DEFENSE BUSINESS BOARD

Report to the Secretary of Defense

Corporate Downsizing Applications for DoD

Report FY11-08

- **Recommendations on downsizing principles from recent successful private sector experiences that could help DoD maintain a high level of combat effectiveness at lower cost**

Corporate Downsizing Applications for DoD

TASK

The Department of Defense is committed to providing the highest level of combat effectiveness in order to protect the Nation from both internal and external threats. It must now also meet this commitment in a new budgetary environment. As Secretary Panetta noted, "our growing national debt, if not addressed, will imperil our prosperity, hurt our credibility and influence around the world, and ultimately put our national security at risk. As part of the Nation's efforts to get its finances in order, defense spending will be – and I believe it must be – part of the solution."

Since many private sector companies have had to engage in substantial downsizing as a result of the 2008/2009 economic recession, the Chairman of the Defense Business Board (DBB) (herein referred to as "the Board") established the Task Group on Corporate Downsizing Applications for DoD. The Task Group was directed to provide recommendations as to which downsizing principles from recent successful private sector experience should be considered by DoD that would allow the Department to maintain a high level of combat effectiveness at a lower cost in a reduced budget environment. A copy of the official Terms of Reference (TOR) may be found at **Appendix A**.

Mr. Joseph Wright served as the Task Group Chair. The other Task Group members were Philip Odeen, Robert Toll, Jack Zoeller, and James Kimsey. CAPT Ronald Carr, USN, and Lt Col Edward Lengel, USAF, served as the Task Group Military Assistants.

PROCESS

The Task Group conducted over 20 interviews with current and former executives from consulting (e.g., Accenture, Alvarez & Marsal, Deloitte & Touche, and McKinsey), financial (e.g., Citibank, JP Morgan, and Cowen Group), manufacturing (e.g., A.O. Smith, General Electric, General Motors, and Timken), and Department of Defense (e.g., former Secretary of Defense; former Deputy Secretary of Defense; former Vice Chairman, Joint Chiefs of Staff; and former DoD Comptroller). To supplement these interviews, the Task Group conducted a literature search to provide additional perspectives and best practices. The Task Group's draft findings and recommendations were presented to the Board for deliberation at the July 21, 2011 quarterly Board meeting. The Board voted to approve the recommendations. See **Tab B** for a copy of the brief presented to the Board.

FINDINGS

Regardless of the size of the company or the industry, best business practices for downsizing were similar. In every case, senior leadership was critical to provide downsizing direction and a sense of urgency. The CEO/senior leadership provided a clear vision for the future, a well defined strategy to get there, and a desired end-state. Reductions started at the top of the organization where the CEO and senior executives all led by example. Communication from the top leadership was critical and ongoing through the entire downsizing effort. In many instances, senior executives who did not support the strategy were told to leave. Strategic planning was a key element of all successful downsizing activities in commercial organizations. Downsizing began quickly without waiting for a future fiscal year and with plans and budgets that met targets and goals. Hiring and spending on major capital investments often required corporate headquarters' approval. In many cases, downsizing efforts required the use of consultants or a separate corporate organization working in tandem with the existing corporate structure to ensure downsizing measures took effect.

The Task Group found that as corporations rationalized operations, they focused on reducing overhead, duplication, and unnecessary activities, staff, and facilities. Any organization or business line that had limited potential was closed or sold. There was consistent emphasis on no "across the board" percentage cuts. Any cost center or function not critical to customers was eliminated. Organizational layers, administrative offices, and management processes were reduced and simplified.

Since successful downsizing organizations aligned cost reductions with strategic planning, there were continued investments in technology, new production capacity, and market expansion. Therefore, these organizations emerged from the depths of the downturn leaner, more competitive, and more profitable.

A consistent goal for the long term "health" of the successful downsizing companies was to fairly treat personnel who were laid off as well as those personnel who were retained. Severance plans were fair and consistent across the organization.

Open and honest communications were keys to success. The Chief Executive Officer was frank and frequent in communications in order to demonstrate the "sense of urgency." They did not delegate this responsibility. Employees, shareholders, suppliers, and local communities were kept informed.

RECOMMENDATIONS

After reviewing many private sector companies' successful efforts to reduce cost without impacting performance, the Task Group developed nine recommendations for the Department of Defense. More detailed descriptions of recommendations can be found in **Tab B**.

1. **<u>Top Leadership is critical to success.</u>** The Secretary of Defense must drive the process and emphasize the "urgency" of the situation. The downsizing effort must be a priority that has his strong involvement and public support from the Joint Chiefs of Staff, the Service Secretaries, and other key leaders. Senior leaders within the Defense Department who do not support the downsizing effort should resign or retire. During implementation, there should be consideration for both "incentives" and "penalties" at all levels within the Department.

2. **<u>Key constituents must be supportive.</u>** Congressional support will be needed to enable the Secretary of Defense's downsizing efforts, especially from key appropriations and defense committees. In addition, acceptance from influential trade associations, unions, and other non-profit organizations (e.g., Aerospace Industries Association, Military Officers Association of America, and American Federation of Government Employees) is essential to remove barriers and impediments to successful implementation.

3. **Reductions are driven by strategy.** In order to be successful in "rightsizing," the Secretary of Defense and his leadership team must develop strategic goals to identify essential capabilities that define the future requirements for combat effectiveness. These must be translated into implementation plans within the Programming, Planning, Budgeting, and Execution (PPBE) process. Capabilities that are least critical should be reduced or eliminated (remove the work). Considering the difficulty in achieving cost reductions across the Department, the implementation plans should address only significant opportunities that achieve major savings.

4. **Organization/process needs to ensure results.** As the Chief Management Officer within the Department, the Deputy Secretary of Defense should be the full-time leader to oversee and implement the "rightsizing" plans. A team of senior advisors who are tightly aligned with the Secretary's course of action should assist the Deputy Secretary of Defense in a disciplined and focused approach to deliver a "sense of urgency" in addressing the organizational and budgetary challenges. External downsizing specialists may be required to help plan, organize, and monitor the effort.

5. **Reducing people costs is critical.** The elimination of least critical activities must result in a meaningful reduction in the number of personnel within the Department. It is vital that reductions begin immediately, take advantage of retirements, reduce replacement recruiting to a minimum, and require senior leadership approval for civilian hires. Senior leaders must also be disciplined and focused to make it difficult to maintain or increase the number of consultants and contractors. The process must also be transparent and include a critical evaluation of military and civilian pay and benefits, perhaps using a bipartisan commission panel to achieve broad consensus.

6. **Eliminate redundant/unnecessary activities with special attention to overhead and staff/offices.** Considering the Office of the Secretary Defense has a staff that exceeds 2,700 military and civilian personnel (over 5,000 with consultants), it is important that senior leaders set an example to reduce overhead and personnel in non-value added activities, as well as non-warfighting agencies, organizations, and commands. The organizational structure across

the Department and unnecessary support staff should be substantially simplified and reduced, respectively. In addition, as the Department eliminates work and reduces personnel, unnecessary facilities should be consolidated, closed, or sold.

7. **Current DoD force structure, logistics support, and procurement programs must be critically assessed to improve productivity and reduce product costs.** Existing capabilities should be quickly identified to determine least critical elements for reduction, consolidation, or elimination. For essential capabilities and future critical acquisition programs beyond 2020, more cost effective methods, including a larger proportion of “tooth-to-tail,” must be employed.

8. **Despite the intense focus on cost reductions, investments for the future should be continued/increased.** With the elimination of least critical capabilities and the removal of unnecessary work, the Department should focus critical financial and human resources on the most critical capabilities that support the Nation’s key national security objectives. New acquisition systems that are critical to the Department’s core missions should be identified and their transition accelerated.

9. **Communicate - you can’t do too much.** The Secretary of Defense, as the leader of the Department, must stress the “urgency” of this effort and demonstrate confidence in the “rightsizing” objectives with regular, frank communications on why the downsizing effort is essential to U.S. national security.

CONCLUSION

The Board recognizes the importance of maintaining the highest level of combat effectiveness, but also appreciates the seriousness of the need to do so at lower costs and increased efficiencies in this era of pressures to reduce budgets and deficits. The recommendations included in this report, based on the best commercial downsizing practices, can provide direction to senior DoD leadership in a critical effort to “rightsize” the organization and to employ cost effective, mission oriented, strategic planning solutions in order to effectively position DoD to meet today's requirements and future strategic threats.

Respectfully submitted,

Joseph Wright
Task Group Chair

TAB A

TERMS OF REFERENCE

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DEFENSE BUSINESS BOARD
1155 DEFENSE PENTAGON
WASHINGTON, DC 20301-1155

DEFENSE
BUSINESS
BOARD

April 27, 2011

MEMORANDUM FOR JOSEPH WRIGHT

SUBJECT: Terms of Reference – "Corporate Downsizing Applications for DoD"

The Department of Defense, while maintaining the highest level of combat effectiveness, is facing increased pressure on its ability to finance its many diverse operations around the world due to reduced budgets. This situation is not likely to improve in the near future because of the Federal deficit. Companies in the private sector have often been faced with similar challenges, particularly in the past few years. These companies have had to substantially reduce costs in order to maintain financial health or to just stay in business, including:

1. Sharply reducing overhead expenses;
2. Reducing personnel, pay, and benefits;
3. Streamlining facilities and supply chains – reducing excess capacity;
4. Eliminating low priority R&D, product lines, and operating entities;
5. Renegotiating supplier contracts; and
6. Developing innovative ways to increase productivity.

As DoD's independent advisory board for business affairs, we are forming a task group to review the downsizing activities of private sector companies that have been the most effective in reducing costs without impacting performance and to make recommendations to the Department on best practices for cost containment.

The Task Group will consist of you, Phil Odeen, Bob Toll, and Jack Zoeller. Please provide me with your findings and any recommendations to improve our processes by the Defense Business Board's Quarterly Meeting in July 2011. Captain Ron Carr, USN will serve as the Task Group's Secretariat Representative.

As a subcommittee of the Board, and pursuant to the Federal Advisory Committee Act of 1972, the Government in the Sunshine Act of 1976, and other appropriate federal regulations, this Task Group shall not work independently of the Board's charter and shall report its recommendations to the full Board's public deliberation. The Task Group does not have the authority to make decisions on behalf of the Board, nor can it report directly to any federal officer who is not also a Board member. The Task Group will avoid discussing "particular matters" according to Section 208 of Title 18, U.S. Code.

John B. Goodman

John B. Goodman
Chairman

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TAB B

FINDINGS AND RECOMMENDATIONS

PROVIDED TO THE BOARD ON JULY 21, 2011

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DEFENSE BUSINESS BOARD

Corporate Downsizing Applications for DoD

Task Group

July 21, 2011

Task Group Overview

Terms of Reference

Identify best business practices from the private sector in downsizing efforts that have been most effective in reducing costs without impacting the most critical activities.

Deliverables

Provide recommendations as to which downsizing principles from recent successful private sector experience should be considered by DoD to maintain a high level of combat effectiveness at lower cost in a reduced budget environment.

Task Group

Joseph Wright (Chair), Philip Odeen, Jack Zoeller, Robert Toll, and James Kimsey

Military Assistants

CAPT Ronald Carr, USN and Lt Col Edward Lengel, USAF

"It is not a great mystery what needs to change – what it takes is the political will… as Eisenhower possessed, to make hard choices – choices that will displease powerful people both inside the Pentagon and out." ***Secretary Robert Gates***

Assumptions

- Budget reductions will be required by all Federal agencies, including DoD, in the near future – urgent fiscal action may be required by DoD beginning in FY12/13.
- Past efforts by DoD to downsize (mid 90's) achieved real spending cuts, but issues will be more challenging this time (e.g., major platforms are not as modern).
- Private sector best business practices in successful downsizing efforts can be translated to actionable strategies and tasks within DoD.
  - Substantial budget cuts (5-15%) can be achieved without affecting future mission readiness if there is an intense focus on reducing "overhead and infrastructure" spending.
  - Flexibility in meeting global requirements can be maintained while downsizing.
- Resistance to change will be a challenge, but with proper leadership, people will support the effort and end-state.

Process

- Reviewed selective reports and private sector comparables/benchmarks.
- Evaluated past downsizing efforts in private sector, Federal government, and DoD to identify specific practices that led to both success and failure.
- Interviewed current and former executives in industries and government, including:
  - Consulting:
    - Accenture
    - Alvarez and Marsal
    - Cushman & Wakefield
    - Deloitte & Touche
    - Grant Thornton
    - IBM
    - McKinsey
  - Financial:
    - Citibank
    - Cowen Group
    - JP Morgan
  - Manufacturing:
    - A.O. Smith
    - Crane
    - GE
    - GM
    - Meritor
    - Steelcase
    - Terex
    - Timken
  - Media:
    - Gannett
  - DoD:
    - Former Secretary of Defense
    - Former Deputy Secretary of Defense
    - Former Vice Chairman, Joint Chiefs of Staff
    - Former Comptroller of Defense
  - Federal Government:
    - Current and former OMB officials
    - Former Vice President Gore's downsizing official

Background
Cost of Providing Combat Capabilities Increased Substantially

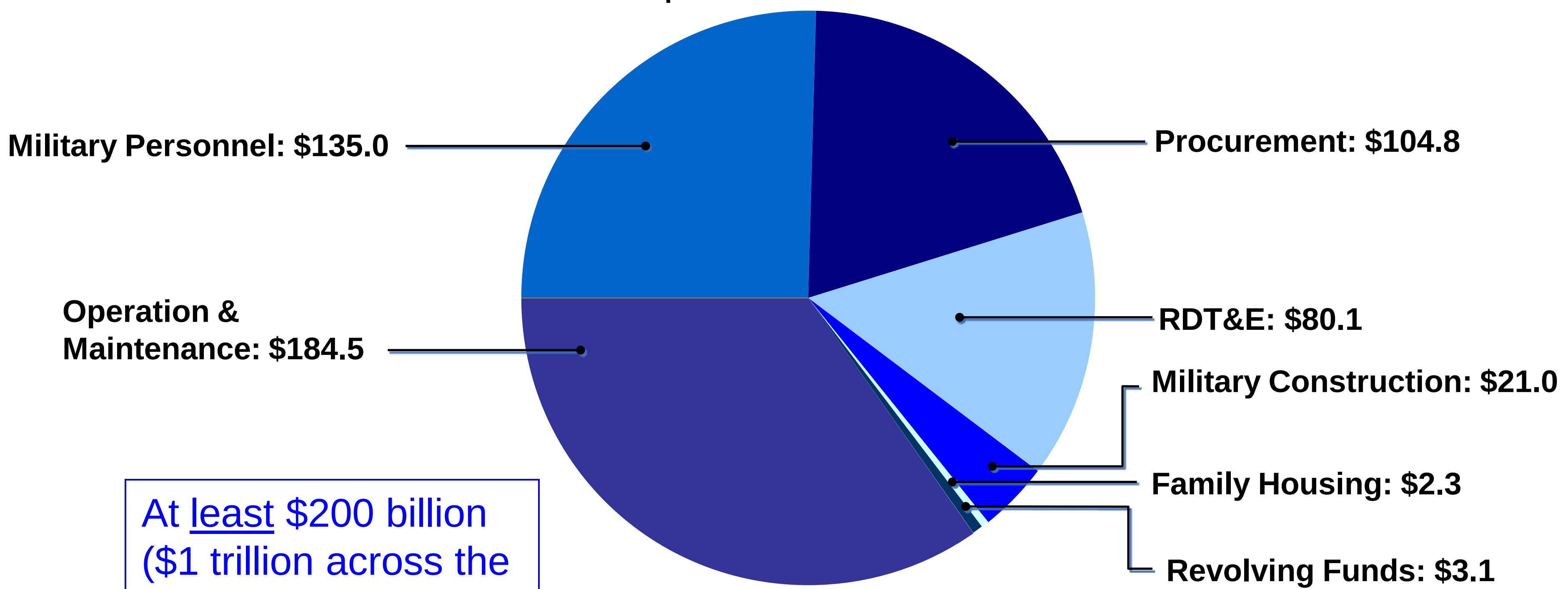
- DoD's topline budget increased from $409B to $661B from 2001-2010, despite no change in active duty end-strength.
  - DoD's base budget increased 85% over past decade (from $287B to $531B).
  - Civilian personnel increased from 687,000 to 778,000 from 2001-2010.
  - Healthcare spending increased from $19B to proposed $52B from 2001-2012.
- Future Years Defense Program (FYDP: FY12-16) "best case" is currently flat over the next five years.
  - Cuts in DoD budgets are widely anticipated.
    (President directed a $400B cut over 12 years)
  - Base investment budget to increase 13% from $113B to $128B (FY08: $174B).

Note: Constant Dollars

FY 2010 Base Budget
(Enacted)

(Dollars in Billions)

$530.8B



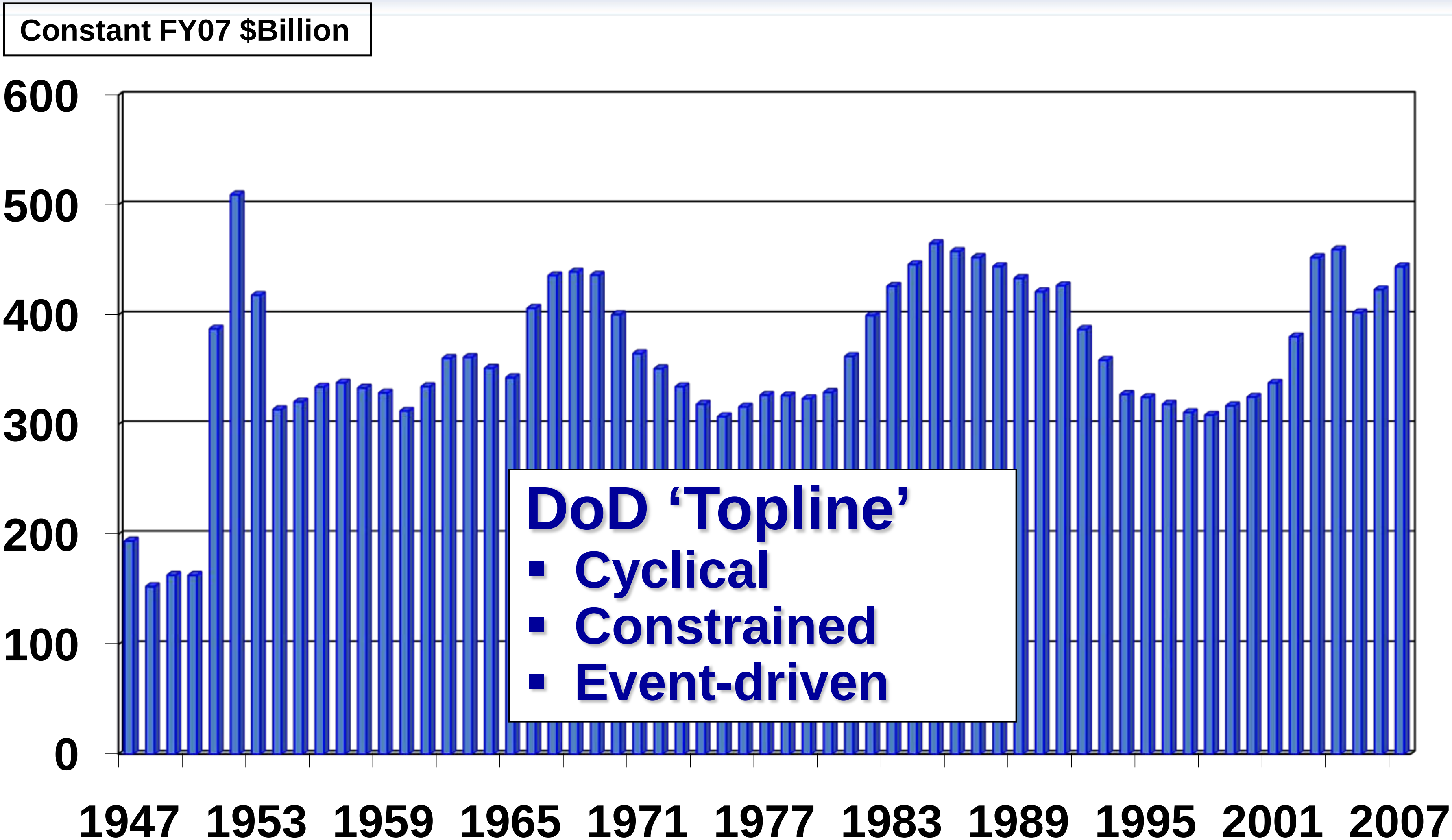
At least $200 billion ($1 trillion across the FYDP) is "overhead"

$660.7B with OCO

FYDP: Future Years Defense Program
OCO: Overseas Contingency Operations

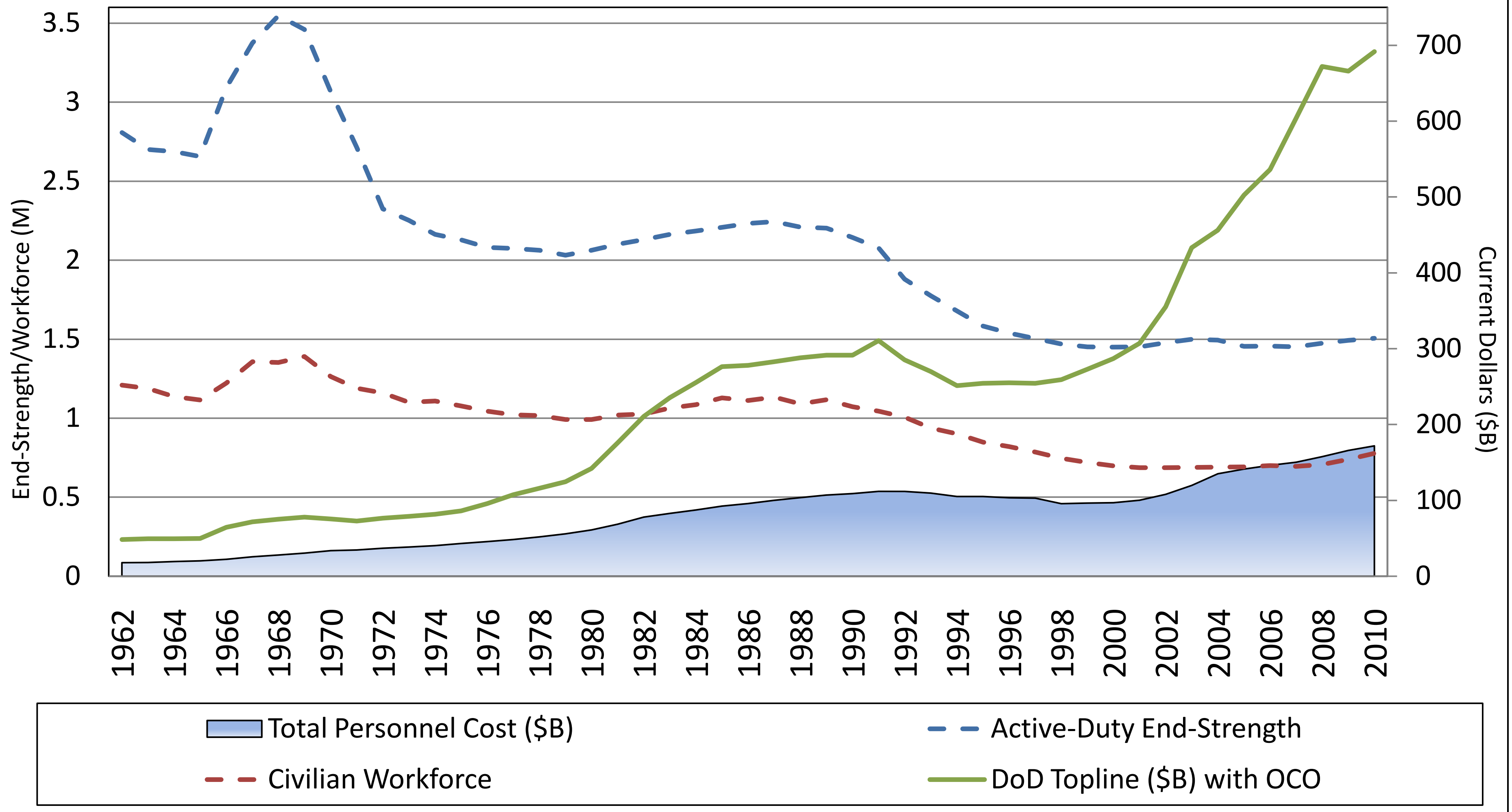
Source: DBB-Reducing Overhead and Improving Business Operations

DoD Total Obligation Authority



Source: http://www.gpoaccess.gov/usbudget/fy07/hist.html – FY 2007 Budget

DoD Labor Costs are Substantial
(1962-2010)



Main Source: FY12 Green Book, OUSD(C) http://comptroller.defense.gov/defbudget/fy2012/FY12_Green_Book.pdf

Background
Last Major DoD Downsizing Efforts in 1990's

- DoD budget has been cut before, i.e., after WWII, Korean, and Vietnam conflicts. Most recent deep reductions in 1990s followed collapse of the Soviet Empire when total budget was reduced 25% from $516B to $385B.
- Force structure sharply reduced: Army divisions down 44% from 18 to 10, Air Force fighter wings down 50% from 24 to 12, strategic bombers down 73% from 324 to 89 and Navy combatant ships down 42% from 546 to 314 (carriers from 15 to 11).
- Major Weapons Programs cancelled/scaled back: major aircraft procurement programs cut from 8 to 4, Army had no funding for heavy combat vehicles, new ships being built dropped by two-thirds.
- 50 major bases were closed by the BRAC process from 495 to 445.
- Total Active Duty Military Manpower dropped 29% from 2.1M to 1.5M, and Civilian personnel reduced 32% from 1.1M to 750,000.

Note: Constant Dollars

Background
Economic Pressures Required Private Sector Downsizing

- America's commercial sector experienced periodic downturns; most recent recession in 2008 was the deepest since World War II.
  - Unemployment rate increased from 5.0% in Dec 2007 to 9.9% in Dec 2009.
  - Auto production was cut nearly in half: GM/Ford/Chrysler laid off 144,600 workers from 2006-2009.
  - Housing starts dropped 73% in annual new construction from 2005-2009.
  - "Top 3" banks took a total write down/credit loss of $61.5B from 2007-2009.
- Companies forced to take extremely aggressive actions to survive.
- Companies that responded effectively emerged stronger as the economy recovered.

(Examples Follow)

Background
Recent Commercial Downsizing-More Dramatic Than In Past

- A major automobile manufacturer with serious structural problems experienced dramatic decline in revenues threatening company's viability.
  - CEO was replaced with one who brought sense of urgency and downsizing strategy.
  - $16B in cost reductions required quickly.
  - U.S. workforce reduced from 110,000 to 50,000; dealerships reduced by 25%.
  - Eliminated/sold under-performing product lines internationally.
  - Converted salaried employees hired after Dec 2000 to defined contribution retirement plans.
  - Renewed commitment to forward-looking technologies.
  - <u>Result:</u> Filed bankruptcy and emerged as a stronger company in 2010.
- A manufacturer of household appliances rationalized product lines, cut costs, and improved profitability just before recession.
  - Replaced 3 top leaders with individuals who "got it."
  - Cut corporate staff by one third and eliminated one third of operating facilities.
  - Standardized products, consolidated production, and reduced management layers.
  - Restructured procurement activity with suppliers to reduce raw material costs.
  - <u>Result</u>: Revenues have recovered and profits are at record levels.

Background
Recent Commercial Downsizing-More Dramatic Than In Past

- A manufacturer of heavy duty vehicle components saw revenues drop from $9B to $3.2B.
  - CEO widely communicated plan, personally approved all capital spending and new hires.
  - Sold off two thirds of entire company focusing on core business.
  - Substantially reduced personnel in three downsizings.
  - Salary of remaining personnel reduced 5-10%.
  - <u>Result:</u> Revenues back to $5B in more profitable core business and improving.
- Large industrial equipment manufacturer grew 25% annually for 12 years; then hit "down-turn like no other."
  - Entered crisis management mentality as total organization vs. separate divisions.
  - Reduced headcount by 35% – office personnel worked part-time.
  - Eliminated all non-value added activities.
  - Managed for cash – not earnings or budget.
  - <u>Result:</u> Downsizing completed in 2009; company competitive today – expecting revenue growth 25% annually.

Findings
Successful Commercial Downsizings Have Similarities

1. **Companies from a range of industries and varying sizes pursued largely similar downsizing approaches in order to survive/thrive.**

2. **Top leadership critical to provide downsizing direction and urgency.**
   - CEO/top leadership and Board drive effort and are constantly involved, emphasizing "sense of urgency" and a focused short-term effort (1-2 years).
   - A clear vision for the future, well-defined strategy/plan to get there, and desired end-state defined and widely communicated internally and externally.
   - Reductions started at top: CEO and division staffs took major reductions.

"Unless you explain how this effort will result in a new, better company – it will be looked at as a short term exercise and they will wait you out." ***Private Sector CEO***

Findings
Successful Commercial Downsizings Have Similarities

3. **Reductions are tied closely to corporate strategy and make a difference.**
   - CEO/top leadership had a good understanding of future strategy and "end state" for company after downsizing.
   - Cost reductions were focused on those activities that "made a difference in reducing costs" and did not fit within the strategy for success/growth.
   - CEO/top leadership always tried to avoid cutting into the "bone" of core activities at all cost.
4. **Organization and discipline are required for success.**
   - While some downsizing efforts used consultants or a separate corporate organization, existing corporate structure is critical to implementing downsizing.
   - Senior executives were asked to support downsizing – or leave quickly.
   - Timing critical – downsizing started immediately – i.e., not next "fiscal year."
   - Plans/budgets revised to meet targets/goals, benchmarking often used.
   - Approval levels tightened on hiring, capital spending, etc.
   - Compensation and bonuses tailored to reward downsizing performance.

Findings
Successful Commercial Downsizings Have Similarities

5. **Cost reductions focus on overhead, duplication, unnecessary staff, and facilities, but operations also often rationalized.**
   - Organizations/business lines with limited potential cut deeply, closed, or sold – focus on core businesses for growth.
   - Deep personnel cuts common from 15% to 30% of “white collar” workforce, but no “across the board” percentage cuts in “successful” downsizing.
   - Organization layers reduced, administrative offices consolidated, management processes simplified, all overhead expenses not critical to customers reduced.
   - Production sites rationalized, consolidated, and excess plants closed and sold/leased.
   - Suppliers asked to share in cost reductions – inventories reduced.
6. **Despite intense focus on conserving cash, most companies continue to invest in the future.**
   - Investments normally focused on technology, new productive capacity, and market expansion.
   - Companies also often took advantage of harsh environment to hire outstanding talent.
   - Successful companies emerged from recession leaner, more competitive, and more profitable.

Findings
Successful Commercial Downsizings Have Similarities

7. **An Important Goal: Treat people fairly.**
   - Severance plans were fair and consistent across the organization (no special deals for a few people). In some cases, added severance benefits provided for all.
   - The goal was to have departing personnel feel they were fairly treated with, if possible, a positive view of company.
8. **Open and honest communication are keys to success.**
   - CEO provided frank and frequent communications on company's situation, planned actions, and successes - did not delegate to HR or PR - it was his/her "show."
   - CEO reached out to all constituencies, employees, shareholders, and local communities.
   - Small number of clear metrics defined and communicated to all employees.
   - Progress measured and reported. Successes celebrated.
   - Special reports, emails, and meetings held at all levels of organization.

In every case, top management communicated frankly and frequently to the organization. People want to know what is happening, even if the news is bad.

Downsizing Principles Learned From Private Sector

1. **Sense of urgency needed for successful downsizing.**
2. **Top leadership initiates and drives effort.**
3. **Reductions driven by corporate strategy and make a difference in cost reduction.**
4. **Organization and discipline required of executives and staff.**
5. **Eliminate redundant/unnecessary activities with special attention to overhead and staff/offices.**
6. **While downsizing, continue to invest in the future.**
7. **Treat people fairly.**
8. **Open and honest communication: keys to success.**

Recommendations
Commercial Downsizing Practices Applied to DoD

1. **Top Leadership is critical to success:** The DoD downsizing effort must be the priority and sustained focus of SECDEF. He must drive the process.
   - Strong involvement and public support from the Service Chiefs will be critical.
   - Key leaders must be on board - Service Secretaries and other senior military.
   - Those who will not fully support the effort should move on.
   - Consider both “incentives” and “penalties” for all levels participating in implementation.
2. **Board/key constituents must be supportive:** Intense efforts by DoD will be required to gain and retain the support of key stakeholders.
   - The Corporate Board equivalent, Congress, must be supportive (leadership of key committees).
   - Senior military leaders will be key to getting support (or at least acceptance) from influential trade associations/lobbying groups.
   - Unions and other employee groups are also important.

“We have all the information we need – We can’t make decisions.”
Senior JCS officer

Recommendations
Commercial Downsizing Practices Applied to DoD

3. **Reductions are driven by strategy:** SECDEF and Leadership Team must agree on goals, strategy, and implementation plan with clear metrics and milestones.
   - Must determine essential capabilities to support a new military strategy for 2020 and beyond (consider a repeat of the “bottoms-up” review, led by General Powell in the 1990’s).
   - Approved capabilities need to be translated into implementation plans – PPBE process (FY12 and POM-13) needs to be revised – done in months, not years.
   - Capabilities that are the least critical should be cut or eliminated (i.e., strategy driven).
   - Only major savings opportunities should be targeted because of the difficulty involved in achieving cost reductions.

“The armed services continue to operate predominantly Reagan-era aircraft, ships and ground vehicles that gradually are becoming technologically obsolete and increasingly costly to maintain. After a decade of lavish spending, the Pentagon is now left with an aging fleet of weapon systems, an overstrained force, out-of-control personnel and health care costs…”
National Defense, July 2011

Recommendations
Commercial Downsizing Practices Applied to DoD

4. **Organization/process needs to ensure results:** Secretary/Deputy Secretary to establish the organization and process for aggressively pursuing the "right sizing."
   - Consider identifying senior DoD executive (DEPSECDEF?) as full-time leader of the effort.
   - A separate, very senior organization (i.e., "SWAT team") advising SECDEF and working with OSD & Services may be needed for sense of urgency, focus, and discipline. An idea: Assign 3-4 star officers from Services, COCOMs, or retired Senior Officers to SWAT team who "get it", or
   - Experienced downsizing executives may have to augment the SECDEF team.

"Few people in Government have experience in downsizing…Should focus on:
1) **DoD should be re-engineered to meet new requirements,**
2) **Control staff should be reduced (over-control today), and**
3) **Employees/Supervisor ratio should be increased from 7-to-1 to the private sector's 25-to-1."** ***Former Gore Downsizing Official***

Recommendations
Commercial Downsizing Practices Applied to DoD

5. **Reducing people costs is critical:** Needs special attention as they drive costs across the DoD enterprise.
   - Reducing head count should be based on decisions to eliminate or reduce the least critical activities – not across-the-board cuts.
   - Reductions should be implemented ASAP – retirements can help as they are a painless way to downsize. New hires should require a high level of approval. Make it difficult to be downsized and then become a consultant/contractor.
   - Pay and benefit costs will be of particular importance. A "Blue Ribbon," or bi-partisan commission panel, may be needed to get broad buy-in (i.e., health care and retirement).
   - Given the sensitivity, the processes must be transparent and even handed (shared sacrifice is important).

"The current TRICARE arrangement, one in which fees have not increased for 15 years, is simply not sustainable." ***Secretary Gates***

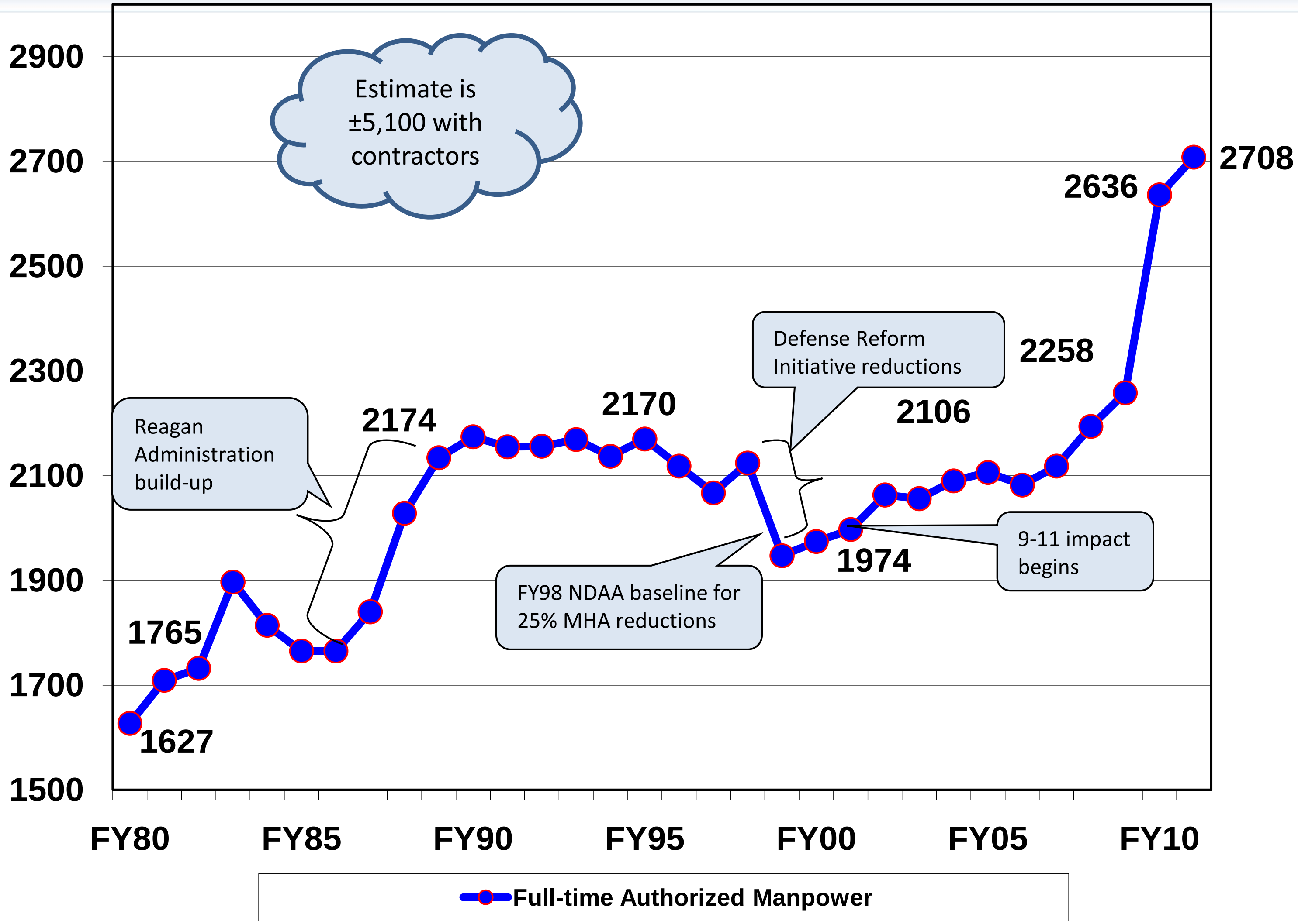
Recommendations
Commercial Downsizing Practices Applied to DoD

6. **Overhead and low priority activities (seen as non-value added) should get special attention**.
   - Reduce number of overhead offices and personnel at OSD, Services, Agencies and COCOMs – senior management should lead by example (OSD staff now exceeds 2,700).
   - Simplify structure by eliminating levels and unnecessary support staff and increasing spans of control. Break the mold and ask tough questions:
     - Why so many "deputies" and their office staff? Why so many billets of 3 and 4 stars and Assistant Secretaries? Why so many military aides? Why so many military in civilian positions?
   - Consolidate facilities and close/sell unneeded offices/locations (may require BRAC process).
   - Look to eliminate entire redundant, unnecessary, and low priority activities – not just people/positions.

> **"…If you just try to cut people it won't be sustainable over time. But, if you cut work, then the people cuts will follow and be permanent."** ***Private Sector CEO***

7. **Current DoD force structure, logistics support, and procurement programs must be critically assessed to improve productivity and reduce product costs.**
   - Challenge existing capabilities to determine which ones are essential and if they can be provided in more cost effective ways.
   - Determine how heavy logistics support costs can be cut substantially (currently $190B).
   - Determine if weapon system acquisition programs are critical to 2020 and beyond.

Trends in OSD Staff Size
Projection a/o June 2010



Note: Chart does not include active duty reservists, detailees, contractor manpower, or temporary overstrengths

Source: Carol Walker at ODAM June 2010

Recommendations
Commercial Downsizing Practices Applied to DoD

8. **Despite the intense focus on cost reductions, investments for the future should be continued/increased:** Preserve DoD resources to invest in the most critical capabilities to support our key national security objectives.
   - R&D to develop critical enabling technology.
   - Selective procurement of new systems that accelerate the transition.
   - Ensure compensation systems will enable attracting/retaining critical talent.
9. **Communicate – you can't do too much:** Regular, frank communication across the Defense enterprise and to major constituents is essential.
   - The Secretary needs to demonstrate confidence that DoD will achieve the downsizing goals.
   - DoD's leadership needs to continuously sell the plan; why it is essential, and why the end result will support U.S. national security (i.e., build a more effective DoD).

"Communicate until it hurts—Be visible and personal…Employees' accomplishments and contributions recognized—Don't assume that your managers all have the necessary communication skills." ***Harvard Business Review***

"DoD still spends too much for Cold War capabilities and is adding new capabilities on top of the old base. They should cut overhead immediately, look at overseas bases for closing, reduce civilian/uniform ratio, allow no contract/replacement for staff augmentation and look at programs that are in trouble. Need to move quickly and complete in two years. Should establish a progress review focused on downsizing." Former Comptroller of DoD

APPENDIX

DEFENSE BUSINESS BOARD

Business Excellence In Defense of the Nation

Selected Quotes
Private Sector Companies

- “We define ‘force level’ that would be required in the future to meet strategy/goals by line of business – this was ‘tops down’ for total strategy/goals and ‘bottoms up’ for businesses to prepare action plans.”
- “DoD has to go through a ‘divestiture-like’ process, getting rid of redundancies and non-core activities. Needs to consolidate.”
- “System will want to spread cuts evenly. Nothing is fair. There has to be a clearly defined set of objectives following a requirements strategy. Can’t be just a numbers exercise.”
- “There are redundant activities among the four Services. Does it make sense to continue maintaining legacy organization in a fiscally restrained environment? The leader has to make a decision and go after that.”
- “DoD, or a company, has to size themselves for competing in a fundamentally different manner (i.e., If its never going to stop raining, you need to build a different kind of camp ground).”
- “Need to make decisions fast – there have been enough studies.”

Selected Quotes
Private Sector Companies

- "If you don't cut deep enough – you're always scrambling to catch up with an increasing cost base."
- "You need to spend more time with the people that stay with the company rather than those who leave or you will lose the top 10% of your employees."
- "Four recommendations for successful downsizing include:
  - Understand the objective of the downsizing and keep it simple with specific metrics.
  - Challenge the status quo and the structure.
  - Establish clarity of command, governance, and execution.
  - Hold key executives and organizations accountable for results."

Selected Quotes
Harvard Business Review

- "Cutting by percentage is crude and ineffective short-term solution to a deep-rooted problem. It's instant gratification that does nothing to fundamentally remedy the situation. The only course is to find a way to eliminate excess staff permanently."
- "The real solution is to rationalize the work, not the workers, and to do so in a manner that prevents the problem from creeping back. Successful companies reduce costs by reducing useless layers of work rather than blindly cutting people."
- "Management must begin by stripping away everything in the company that is not adding value. They must eliminate all middle managers that exist only as power brokers and impediments to communication. They should find where the power structure of the organization prevents workers at every level from taking responsibility. Throughout the company, they must undo bureaucracy."
- "They should devise a costs goal – not a personnel target."
- "Depending on how it is carried out, downsizing can strengthen employee morale or destroy it."
- "The end result of this exercise should be a new strategic direction that includes not only cuts but also new investments."

Selected Quotes
McKinsey Studies

- "According to McKinsey studies, 89% of the current year's budgets can be explained by the previous year's budget. This tremendous inertia drives the predictability of defense spending."
- "Fearful of losing what it already has won, the Pentagon attempts to adapt mature programs to new threats."
- "Defense spending can be predictably described because of the nature of the three underlying forces that shape it: the inertia of existing defense programs, threat, and affordability."
- "When the budget is tight, people do not miss the new weapons and programs they've never had. But tamper with food, salaries, benefits, and pensions, and morale plummets. Shave maintenance and construction, and the fighting infrastructure falls into disrepair."
- "There were roughly 9,000 primary suppliers in 1991 of defense products and a far greater number of secondary companies in more than 200 industry segments. Together these companies represented about 3% of GNP, a similar slice of all manufacturing jobs, and the source of some of the nation's finest R&D."