

Performance Based Payments (PBP) Analysis Tool for Contracting Professionals Professor of Contracting Pinpoints Critical Lessons Learned

Anthony J. Nicoletta

On Sept. 14, 2010, Dr. Ashton Carter, Undersecretary of Defense for Acquisition, Technology and Logistics, issued a memorandum entitled, "Better Buying Power: Guidance for Obtaining Greater Efficiency and Productivity in Defense Spending." In this memorandum, Carter introduced five major Better Buying Power Initiatives. Under the initiative "Incentivize Productivity and Innovation in Industry," Carter directed the development of a cash flow model to be used by all contracting officers contemplating financing other than the use of customary progress payments such as Performance Based Payments (PBP).

Following that directive, Shay Assad, then director of Defense Procurement and Acquisition Policy, issued a memorandum on April 27, 2011, entitled, "Cash Flow Tool for Evaluating Alternative Financing Arrangements." In this memorandum, Assad directed the use of the PBP Analysis Tool when evaluating alternative financing arrangements on all new fixed-price type contracts resulting from solicitations issued on or after July 1, 2011.

Shortly thereafter, the Defense Acquisition University (DAU) developed CLC 057, Understanding Performance Based Payments and the Value of Cash Flow as well as a robust PBP Demonstration Lesson for CON 270, Intermediate Cost and Price Analysis. The lessons learned as an instructor teaching the PBP Analysis Tool demonstration in CON 270 are the focus of this article.

The purpose of the model is to quantitatively measure risk and benefits of a particular PBP schedule to facilitate a win-win financial arrangement.

The cash flow model was formally introduced to students during the first offerings of CON 270 in December 2011. At that time, the version of the model being used was Version 3.0. This version was a vast improvement over Version 2.9 and as of the date of this article, yet another more advanced version of the model, Version 3.1, has been fielded and is being used by contracting professionals.

Since DoD guidance requires the use of the model, it is the responsibility of all contracting professionals to master the

model. The following eight lessons learned will increase the probability that you will master this analysis tool:

1

Read the model instructions very carefully. This sounds very simple and obvious, yet many people do not take the time to do this and become frustrated with the model when it appears to malfunction. Understand what the model can and cannot do.

2

Pay attention to detail. Paying attention to detail is a fundamental requirement when it comes to contracting, and it is no different when using the model. Sloppy work will get you in trouble just as quickly with the model as it would in any other area of contracting. Missed entries and typographical errors will cause the model to not work properly and increase your workload.

3

Pay attention to sequencing. There is a certain sequence that must be followed when using the PBP Analysis Tool. With Version 3.0, it was to populate the "Data Input" Tab, "Contract Summary" Tab, followed by the "Win-Win Analysis" Tab. However, when Version 3.1 was fielded, the sequence of events changed to "Contract Summary," "Data Input," and "Win-Win Analysis." So be prepared for the possibility of sequence changes in performing the model functions whenever a new version of the model is fielded.

4

Find and use the latest version of the model. The latest version of the model can be found at: www.acq.osd.mil/dpap/cpf/performance_based_payments.html. Always go there first to download the latest version of the analysis tool. Get familiar with the new version since some of the features on it may be different than the previous version you were using. If you find a version of the model that works, save it. You want to do this in case the new version of the model has some initial shortcomings or some previously unidentified deficiencies.

5

Exercise caution when using traditional Excel functions like cutting and pasting data or even clicking and dragging. Even though the model is quantitative in nature and Excel-based, some of the traditional Excel functions can cause the model to malfunction. This is not a shortcoming of the model because the instructions clearly state what functions, e.g., cutting and pasting, should not be performed. So be prepared to enter your data manually. Ensure you set aside adequate time to do this.

6

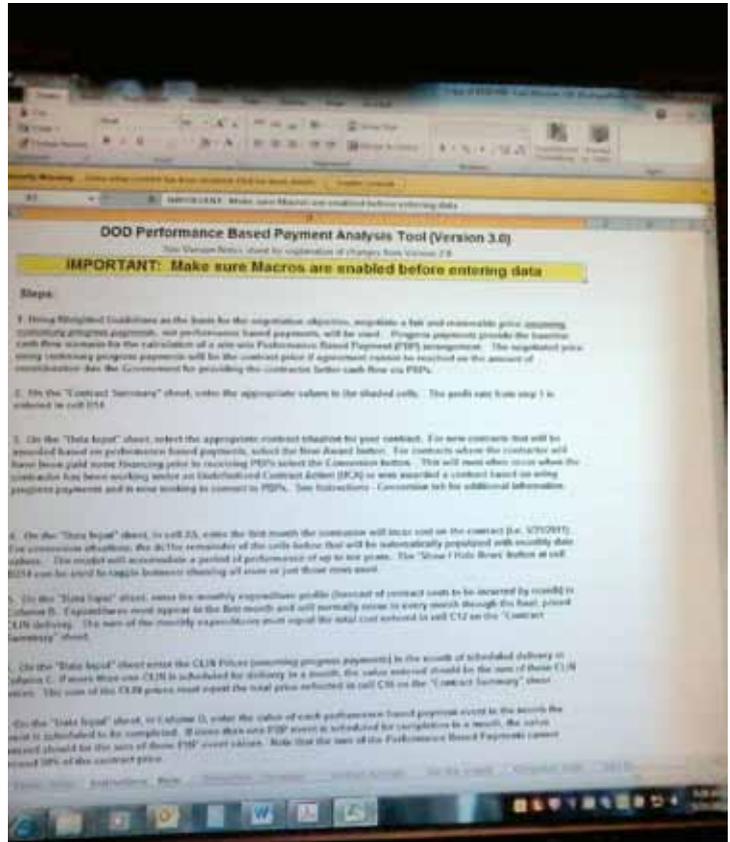
Know your assumptions. The model allows the user under the “Win-Win Analysis” Tab, Assumptions, to input or change fields such as progress payment rate, cost of money (COM) rate, contractor hurdle rate, etc. Know where to find this information and have it readily available to properly populate these fields. For example, the COM Rate, also known as the Treasury Rate, can range from 2 percent - 10 percent. You can find the most current COM Rate at the U.S. Treasury website: www.treasury.gov/Pages/default.aspx.

7

Another issue for some has been performing the “What If” functions. Again, the instructions are very clear on how to do this. However, this function can only be performed under “the Win-Win Analysis” Tab, PBP Column, and not under the “Data Input” Tab, which seems to be one of the most common mistakes. Remember, a right click in this column moves up the event and a double left click pushes back the event. This feature is very useful in that once performed, the model will recalculate cash flow - Net Present Value (NPV), Internal Rate of Return (IRR), etc. Remember to hit the “Reset” button to return to your original position. The model will not allow you to move up the very first event. After pushing back an event more than four times the model stops calculating the effects of this change. This is a constraint that the developer of the model felt was necessary. In the event this happens, a “pop-up” window will appear and ask if you think it is wise to continually push back an event. The model correctly assumes that if an event has been pushed back this many times, then one of two things has happened. One, the contract would have been modified, thereby changing the event date(s); or two, the contract would have been terminated due to poor performance, e.g., multiple missed events.

8

Understand model color coding. The last and possibly one of the most important features of the tool is the color coding of the certain PBP fields, under the “Win-Win Analysis”



Tab. This is a useful feature in that the model will color code with the colors green, yellow, or red the IRR, final cost to the Government, etc. This allows the user to quickly identify whether or not the PBP position using the model is more favorable than the traditional progress payments position using Weighted Guidelines (WGL). Green means the PBP position is more favorable, yellow means they're equal, and red means the progress payment position is more favorable than the PBP position. Users must understand the colors and factor them into their analysis and ultimate determination.

In this short article, I tried to identify some of the lessons learned that I believe will help contracting professionals optimize their use of the new PBP Analysis Tool. Sharing lessons learned has been a fundamental way of capturing and communicating better ways of doing business for years. As most of users of the model probably know, much of the information presented in this article is not new. It can all be found in the model's user manual or instructions. Like any new tool, to master the tool you must be familiar with it, you must know its limitations, and you must practice using it. Too many people do not do this and thus do not retain much of the information; therefore, when it comes time to use the model on a real-world acquisition, they stumble or worse, do not obtain the best possible outcome for the government.

Do not let this happen to you. Remember, you and you alone are responsible for knowing, retaining, and mastering the tools and skills needed to be a competent contracting professional. The age old adage of “practice makes perfect” holds true when it comes to the model. If you remember these lessons learned, you will minimize any issues when manipulating the model and achieve a win-win position that provides increased cash flow to the contractor and a lower price to the government.

Nicolella is a Professor of Contracts at the DAU – South Region. He is an Army Acquisition Corps member and is certified Level III in Contracting.

DAU and NDIA to Sponsor Defense Systems Acquisition Management Course Offering for Industry Managers

The Defense Acquisition University and the National Defense Industrial Association will sponsor an offering of the Defense Systems Acquisition Management course Sept. 10-12, 2012, at the Hotel Valencia Riverwalk in San Antonio, Texas. The course is targeted for industry program managers, assistant program managers, systems engineers, industry personnel serving on DoD integrated product teams, and other personnel who must interface with DoD program offices involved in program development and execution. The result of successful completion of this course is a comprehensive understanding of the environment and driving forces affecting your DoD counterparts that will significantly increase your awareness and effectiveness in dealing with programmatic issues.

The course is also open to a limited number of DoD personnel in grades O4-O6 and GS 13-15, tuition-free. Government students should already be certified at Level II to obtain maximum benefit from this course. Government employees and supervisors may apply the DSAM course towards fulfillment of the DoD requirement for acquisition workforce personnel to earn 80 continuous learning points every 2 years. DSAM counts for 34 CL points, or 3.4 continuous education units. DSAM presents the same acquisition policy information provided to DoD students who attend the DAU courses for acquisition certification training. It is designed to meet the needs of defense industry acquisition managers in today’s dynamic environment, providing the latest information related to:

- Defense acquisition policy for weapons and information technology systems, including discussion of the DoD 5000 series (directive and instruction), and the *Defense Acquisition Guidebook*;
- Defense acquisition reform and initiatives;
- Defense acquisition procedures and processes;

- The planning, programming, budgeting, and execution process, and the congressional budget process; and
- The relationship between capability needs determination, resource allocation, science and technology activities, and acquisition programs.

All course materials will be provided to students on CD-ROM. It is highly recommended that students bring a laptop computer to the class. If you do not have access to a laptop, please contact the respective meeting planner as soon as possible. There will be a limited number of laptops available for use through NDIA, so please call early.

For further information, see www.ndia.org/meetings/202A/Pages/default.aspx. Industry students should contact Taryn Crowder at tcrowder@ndia.org or 703-247-9478.

A limited number of experienced government students may be selected to attend each offering. Prospective government students must first contact Karen Byrd at 703-805-3728 or e-mail Karen.Byrd@dau.mil prior to registering with NDIA.

DAU Partners with DCMA to Establish College of Contract Management

Defense Acquisition University President Katrina McFarland and Charlie Williams, director of the Defense Contract Management Agency (DCMA), have signed a Memorandum of Agreement creating the College of Contract Management (CCM). The purpose of this strategic partnership is to develop an accredited contract management curriculum to enhance the knowledge and skills of the DCMA workforce, eventually utilizing these quality learning assets for the entire Defense Acquisition Workforce. Ultimately, DAU and DCMA aim to provide the needed training to deliver quality products and services to the warfighter—on time and within cost specifications.

The training portfolio extends across all contract management career fields, including quality assurance, contracting, systems engineering, production and manufacturing, program management, and specialized areas such as Naval Special Emphasis and Contingent Contracting. This joint effort leverages current DAU and DCMA learning assets to support development of training by functional discipline. The curriculum development strategy is to focus first on the highest concentration of functional disciplines: contracting, quality assurance, and production and manufacturing.

Kurt Stonerock was selected for the position of CCM dean in early March. He has more than 30 years of experience as an Air Force leader. He served in contract administration positions for 14 years as an Authorized Contracting Offi-

cer (ACO), a commander of DCMA field activities in the United States and overseas, and as DCMA Chief of Staff. He also served as a faculty member of the U.S. Air Force Command and Staff College. He earned his doctorate from Auburn University.

The Optimal Program Structure

Under Secretary of Defense for Acquisition, Technology and Logistics Frank Kendall recently published an article entitled "The Optimal Program Structure." Read the article in its entirety at www.dau.mil/pubscats/ATL%20Docs/The%20Optimal%20Program%20Structure.pdf.

Reinforcing Ethics, Integrity, and Accountability

Secretary of Defense Leon Panetta has published a memorandum reminding every DoD employee, military service-member, and civilian to protect and reinforce ethics as a central element of workplace culture. View this memorandum from the Secretary defining integrity and asking each DoD employee to avoid even the perception of unethical behavior or impropriety at www.dau.mil/homepage%20documents/SECDEF_Memo.pdf.

DAU Continues to Embrace Social Media

The popularity of technology forces companies to rethink how they interact with their customers. Consumers expect relevant and meaningful information as soon as possible. Government organizations are not exempt from this heightened use of technology. Government organizations play an important role in people's lives and must provide information quickly.

One way DAU stays connected to our customers and stakeholders is through social media. In the last several months, DAU's Social Media Team, working closely with the chief of staff, has worked to set up and encourage the use of social media for our external customers.

DAU is currently using several social media outlets and planning to use others in its outreach efforts:

Facebook

With more than 700 million members worldwide, the Social Media Team established a presence on a website where many workforcemembers were already users. By jumping into Facebook, the university has been able to reach the workforce with targeted messages. In turn, DAU customers and stakeholders have posted valuable feedback on innovations that are important to them.

Flickr

The photo-hosting website Flickr allows DAU to highlight the best photos from the university, giving users a glimpse of life at DAU and a way to share high-resolution photos with external award winners.

YouTube

YouTube is a video-sharing website that allows users to upload, view, and share content. The Social Media Team is leveraging YouTube's extensive reach to market DAU's services and to spread awareness of defense acquisition. Similar to DAU, many organizations block access to the YouTube website due to security, productivity, and bandwidth concerns. The page will aim to reach external audiences when they are using the website the most—at home.

DAU's videos on YouTube will be "teasers," ultimately driving users back to DAU's own Media Library. Anticipate the arrival of the DAU YouTube page in a few short months.

LinkedIn

LinkedIn is a business-related social media site developed as a means for professionals to network. By creating a DAU interest group, users are able to maintain and communicate with contacts from their professional lives.

The Social Media Team plans to create a sense of community for the Defense Acquisition Workforce to network, share, and learn from each other. DAU's LinkedIn page will launch later this summer.

If you have any questions or suggestions for DAU's social media efforts and websites, feel free to e-mail social.media@dau.mil.

DAU Welcomes Colorado Technical University As a New Excelerate Partner

Colorado Technical University (CTU) has joined DAU as a new Excelerate Partner. Through the new partnership, credits earned through certain DAU certifications can be transferred into various CTU master's programs. The CTU master's programs include: MBA - Accounting, MBA - Finance, MBA - Project Management, MBA - Logistics & Supply Chain Management, MS - Information Technology, and MS - Systems Engineering (only for Colorado Springs and Denver campuses). In addition, students will receive a waived application fee. To learn more about the Excelerate partnership opportunities with CTU, visit www.ctutoday.com/DAU.