a real opportunity to earn performance, gainsharing, or goalsharing bonuses for their cost-saving efforts.² Additionally, organizations

²Gainsharing bonuses are sometimes used as an incentive for a workforce to reduce the costs of production. In a gainsharing plan, costs of production are periodically

might be permitted to apply a portion of savings toward other (unfunded) needs.

Functional managers at service and major command headquarters also play a key role in making operations more efficient. These managers often have a significant voice in both the design of processes used locally and in resourcing local operations. Because of these roles, headquarters functional managers may in some cases have more impact on the efficiency of local operations than local commanders and managers. Compared to local commanders and managers, headquarters functional managers are more likely to be confronted with competing demands, and therefore more likely to seek the kind of efficiencies that would stretch scarce resources so as to meet as many demands as possible. However, like local commanders and managers, headquarters staffs have little or no incentive to reduce the overall level of resourcing in their function. Thus, considering performance, gainsharing, or goalsharing bonuses for these staffs might also be useful.³

To ensure that mission support would not be inappropriately sacrificed for personal gain, any such system of incentives would require clear and measurable organizational performance benchmarks that encompass the most important organizational outputs and outcomes. These outputs and outcomes would have to be routinely measured. Additionally, legislation might be necessary to implement bonus systems that are large enough to provide the necessary incentives and can be applied equally to military and civilian members of the workforce. In devising such a system, forethought would be required to ensure that costs of the measurement and incentive systems do not exceed the expected efficiency gains.

compared to expected costs and a portion of the difference is returned to workers in the form of a bonus. When costs of production are difficult to track, as in many public-sector organizations, a variant called goalsharing is sometimes used. In this variant, bonuses are awarded to the workforce whenever an activity meets a substantial proportion of predetermined performance goals.

³Baldwin et al. (1998) discuss a related topic, namely the incentives encountered by Air Force employees at many levels of the organization to initiate A-76 competitions. They argue that the incentives facing the installation-level functional managers and commanders tend to work against A-76 efforts promoted by the major commands.

A second and more difficult task is to eliminate negative incentives inhibiting efficiency-enhancing changes. Many of these stem from long-standing DoD management practices. In the current environment, managers resist streamlining the workforce because keeping an organization fully staffed is difficult. In addition, they fear that when future budget and personnel cuts are implemented, their previous cost-cutting efforts will not be acknowledged and they will face the same across-the-board cuts as everyone else. These are real concerns for managers.

In terms of staffing, OSD, Military Departments and Defense Agencies might be able to provide a more encouraging environment for reform by streamlining staffing procedures for highly efficient organizations, exempting them from installation hiring freezes, or by giving them staffing priority in the event that a position becomes vacant during a time when there are hiring restrictions placed on installations. Such functions also might be exempted from across-the-board budget and manpower cuts for a specific period of time unless there were a change in mission or demonstrable inefficiencies in the function. Such an arrangement would require effective metrics to identify efficient and inefficient organizations. Furthermore, such metrics would have to be accessible to both installation-level commanders and higher-headquarters functional managers, since either or both might play a role in allocating arbitrary cuts.

Finally, competition-related incentives can be extended immediately and continuously to all commercial organizations by requiring them to compete on a “come as you are” basis in A-76 cost comparison competitions. Although there are some negatives associated with this approach, it warrants further study.

While providing managers with positive incentives and removing negative incentives is crucial, it is also important that front-line managers receive training and support that enable them to undertake such reforms. Our interviews suggested that civilian front-line managers, who tend to be promoted into supervisory positions through functional ranks, do not necessarily receive training in management-related skills comparable to the leadership and management training incorporated in officer and enlisted professional military education courses. Documenting and

disseminating information on cost-saving initiatives throughout DoD may be important, but these cannot replace broader training and education of functional managers.

Better Data Are Needed to Support High-Level Decisionmaking

In spite of the emphasis being placed on the A-76 process as a method to generate cost savings, the data on which high-level decisions (such as budget cuts) are currently being made have many problems. Existing estimates of savings from our case studies are hampered by a lack of guidance on calculating baseline costs and a lack of good accounting of the costs of support activities before or after the implementation of a more efficient organizational form.

DoD must improve the quality of the information to determine how much it will actually save, how much it will cost installations to perform competitions, and which activities generate the most savings. In particular, it is important to evaluate cost savings from the perspective of DoD as a whole, as opposed to narrowly defined activities subject to A-76 competition. In defining the scope of the cost analysis too narrowly, costs that are incurred outside the entity under scrutiny, yet still borne by DoD, are easily overlooked. For example, little or no information currently is available on the costs of conducting a competition or implementing A-76 results, including contract monitoring.

Ad hoc features of the A-76 process make estimating savings more difficult. For example, as of 1996, OMB has required government agencies involved in A-76 competitions to add 12 percent of direct labor costs (including fringe) to the in-house bid to reflect indirect costs, specifically operations overhead and general and administrative overhead. However, to the extent that this 12 percent overhead is viewed as a real cost that must be included in the cost comparison competition, we would argue that it should also be included when calculating the costs of the baseline organization and the cost of monitoring the contract. This 12 percent rate is completely arbitrary and does not appear to reflect the extent to which overhead costs actually vary with the number of personnel employed.

Consistent, high-quality information on cost savings and other outcomes of the A-76 process will allow OSD, Military Departments, and Defense Agencies to make better decisions about the future implementation of the process—the kinds of savings that can be expected, the time frame during which they can be expected, and the activities that should be targeted. Better information requires precise definitions of terms like *baseline cost* and *cost savings* that are consistent across installations and services. In addition, the government must gather information on the cost of conducting the competitions and continue to collect cost information during the implementation phase of the contract or MEO. In late 1999, the Deputy Under Secretary of Defense for Installations issued new CAMIS procedural guidance that addressed many of these issues (Yim, 1999).

New Approaches to Managing the MEO

OSD, Military Departments, and Defense Agencies also should think about the procedures in place for managing MEOs. It is telling that none of the managers of MEO wins could provide us with cost information—only personnel authorization information. During the A-76 process, the organization is treated like a separate entity and asked to develop a most efficient organizational form—an entity that can provide a specified level of service at the lowest possible cost. However, once the competition is over, no system exists to monitor these organizations and their fulfillment of the MEO. Managers should be given tools to monitor and manage their costs, freedom from additional constraints on the number of personnel authorizations, and other abilities. Similarly, DoD should consider giving MEO managers more control over the staffing of their organizations: The use of the PPP could be expedited for MEOs, and they could be exempt from on-base hiring restrictions for some period after implementation.