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PRIVATIZING THE DEFENSE FINANCE AND ACCOUNTING SERVICE

BY

MR. DALE LYNN

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U.S. ARMY WAR COLLEGE, CARLISLE BARRACKS, PA 17013-5050
Privatizing the Defense Finance and Accounting Service

by

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The end of the Cold War has brought with it a dramatic decline in overall United States defense spending and a sharp decrease in funding for force modernization. This trend cannot continue without serious negative impacts on readiness. The DoD has identified a need to increase investment on modernization from the current $45 billion a year to $60 billion by fiscal year 2001. Privatizing non-core missions offers one possible way for the Department to obtain funds for this purpose. This paper examines the possibility of accruing savings through the privatization of Defense Finance and Accounting Service (DFAS) functions. The paper concludes that, while privatization will eventually provide significant savings, the department must take action to first streamline DFAS operations and requirements before outsourcing will provide a viable means of reducing operational costs.
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PRIVATIZING THE DEFENSE FINANCE AND ACCOUNTING SERVICE

THE CHALLENGE

The Department of Defense is currently conducting a much-needed search for a means to increase modernization funding. The funding accounts that constitute modernization and procurement have been slashed by over fifty percent over the last ten years in order to make up for shortfalls in the Services’ operations and maintenance accounts. While the reduction in procurement accounts was necessary to maintain training and fund involvement in numerous military operations, the impact on the department’s ability to field new systems has been enormous. A stated goal of the Department of Defense is to increase spending on weapon systems from $45 billion a year to $60 billion per year by the year 2001.¹ In the current budget environment, this increase will not come from Congress, but must come from within the department’s current budget levels.

The revolution in business affairs (RBA) provides one possible approach for capturing at least part of the needed cost savings. Just as private sector corporations were forced to reexamine their core missions during the 1980’s, the DOD must now follow suit. The Commission on Roles and Missions, the Defense Science Board Task Force on Outsourcing, the Quadrennial Defense Review, and the Defense Reform Initiative have all identified parts of the financial management function as an example of non-
core activities for the Department of Defense that could be performed by private industry.

This paper pursues this idea and takes a hard look at the possibility of privatizing defense finance and accounting functions. Outsourcing these functions holds the possibility for significant cost savings while improving service to the customer. It is the position of this paper that, regardless of the outcome of outsourcing studies, DOD should at least explore this possibility.

SETTING THE STAGE

The post-Cold War era is well upon us. The euphoria over the fall of the Berlin Wall is gone, and the reality of international relations without the constancy of an implacable known enemy has set in. It is no news to the military departments that the collapse of the Soviet Union and the Warsaw Pact has brought mixed blessings. While the omnipresent threat of nuclear annihilation has receded, the stability of a bipolar world has also disappeared. At the same time that the United States has embarked upon its usual post-war reduction in military spending, the number of military operations has increased. To balance this equation, the Service's have repeatedly underfunded the modernization accounts in favor of operations and maintenance. Figure 1 provides the trend line procurement spending since 1951. Since the mid-1980's, all Service's have experienced over 50 percent reductions in procurement total
obligating authority. The situation is more critical than it may first appear. While the constant dollar amount is roughly the same as it was during the 1960’s, the high technology weapons of today are infinitely more expensive than they were at any other time in history. For example, the current price tag for a new F-15E is approximately $46 million. The projected cost of its replacement, the F-22, is estimated to cost $160 million.

Similarly, The AH-64 Apache helicopter costs around $17 million while the new RAH-66 Comanche is projected to cost $35 million per copy. This same cost escalation is prevalent across all major weapons systems.

**PROCUREMENT BY SERVICE**

**CONSTANT FY1998 DOLLARS**

![Graph showing procurement by service from 1950 to 1995.](image)

**FISCAL YEAR**

Figure 1 - Procurement by Service
Both the Quadrennial Defense Review (QDR) and the Defense Review Panel reports agree that the department must increase its modernization efforts or face fighting a future war with obsolete equipment. The reports also concur on a goal of $60 billion per year by the year 2001 as the appropriate level to maintain a viable modernization program.

The department has turned to the revolution in business affairs (RBA) as a major approach for finding the cost savings necessary to increase modernization funding. The RBA, as cited in the QDR includes:

Reducing overhead and streamlining infrastructure; taking maximum advantage of acquisition reform; outsourcing and privatizing a wide range of support activities when the necessary competitive conditions exist; leveraging commercial technology, dual-use technology, and open systems; reducing unneeded standards and specifications; utilizing integrated process and product development; and increasing cooperative development programs with allies.\(^7\)

Outsourcing and privatization, besides being viable when necessary conditions exist, are appropriate for those functions that are not inherently governmental and are considered non-core missions. The key to this effort is the identification of core and non-core missions. The QDR\(^8\) and the National Defense Panel\(^9\) both identified major portions of finance accounting as non-core missions and therefore subject to outsourcing or privatization. But what does this mean for the department and for the Army?

To reach an answer to this question, we must examine the concepts of outsourcing and privatization, the conditions that
contribute to high current defense finance and accounting costs, and the prospects for privatization of finance and accounting functions. Before we go too far, however, a brief discussion of the history and structure of the Defense Finance and Accounting Service will be useful to appreciate the size and complexity of this organization.

THE DEFENSE FINANCE AND ACCOUNTING SERVICE (DFAS)

Prior to 1991, all the Services owned and operated a finance and accounting service. In 1990, the department issued a number of Defense Management Review Decisions (DMRD). The purpose of these decisions was to achieve major cost savings through cancellation of programs and creation of defense agencies that would consolidate and reduce overall department costs. One such decision was DMRD 910. This DMRD established the Defense Finance and Accounting Service (DFAS) as the defense agency responsible for providing finance and accounting functions to all the Services. In addition, the DMRD changed the funding source for DFAS. In an effort to gain cost visibility and then create incentives for cost reductions and greater efficiencies, DFAS was created as a revolving account funded activity. In other words, DFAS does not receive an annual appropriation. Instead, it charges its customers — the Services — for each transaction it performs. In an open, competitive system the Services would be able to shift their business elsewhere if DFAS did not provide adequate service at a reasonable price. This, in turn, would
provide economic pressure on DFAS to reduce unit costs. Unfortunately, due to current DOD policy, the Services cannot take their business elsewhere and are forced to pay whatever cost DFAS management determines is needed to cover operating costs.

In December 1992, DFAS assumed responsibility for 332 installation finance and accounting offices and began consolidating operations. The consolidation process was aggressively pursued and has been extremely successful in reducing the number of operating locations. By the end of fiscal year 1998, "DFAS will consist of a headquarters in Arlington VA, with five centers located in Cleveland, Ohio; Columbus, Ohio; Denver, Colo.; Indianapolis, Ind.; and Kansas City, Mo., and 17 OPLOCs (operating locations) located nationwide."\(^{10}\)

The DFAS is big business. It processes a "monthly average of 9.8 million payments to DOD personnel; 830,000 commercial invoices; 730,000 travel vouchers/settlements; 550,000 savings bonds issuances; and 200,000 transportation bills of lading. The agency's monthly disbursements total approximately $22 billion."\(^{11}\) To perform these functions in FY97, DFAS employed 22,000 personnel and charged the Services nearly $1.8 billion just for the finance side of operations.\(^{12}\) It has long been the contention of the Services that the DFAS bill is too high. A comparison with private industry tends to support this claim. Private industry pays approximately 1.5 percent for financial services. The Services pay around 3 percent or roughly twice as
much. The DFAS management has recognized the need to reduce costs and has taken numerous steps in this direction. At the same time, Congress has noted the need to trim the size of government and to take advantage of the private sector trends. Accordingly, the Defense Authorizations Act for Fiscal Year 1995, Section 352 directed the Secretary of Defense to submit a plan for private-sector performance of civilian payroll. The same act (section 353) directed a pilot program to privatize finance and accounting for defense non-appropriated funds (NAF).\textsuperscript{14}

Privatization would certainly reduce the number of DFAS personnel. The real issue is whether outsourcing or privatization of DFAS functions is feasible and if privatization can produce dollar savings significant enough to materially contribute to the increase in modernization funding both Congress and the department are seeking.

Throughout this paper, the terms outsourcing and privatization are used interchangeably. There are, however, distinctions between the two terms. Outsourcing is generically used to indicate shifting a function from in-house operation to an outside service provider. For the government this can mean transferring a function to another government agency or to a commercial firm. Privatization is usually considered a subset of outsourcing that transfers a function to the commercial sector.
OUTSOURCING/PRIVATIZATION

The practice of outsourcing non-core functions was widely adopted by private industry during the recession of the late 1980's. Under the stress of international competition, private industry went through major reorganizations and 'downsizing.' Companies in all sectors of the economy, from Boeing, Kodak, to IBM sought to reduce their infrastructure and focus on core business competencies. Tools for accomplishing these reductions included plant closures, elimination of middle management and outsourcing of functions. Functions most frequently outsourced included information technology (28%), transportation management (21%), human resource management (12%), and financial management (6%). The concept is that all of these functions can be provided with better results and at lower cost by outside firms that specialize in them. In order to analyze whether privatization of DFAS is an appropriate strategy for the Department of Defense, we need to understand why and under what circumstances private industry outsources functions.

Private Industry Outsourcing.

According to the Outsourcing Institute, the top ten reasons that the private sector outsources functions are:

1. To make capital funds available.
2. To create a cash infusion.
3. To reduce and control operating costs.
4. When resources are not available internally.
5. The function is too difficult to manage or is out of control.
6. To improve company focus.
7. To access world class capabilities.
8. To share risks.
9. To accelerate reengineering benefits.
10. Free resources for other purposes.¹⁶

While items such as numbers 1 and 2 (gain capital funds and cash infusion, respectively) clearly do not apply to the DoD, it is evident that many of the same reasons that drive private industry to outsource functions are applicable to the department. If nothing else, the department is anxious to free resources for other purposes.

Before private industry can outsource a function, however, three conditions must exist.

1. Capability outside the company to perform the function,
2. A competitive commercial market, and
3. A best value opportunity that reduces cost while maintaining or improving services.¹⁷

The same conditions must exist for governmental functions to be outsourced. Whether these conditions exist for DFAS services will be discussed later in this paper.

THE HIGH COST OF DFAS OPERATIONS

The idea of outsourcing government functions is not new. The Office of Management and Budget (OMB) Circular A-76, which provides guidance for conducting outsourcing studies, has been in existence since 1955. Beginning in the late 1970's, the Defense Department regularly conducted A-76 studies and outsourced functions at numerous military installations. Today, the Services regularly contract for base operations support for
deployed forces. "Since F 83, the Army completed 331 A-76 cost competitions covering over 20,000 manpower positions."^{18}

In a very real sense, however, through the creation of DFAS the Services have already outsourced the finance and accounting function. The real question is whether the department should now privatize and totally divest itself of these functions. Whether the functions are privatized or not, taking a hard look at outsourcing the finance and accounting functions will result in trimming in-house operations and a close examination of our processes and requirements. Recent history supports this position. Over the last three years, DFAS has studied five areas for outsourcing and is scheduled to study five more (see Table 1).^{19}

<table>
<thead>
<tr>
<th>STUDY</th>
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<th>END</th>
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<tbody>
<tr>
<td>A-76 Debt &amp; Claims Mgt</td>
<td>Mar 95</td>
<td>May 96</td>
</tr>
<tr>
<td>Fac, Log, Admin</td>
<td>Mar 95</td>
<td>May 97</td>
</tr>
<tr>
<td>DeCA Vendor Pay</td>
<td>Nov 95</td>
<td>Sep 97</td>
</tr>
<tr>
<td>DeCA Acctg</td>
<td>Jul 97</td>
<td>Jul 99</td>
</tr>
<tr>
<td>Depot Maint Acctg</td>
<td>Feb 97</td>
<td>Jan 99</td>
</tr>
<tr>
<td>Trans Acctg</td>
<td>Mar 97</td>
<td>Feb 99</td>
</tr>
<tr>
<td>Congress Directed</td>
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<td></td>
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<tr>
<td>Civilian Payroll</td>
<td>Feb 96</td>
<td>Oct 96</td>
</tr>
<tr>
<td>NAF Payroll</td>
<td>Feb 96</td>
<td>Oct 98</td>
</tr>
<tr>
<td>NAF Acctg</td>
<td>Apr 97</td>
<td>Apr 99</td>
</tr>
<tr>
<td>DFAS Initiated</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Information Svcs</td>
<td>Sep 96</td>
<td>Sep 97</td>
</tr>
</tbody>
</table>

Table 1 - DFAS Privatization Schedule
Of the five completed studies, none resulted in outsourcing of the function. The savings that resulted from the threat of competition, however, were very impressive. Over 400 positions were eliminated and $8 million annual savings are being realized. In fact, the government bid for the functions was an average of 23 percent lower than bids submitted by private industry. If this is the case, why is the DFAS bill to the Services so much higher than the industry norm? The answer can be found in three factors:

1. The complexity and number of legacy systems DFAS inherited from the Services.

2. The difficulty and time required to consolidate and streamline an organization as large as the Department of Defense.

3. Requirements demanded by the customer.

Legacy Systems.

Establishing DFAS did not magically create one system for department finance and accounting. In reality, DFAS inherited 324 separate finance and accounting systems (197 accounting and 127 finance). Over time, all the Services had developed their own systems, none of which was compatible with any of the others. Maintaining all of the separate systems adds considerable cost to the DFAS operations. It also drives up bids from commercial vendors in the outsourcing process. While DFAS has made major strides towards consolidating systems, it has a long way to go.
As of 1996, DFAS had eliminated 107 systems and is working towards trimming the total number of systems down to 32 (23 accounting and 9 finance) by fiscal year 2003.21 Table 2 provides the DFAS schedule for elimination of finance systems and Table 3 shows the reduction in accounting systems. Until such time as DFAS can migrate from these numerous old systems, the costs to the Services will be higher than it should be. A plethora of systems not only requires fragmented operations and increased maintenance costs, it also means that data is being entered into systems more than once. This leads to higher error rates and increased personnel costs to correct the errors.

<table>
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<th></th>
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<tbody>
<tr>
<td>Military Pay</td>
<td>32</td>
<td>13</td>
<td>2</td>
<td>2</td>
</tr>
<tr>
<td>Civilian Pay*</td>
<td>27</td>
<td>10</td>
<td>1</td>
<td>1</td>
</tr>
<tr>
<td>Contract/Vendor Pay</td>
<td>10</td>
<td>7</td>
<td>6</td>
<td>1</td>
</tr>
<tr>
<td>Travel/Transportation</td>
<td>8</td>
<td>7</td>
<td>4</td>
<td>2</td>
</tr>
<tr>
<td>Disbursing</td>
<td>6</td>
<td>7</td>
<td>1</td>
<td>1</td>
</tr>
<tr>
<td>Retired/Annuitant Pay</td>
<td>5</td>
<td>1</td>
<td>1</td>
<td>1</td>
</tr>
<tr>
<td>Debt Management</td>
<td>2</td>
<td>1</td>
<td>1</td>
<td>1</td>
</tr>
</tbody>
</table>

| Total                  | 90     | 46     | 16     | 0**    |

* Does not include foreign national payroll systems

Table 2 - Reduction in Finance Systems
Table 3 - Reduction in Accounting Systems

Streamlining Operations.

As was noted earlier, when DFAS was established it inherited 332 different branch operations and associated manpower. In conjunction with the overwhelming number of separate systems that DFAS must operate, the large number of locations and personnel necessarily leads to less than optimal cost performance. In addition, establishing DFAS itself created a new headquarters whose costs are part of the overall bill to the customer. Over the last seven years, DFAS has not only reduced the number of finance and accounting systems; it has greatly reduced its number of offices and personnel. Since its inception, DFAS has eliminated over 9,000 positions. Streamlining has also taken place in operations and processes. As Figure 3 illustrates, DFAS has great plans for reducing personnel over the next several years.

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<tr>
<td>Working Capital</td>
<td>93</td>
<td>73</td>
<td>34</td>
<td>15</td>
</tr>
<tr>
<td>General Funds</td>
<td>64</td>
<td>40</td>
<td>17</td>
<td>3</td>
</tr>
<tr>
<td>Security Assistance</td>
<td>9</td>
<td>9</td>
<td>4</td>
<td>1</td>
</tr>
<tr>
<td>Non-Appropriated</td>
<td>8</td>
<td>7</td>
<td>7</td>
<td>1</td>
</tr>
<tr>
<td>Other</td>
<td>23</td>
<td>21</td>
<td>5</td>
<td>3</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>197</strong></td>
<td><strong>150</strong></td>
<td><strong>67</strong></td>
<td><strong>23</strong></td>
</tr>
</tbody>
</table>
years...to include outsourcing of functions. As these planned for reductions are realized, the DFAS bill will necessarily decline. This leaves one last key factor in keeping the DFAS bill high — customer demands.

FY 1993 - FY 2003

48% Manpower Reduction

Figure 2 - DFAS Manpower Reductions

Customer Demands.

Since the Services have already (although not willingly) "outsourced" their finance and accounting functions, there is already a customer—service provider relationship that the Services can control to a greater extent than the Services may recognize. Mr. Ernest Gregory, Deputy Assistant Secretary of the Army (Financial Management and Comptroller) for Financial Operations, strongly believes that the Services are often their
own worst enemy for increasing DFAS costs.\textsuperscript{23} He uses the IMPAC card as a telling example. This card allows authorized holders to make purchases up to $2,500 without the requirement for the normal procurement forms. The IMPAC card greatly reduces procurement lead time for small purchases, but the DFAS accounting bill to the Army was astronomical. After some investigation it was found that the Army (and the other Services as well) required DFAS to provide a separate breakout of every IMPAC purchase by element of expense line item accountability. This meant that every purchase on an IMPAC card cost the Army $23.92 — and one card billing could have hundreds of purchases over the course of a billing cycle. It was determined that the Army didn’t really need this level of detail, and the requirement was changed so that each bill contains one summarized line for each EOR. This reduced the cost per card billing statement to $20. By implementing this change department-wide, DFAS will be able to eliminate 2,200 personnel and their associated costs.

Another example is the travel voucher settlement process. The Under Secretary of Defense (Comptroller) and the General Accounting Office set the requirements for this process, not DFAS. Through the efforts of the DOD Travel Reengineering Office, the department is attempting to simplify and streamline the travel voucher process and make it more closely resemble private industry norms. The key here is that DFAS cannot do this unilaterally. They are merely the service provider, and we tell
them what to do. Until we the customer change the requirements, the DFAS bill will always be high in comparison to private industry.

The impact of the three areas discussed above — legacy systems, inherited organizational structure, and customer demands — all conspire to drive DFAS charges higher than private industry norms. They also tend to make efforts to privatize DFAS functions more difficult. Commercial vendors are confused by the complexity of our systems and requirements and are sometimes overwhelmed by the magnitude of the operations we are attempting to privatize. The next section examines these points.

PRIVATIZING DFAS

The pressure to reduce the size of the government "footprint" and to realize cost savings to apply to force modernization virtually ensures that studies will continue to be conducted and that some functions will be outsourced. In fact, DFAS currently outsources 10 percent of its workload to private sector businesses and another 23 percent to other government agencies.24 And, although DFAS has never lost an A-76 competition, the agency anticipates saving over $30 million and 455 work years through currently planned commercial activity studies. Privatization studies will be a constant for DFAS for the foreseeable future.

As was stated earlier, there are three basic conditions which must exist before a function can be outsourced. Let’s examine each one and how well they apply to various DFAS functions.
Private Industry Capability.

On the surface, there would seem to be little doubt that private firms have the capability to perform virtually any defense finance and accounting function. After all, payroll is payroll, vendor payment is vendor payment. Conceptually there should be no argument, but in practice the issue is not so simple. The reality is that DFAS is the largest finance and accounting operation in the world. DFAS financial operations are larger than the combined annual sales of over half of the Fortune 500 companies. DFAS handles more funds than over three times the revenue of Exxon’s and 20 times that of Coca-Cola. In recognition of the sheer size of DFAS operations, there has never been an attempt to look at contracting out the entire operation. Rather, designated functions such as civilian payroll or travel pay are typically studied for possible privatization. Even then the magnitude of operations is staggering. For example:

Civilian Pay.

DFAS pays 2.2 million civilian personnel every payroll cycle. By comparison, General Motors pays 708,000 and Lockheed Martin pays 190,000 employees. The difference is significant in its affect on systems requirements. The reality is that even the largest payroll service providers would be hard pressed or incapable of performing this function. When, in the course of reviewing civilian payroll, DFAS approached private industry to determine interest in competing, the resulting cost estimates
submitted were significantly higher than DFAS bill. In attempting to ascertain why, the common answer was that the system for paying civilians was too large and too complicated. In addition, unlike most private corporations, DOD does not have an integrated personnel and payroll system. That is, whenever a change occurs to an employee's status — hiring, promotion, pay increase, cash awards, etc. — the action must be annotated in both the personnel system and in the financial system. In private industry, the norm is for the action to be entered once in the personnel office and for the change to flow directly to the payroll system. The department recognizes the need to create a single entry personnel/payroll system, but progress toward this goal has been slow, and there is no projected fielding date for such a system.

Military Pay.

DFAS pays 2.6 million military personnel every month. The average mid-level officer receives: base pay, housing allowance, and has allotment distributions to the Combined Federal Campaign and to savings bonds. Send this officer to Bosnia and he or she also receives a variety of deployment bonuses, Carry over leave, and deployed per diem. By comparison, the average mid-level private sector executive only receives base pay. Again, the differences in quantity and complexity are extreme. In fact,
there is no assurance that there is a private sector corporation currently capable of accomplishing these functions.

A possible solution for solving this problem would be to divide functions such as civilian pay into regional pieces and compete them separately. A similar approach is being pursued by the DOD Travel Reengineering Office for issuance of airline tickets and settlement of travel vouchers. The travel reengineering Office plans to divide the country into ten regions and compete each one separately. The difficulty with this concept is that it has the potential for producing ten incompatible software systems that will create the same type of long term problems that plague many of our legacy systems.

In the travel arena, it is possible that regionalization, and the associated risk of systems fragmentation may work. After all, most temporary duty travel (TDY) is short-term and personnel will only deal with one region for a given TDY trip. The same can not be said for many other DFAS functions to include travel pay for permanent change of station moves. For these other functions, regionalization does not appear to be a viable alternative. In any event, it would be naive or arrogant on our part to believe that private industry is incapable of performing DFAS functions without reducing the scope of the operation.

**Competitive Commercial Market.**

To have a competitive market, there must be at least two, and preferably more, private entities interested and capable of
performing the function in question. A competitive market does exist for both finance and accounting functions. There is no lack of financial institutions that could conceivably take on the DFAS workload. From City Bank and Chase Manhattan to Arthur Anderson and Peat Marwick, both finance and accounting firms exist. It is the existence of commercial sources for finance and accounting functions that has led Congress to direct privatization studies. The dilemma, as noted above, is whether they have the capability to perform the functions as they are currently structured. The challenge for the department is to reengineer our internal systems to the point that our processes begin to resemble commercial practices.

Best Value Opportunity.

Whenever DFAS has performed an A-76 study private industry has responded. As noted earlier, however, the bids have not been competitive. The best value opportunity in all cases has been for continued in-house performance. While complexity and magnitude of operations have some bearing on this, another factor is the way the government contracts for services.

Any commercial firm that picked up a DFAS function would be faced with an enormous undertaking to establish the infrastructure necessary to meet contract requirements. Many firms are simply not willing to invest the upfront costs necessary to be competitive. An example of this occurred recently.
In response to congressional direction, DFAS has been actively pursuing privatization of non-appropriated fund (NAF) accounting. The DFAS only operates Army NAF accounting and payroll. The other Services still maintain their own systems. This is scheduled to change, and DFAS will assume all NAF accounting over the next two years. Regardless, during FY97, the Army generated over $800 million in NAF revenue. Congressional direction was to conduct a pilot program to ascertain whether privatization of NAF could save both NAF and APF. DFAS canceled the review this Fall when the commercial vendors that had originally expressed interest in bidding on the contract stated that they were unwilling to invest in establishing operations for a pilot program. While Army NAF uses accrual rather than cash accounting, it is familiar to, and used by some portions of private industry. Accordingly, commercial off the shelf (COTS) software is available that, with some modification, could handle Army NAF accounting. The uncertainty involved with a pilot program, however, was too much risk for the interested bidders.

If this condition exists for a rather straightforward operation like NAF accounting, it is reasonable to assume that it also exists for the more formidable APF functions. According to Mr. Redding, DFAS Outsourcing, Privatization and Commercial Activities program manager, this is exactly what occurred when DFAS originally studied civilian payroll. Interested contractors were extremely weary of investing in the required upfront
physical and information technology infrastructure just for a one-year contract with four option years. The start-up costs for a short-term contract are simply too high.  

Lessons learned from private industry indicate that one of the most important keys to successful outsourcing is establishment of a close, long-term relationship with the service provider. The wisdom of this suggestion has been realized by the defense acquisition community and can be seen in the prime vendor program. To ultimately obtain the best value from private industry in contracting out DFAS functions, the department may need to consider establishing contract vehicles that allow for 10 or 15-year contracts.

CONCLUSIONS

After years of dramatic decline in top-line resourcing, the Department of Defense can now be reasonably assured of a relatively constant yearly funding of $250 billion. Continued strong national economic performance and the first budget surplus in several decades will not increase this funding. For the department to increase its force modernization expenditures, reductions must be found or forced elsewhere. Private industry experience shows a road map for finding at least part of the needed savings. While privatization of non-core missions is not a panacea, it can be part of the overall strategy for reducing department operating costs. As all of the recent reviews of the department, from Congress to the Defense Science Board, have
recommended, department finance and accounting are two of several non-core missions that should be considered for privatization. Until such time that department finance and accounting functions, systems, and organization are reengineered, however, the prospects for successfully privatizing major portions of the DFAS mission are not good.

This does not mean that the effort should be abandoned. Privatization of DFAS functions must be pursued. The pressure it places on the agency to continue to reengineer operations and systems is crucial to future improvements in efficiency and service. As Alice Maroni, Principal Deputy Under Secretary of Defense (Comptroller) stated in recent remarks to the Defense Agencies Comptrollers Conference, Wintergreen, Va., "Sometimes, of course, the only way to get a process changed is first to cut the resources allocated to that process. Only then can we sort out what actions are really essential."\textsuperscript{31} This applies both to DFAS and to the Services. The Services must rationalize the requirements for information they place on DFAS, and they must be willing to part with the comfort of their familiar but obsolete legacy systems.

Privatization reviews of DFAS functions will continue. Realistically, however, current opportunities for large-scale success in outsourcing are slim. This does not mean that outsourcing will not be viable in the future. To arrive at a point where this will be possible, DFAS, like the rest of the
department, must look to reengineering, reorganization, and restructuring to reduce costs. (5,453)
ENDNOTES


5 Nicholas, 2-2.

6 Thompson, 52.

7 Cohen, 15.

8 Cohen, 55.


11 Ibid.


15 Carnes, 18.

16 Outsourcing Institute. “Redefining The Corporation: Bringing Order to a New Industry,” available from
Carnes, 8.


Ibid, 6.

Ibid, 22.


Ibid, 29.

Gregory interview.


Carnes, 25.

Carnes, 35.

It should be noted, however, that contrary to DFAS assertions, an outsourcing study was never actually conducted. When DFAS saw the cost estimates submitted by private industry, the study was called off. DFAS, under congressional pressure, announced on 30 December 1997 that they will now conduct an A-76 study of civilian payroll this fiscal year. It will be interesting to follow this study to see if private industry will submit competitive bids.

Carnes, 24.


Ibid

BIBLIOGRAPHY


