

FAX Cover Sheet

703-699-2735

FROM Gary Amundson

TO FRANK Cirillo or Bob Cook or Gary Dinsick

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MESSAGE Please consider the attached in your final

recommending to the Commissioners. It concerns

SAS JCSC recommendation 003SR.

Thank you —



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23 August 2005

TO: 2005 Defense Base Realignment and Closure (BRAC) Commission; ATTN: Mr. Frank Cirillo; Mr. Bob Cook and Mr. Gary Dinsick; 2521 South Clark Street, Suite 600; Arlington, VA 22202

SUBJECT: Supply and Storage (S&S) Joint Cross Service Group (JCSG) Scenario 0035R

Dear Mr. Cirillo, Mr. Cook and Mr. Dinsick,

I am writing in regard to the S&S JCSG recommendation covered by scenario 0035R which addresses three principal areas: Defense Logistics Agency (DLA) management of remaining military-service managed consumable items; consolidation of procurement and related functions for Dcpot Level Repairables (DLRs) with DLA; and movement of three Army ICP sites and one Air Force ICP site to other Army and Air Force ICPs. I believe that the BRAC commission staff should recommend to the commissioners that this recommendation not be accepted for the following reasons: (1) There is an existing process that could handle the consumable/DLR portion of the recommendations if these portions are deemed of potential value; (2) the savings assumptions (which are the chief rationale) on the DLR portion of the recommendation are very questionable; and (3) the ICP movement portions of the recommendation were added late in the development of this scenario without sufficient S&S JCSG study with the result that they result in no cost savings and in some cases do not meet the stated rationale for movement. I will discuss these three points in order below:

- (1) **Use of BRAC vs existing processes.** In the 1980s and 1990s, DOD transferred approximately 1 million consumable items from the military services to DLA. This was not done via the BRAC route, but rather through an established method in the Department's resource allocation and budgeting process. A series of Program Budget Decisions (PBDs) and Defense Management Review Decisions (DMRDs) were used to propose, gather comment, direct, and implement what became known as the consumable item transfer. Rather than directing a very time line oriented and relatively inflexible process such as BRAC to assess the time to transfer the remaining consumable items, why not use a process that has been used very successfully in the past? DLRs have also been subject to the same process as, for the Army at least, it was a DMRD that directed the stock funding (procurement via working capital funds rather than procurement appropriations) of Army managed DLRs in the early 1990s. The PBD/DMRD approach allows for more flexibility and allows for the use of pilot projects to ensure that the initiative proposed can be tested and, if need be, scaled back or modified. It would be much more difficult to do this under a BRAC process. This is no doubt one reason why a senior Army leader, the head of the PA&E office in the 5 Apr 05, BRAC SRG minutes for meeting 37 (5 Apr 05) noted: "...that, if this action is done inside BRAC and therefore became law, then it would be very difficult to undo the DLR piece if it didn't work out. He strongly suggested adopting the

position that the DLR portion be worked outside of BRAC.” Note that the suggestion here is not that the proposals relating to consumables and DLRs have no merit, but that there is an existing process by which they could be implemented in a more flexible manner. Furthermore, the chairman of the S&S JCSG in his testimony to the BRAC commission on May 18, 2005 noted that there would still need to be a negotiation process with the services “because there are some items that, as an example, are design unstable, that are better left with the services, from a technical perspective...In terms of the depot-level reparable, it’ll be the same negotiation between DLA and the services about what items should be part of this process...” In other words, even though 0035R calls for “ALL” remaining consumables to be transferred, the chairman of the S&S JCSG indicates that a negotiating process will be needed. This is exactly what happens today under the various PBDs and DMRDs that DOD issues. These recommendations do not have to be implemented via BRAC rules/restrictions and in fact if they do have merit, they would be better served by that more flexible process and not by a BRAC action. It appears that the DLR and consumable portions of this recommendation were driven more by transformation concepts than by the eight BRAC criteria. It is difficult to understand why the BRAC process should be used to transform a management process when an established process is already in place by which this could be more flexibly done if the ideas have sufficient merit to go through the PBD/DRMD process.

(2) Savings assumptions on the DLR procurement section of the recommendation. The use of performance based agreements (PBAs) is highlighted in the supporting rationale for 0035R as the chief means by which savings will be achieved. A review of the S&S JCSG minutes and the Army SRG minutes shows that this premise was questioned quite intensely by most of the military services. The idea of splitting the management of DLRs appears to be counter-productive, especially if the savings estimates are questionable. The S&S JCSG believes savings will come from three areas: inventory reduction, cost to hold avoidance, and pricing savings. Several comments need to be made:

(a). The one-time savings in inventory reduction should only be counted against the average on hand level (defined as the safety level plus ½ the operating level). There is no reason to assume a decrease in the operating level, so the only savings in the one-time costs are in a reduction to safety level. This amount would certainly be far less than the analysis used to support the recommendation proposals.

(b) It appears that there is a double counting of the on hand investment savings. Actual investment cost is the holding cost, not the acquisition cost of the inventory since the holding cost is a portion of the acquisition cost. To count both of these numbers is incorrect and overstates savings.

(c) The treasury bond yield doesn’t appear to be correct. OMB guidance is that the short-term real rate, not the long term government securities rate should be used.

Currently the short-term real rate is approximately 1%, a percentage far lower than the 4.5% that the analysis used.

(d) Only one aspect of the increased use of direct vendor delivery (DVD) contracts was considered. If less holding costs are assumed, then the increased administrative costs associated with DVD type contracts must also be addressed. This means that there is more frequent purchasing using a lower marginal cost but with a higher fixed cost of negotiating a DVD contract. As DVDs are used more extensively, the cost of them increases to the point where the holding cost savings and the marginal administrative costs are approximately equal. There is a risk of negating any savings associated with DVDs that should be considered in any analysis of increased use of DVD contracts.

(e) Obsolescence risk is confused with excess inventory in the analysis. These terms are not synonymous in terms of the holding cost equation. An independent look should be given to this calculation.

(f) The shifting of the costs of holding inventory from the government to the contractor is simply cost shifting not real elimination of risk. This must be balanced against some of the potential downsides of increased use of DVDs (longer customer wait times etc).

(g) In earlier versions of scenario 0035 when complete DLR management (not just the procurement piece) was being considered, the models that the S&S JCSG ran indicated that only 8% of the dollar value of DLRs represented common items used by more than one service. How will the increased buying power, which presumably means the consolidation of larger quantities into a single buy, generate large savings when for 92% of the dollar value there will simply be a change in who is buying the item at the same quantity? This is never addressed in the justification and brings up an overarching point in this area. DLRs are much more like the end items that they support than they are like consumable items. How are we to know that the procurement patterns and projected savings will be similar to that experienced for consumable items? This is another reason to pursue this option through the PBD/DRMD process so that some independent analysis of projected savings, some flexibility and perhaps a pilot test on certain DLRs can be pursued. Due to the questionable nature of the savings, something which the GAO report in July 2005 (GAO-05-785, page 216) indicated as "*potentially overstated savings estimates,*" it would be more responsible to have the DOD pursue further study of these proposals through the existing management processes of the department and not through an approved BRAC recommendation.

(h) DOD directed the S&S JCSG to not consider any costs/savings associated with Enterprise Resource Program (ERP) modernized automated logistics systems in developing this estimate. The effect of this decision is to mask the real costs that will be associated with modifying DLA's Business Systems Modernization (BSM) effort in order to process actions associated with DLRs and the costs associated with

military services' modifications to their ERP systems (the Army's Logistics Modernization Program, for example) to reflect the changes required to interface with DLA on DLRs since the management of these items will be split. At one point in the S&S JCSG deliberations, the chairman of the group (14 Mar 05 meeting minutes) used a figure of \$500 million for ERP changes to DLA systems and indicated that this would be an expense with no benefits. In the 21 Apr 05 minutes of the S&S JCSG one of the charts attached to those minutes titled "S&S ERP Recap" indicates: "*Mr. Wynne directed removal of all ERP investment costs and savings from scenarios.*" This documentation provides yet another reason why the cost/savings estimates associated with the DLA assumption of the DLR procurement mission need to be independently evaluated so that all costs are captured. The recommendation from DOD does not provide a reasonable basis for determining if there is good economic reason to pursue what three of the four services are uncomfortable about doing if it does not fully address costs against the savings claimed.

3. Inventory Control Point (ICP) Movement. At least three of the four ICP movements in this recommendation were added to 0035R late in the scenario development process. The Army had a virtual ICP proposal that, for not entirely clear reasons in the documentation available on the DOD website, was combined with the other 0035R recommendations in Feb/Mar 05, only three months before the BRAC list was announced. The bottom line is that if the Army ICP proposal were to stand alone and not be combined with the other 0035R recommendations, there would be no net present value savings. The chairman of the S&S JCSG stated in the 11 Apr 05 minutes of the group: "*...that if the PBA savings were not used in the scenario, that the NPV result would be negative as a result of the revision to the scenario to accommodate Army movements of personnel.*" Thus, this portion of the recommendation does not meet the BRAC criteria regarding cost. Taking the example of the TACOM-Rock Island move to TACOM in Warren, MI to further explore this recommendation, one discovers these additional points:

(a). The Rock Island Arsenal, where TACOM-Rock Island is located, had a higher military value score than the Detroit Arsenal, where TACOM-Warren is located. When asked to explain the reasons for the recommendation to move TACOM-Rock Island based on this military value criteria (7 July 05 request from Mr. Cirillo to Mr. Meyer), the answer provided (12 July 05-OSD BRAC Clearinghouse Tasker 0493C) did not address the question. Instead the answer stated that the reason for the move was "*...a result of an Army initiative to establish three life cycle centers of excellence.*" The answer further stated that this was done at the direction of the ISG at Army's request. However, it is important to note that TACOM is already a single major subordinate command that has multiple sites at Natick, MA (Soldier Systems Command), Rock Island, IL and Warren, MI. Rock Island used to have its own major subordinate command (last known as AMCCOM in the early 90's). Previous BRAC recommendations resulted in the AMCCOM command being disestablished and reporting to the commander of TACOM at Warren, MI. Thus, there is only one CG for TACOM, one business management office, one policy and systems office etc already. The organization works well as a multi-sited entity. One of the reasons that it is multi-sited is that the armament and small arms

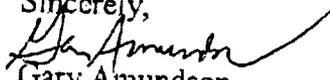
and other weapons engineering work that the former AMCCOM (now TACOM-Rock Island) does is supported by engineers on site at Rock Island Arsenal and at Picatinny Arsenal in New Jersey. There is also weapons testing, an assembly area for world wide management of tool sets (one of TACOM-Rock Island's missions), and a maintenance operations procedure shop for weapons and armament at Rock Island Arsenal. To move the functions indicated in the BRAC recommendation to TACOM-Warren would break the synergy that already exists at Rock Island Arsenal with TACOM-Rock Island. The recommendation would do nothing to consolidate the engineering functions for armament that are at Picatinny Arsenal and at Rock Island Arsenal. Rather than co-locating TACOM-Rock Island personnel with their engineering community, it would move them from the engineers already at Rock Island Arsenal.

(b). Furthermore, the recommendation does not establish one life cycle center of excellence for all TACOM materiel, not only for the reasons already provided, but also because the TACOM-Natick site is not recommended for movement to Warren. It is hard to escape the conclusion that an incomplete understanding of what TACOM-Rock Island's interfaces are with its supporting activities and customers caused the recommendation to be made as it was. Not only was the 7 Jul 05 military value question never answered, but the rationale provided does not support the movement when examined in the light of the facts just presented. In a world with video teleconferencing, desktop vidco, and other instantaneous methods of communication, the necessity to move large numbers of people should unquestionably result in savings, improved processes, and better military value. The movement of Army ICPs envisioned in this recommendation does not achieve any of those things.

In summary, while the consumable and DLR pieces of this recommendation deserve further study and possible incorporation into already existing management processes within the Department of Defense (but NOT implementation via the BRAC route), the ICP movement portion of the recommendations should be rejected outright. This part of the recommendation should be recognized as generating negative savings, deviating from military value criteria, and representing old ways of thinking in terms of consolidation vs new and innovative ways of making multi-sited organizations work without having to disrupt personnel and communities at great cost with little to no payback.

Thank you for your time and I hope you will communicate this to the commissioners even though it arrives at a late date. I also thank you for your service in this task.

Sincerely,


Gary Amundson
Rock Island, IL

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