

NCMA Hosts Deputy Secretary Hamre at East Coast Educational Conference

No Mistakes and No Further Spending to Avoid Mistakes — Irreconcilable Differences?

Editor's Note: Deputy Secretary of Defense John Hamre addressed the National Contract Management Association (NCMA) East Coast Educational Conference on Dec. 4, 1997, at the Omni Shoreham Hotel, Washington, D.C. Focusing on the goal of a paper-free contracting process by the turn of the century, he presented several initiatives toward that end. Approximately 300 senior government and private-industry procurement officials attended. The following text is an excerpt of his remarks. (This information, provided by the Office of the Assistant Secretary of Defense for Public Affairs, is in the public domain and may be accessed at <http://www.defenselink.mil/news> on the World Wide Web.)



"WE WANT NO MISTAKES IN THE ACQUISITION PROCESS, AND WE DON'T WANT TO PAY FOR THE INFRASTRUCTURE IT TAKES TO PROVIDE NO MISTAKES...IT'S NOT POSSIBLE TO RECONCILE THESE TWO INHERENTLY CONTRADICTORY GOALS WITHOUT IT BEING A TEAM EFFORT BETWEEN THE GOVERNMENT AND THE PRIVATE SECTOR. AT ITS CORE IS THINKING FUNDAMENTALLY ABOUT NEW WAYS OF DOING BUSINESS, WHERE...WE TRUST EACH OTHER."

I'm here because I am paying a debt. I had agreed to meet with you all earlier, and I had to drop out on that at the time, and so I'm back now, I hope, with a stronger and richer message than I was going to have before. At that time, I was the Comptroller and was going to try to exhort you into helping me, and now I'm in a different position where people seek my support rather than avoid my meetings.

So I would like to at least share with you some of the things that we are planning to do. Obviously, it is enormously important as we interface with all of you, [especially] those of you in the private sector. I know that there are a certain number of folks here who are from government, and so your lives are going to be more upset by me than are the civilians in the room — non-DoD I should say. But nonetheless, all of our lives are going to change fairly dramatically, and I would like to talk about that.

Two things are very clear to me from watching what has unfolded the last several years in Congress, and that is simultaneously we want no mistakes in the acquisition process, and we don't want to pay for the infrastructure it takes to provide no mistakes. Have I got it

right? And I think that's obviously an impossibility in this world; yet, we keep hearing the drumbeat that there is an army of shoppers at the same time that we are castigated for spending too much money on commercially available equipment when we buy for the government. There is so much dissonance in our lives that it's very hard to sort all that out.

Contradiction, Reconciliation, Hopefully Partnership

So we are marching off on a path where we think it makes sense. We are obviously going to be needing all of your help, and probably will have to modify some of our plans and our direction. But, we are going to try and reconcile these two things — these two inherently contradictory and irreconcilable goals. We are going to try as best we can to deal with that, and I would like to talk with you about that because, in essence, it's not possible to reconcile these two inherently contradictory goals without it being a team effort between the government and the private sector. At its core is thinking fundamentally about new ways of doing business, where at its core we trust each other.

My sense is that's not a common word in your vocabulary because you're frequently thrown into battle as the cham-

pions for your respective sides, and the goal is to kill each other, and to all of a sudden say that this new modality is one where the default premise is trust — I think that ultimately is what we're talking about. We are not going to be able to lower the cost, the transaction costs, associated with the acquisition process and minimize — I don't say eliminate — but minimize mistakes unless we can become more thoroughly integrated as partners in this process.

We're Choking on the Process

There are several initiatives that I think are going to typify the challenges we are all going to face and which I would like to discuss. First of all, we have made a commitment as a Department to become a paper-free acquisition process by the turn of the century. Every time I say that, and knowing individuals in the Department of Defense, they turn white as a sheet for good reason. As I said, I used to be the Comptroller and was responsible for the financial management activities of the Department.

I remember the first time I went out to Columbus, Ohio, where we have the large DFAS [Defense Finance and Accounting Service] Payment Center for large contracts. It's a large operation. We

disburse about \$43 million an hour. The first thing you see is these big sorting wheels that were probably built in the 1930s to sort the paper that comes in the door every morning. There are 15 linear miles of shelf space dedicated to contracts/contract mods.

We are choking on the process. Nobody in the Department – I don't mean this critically – nobody is doing financial management; we are busy coping with the wreckage of financial services. And that's not criticizing anybody; that's the way this system has evolved. Frankly, I think that in some ways we are further ahead than some businesses are. I am shocked to find out that I have 3,000 invoices at Columbus – about 1,000 of them are over three years' old, and nobody is asking for their money. It is for a unique set of reasons having to do with fiscal law. We didn't have available funds to liquidate those invoices, and nobody is saying anything, which tells me that industry is just as messed up as we are.

Now, if you are choking on a paper process – and obviously we are choking on a paper process – thinking in very superficial ways about getting rid of the paper forces you to confront underlying ways of doing business. Think about this: 65 percent of all of our payments out at Columbus are for less than \$2,500. Here we have a contract payment operation where, on the average, it costs us 150 bucks to make a payment, on \$2,500, \$1,500 payments. It's Looney Tunes!

So you need to rethink in fairly fundamental ways and force yourself into the process of thinking about a paper-free environment. It's remarkable – it has had an energizing effect on our community. We are having a series of meetings right now, and I had a late meeting last night – you have to bring everybody to the table, the Air Force and Gen. Malishenko from DCMC [Defense Contract Management Command]. We've got to get Gary Amlin from DFAS and Gen. Kelley from DISA [Defense Information Systems Agency]. You have to bring everybody to the table at the same time to figure out solutions to this, but it is energizing to us right now (the opportunities).

And let me just describe one because, ultimately I'm going to ask you to be potentially partners with us on this. There is a very fast way to get to a paper-free environment for large contract operations. You have to segment this market, and I'll talk to you about some of that in a second. But in terms of large contracts, there is a very snappy, fast way to do this.

Why Not Servers in the Billing Offices?

Even though we have all in our respective worlds spent gazillions of dollars with software houses to develop systems to run all this, [there's] one thing: It's all unique – none of it is standardized, and it's painful to try to put it in an EDI [Electronic Data Interchange] interface. Some of you have been working on that problem. One thing has been normalized in this environment over the last 25 years, and that's the instructions that the computer finally sends to the printer. You all want to be able to swap printers, huh? So it turns out, that's one thing in the office-automation world that has been normalized.

Now, if you can put a server in between the computer and the printer, and steal a set of electrons on the way to the printer, you can get an image of that document. You don't have to turn it into paper. Now, we in the Department of Defense, on the average, when we write a contract will print up to 17 copies of it. Only one went out to Columbus, Ohio, in that 15 linear miles of shelf space. God only knows where all the other stuff is.

If you adopt this approach, where you are putting a server at that contract-writing shop and getting an image of that contract, you can then use standard Internet tools and call that contract up. You come up with an automated indexing mechanism through which you can get that contract. You can now get an enterprise-wide imaging solution, and nobody has to change their business practices. It's revolutionary when you think about it.

You know how hard it is to get people to change business practices. I mean, the hardest problem about converting to EC-EDI [Electronic Commerce-Electronic

Data Interchange] is that you all may want to do it so that you can get your payments faster, but if the rest of your private sector trading partners aren't interested in it, it forces you to bifurcate your billing processes, and nobody wants to do it. So it's like the Mach level, the speed of sound. We can't break that barrier when it comes to EC-EDI because we are forcing you to confront something that you would rather not deal with.

But you can do it this way very inexpensively, and the return on investment, just in the finance world alone...right now, the finance world (DFAS) is buying the servers and putting them in locations, and we get a return on investment from file-clerk savings alone within five months. It's dirt cheap, and anybody can join onto the identified solution when they are ready to, when they get the confidence that they no longer have to look at that sheet of paper to do their business.

Now, one of the things, ultimately that I want to broach with all of you is the subject of us putting a server in your billing offices and not ever turning that invoice into paper. Let us pull it from a server that we would own and put in your organizations so that we can pay you electronically. Now, this is the first you're hearing about this, but I really want you to start thinking "outside of the box," like we're thinking outside of the box.

I want us to become integrated in an enterprise-wide solution to this process where we are genuinely partners, and we'll follow up with you in talking about this.

Why Not Payment Upon Receipt/Delivery?

The second part of this segmentation of the problems is we are increasingly going to try to adopt what I call "hybrid tools" in the contract-payment business. Now, I don't know how many of you are used to producing something and then calling a DCMC inspector and saying, "Okay, come some time, look at this, and then we'll sign the DD-250"; and then, of course, that just triggers the whole paper process for us to eventually pay you, once we can marry up all these

sheets of paper. It's not at all clear to me why instead of it being a DD-250, it can't be a credit card payment authorization, just like when you're buying a pizza: Pay on receipt. Pay at time of delivery. There is no reason we can't do it.

Now it forces you to go through some fairly fundamental rethinking about the business process, about, for example, source acceptance. We've created a whole modality of working with the private sector on source acceptance, but you have to rethink. This is on our side of the equation, and we, the Department of Defense, have to rethink. It also is, frankly, going to force through, I think, a more interactive approach in internal controls with you all, so that if we are, in essence, taking delivery and paying on location, then we have confidence in the liabilities that come with that and your responsibilities that come with that. We can, both sides, streamline our business process so you are no longer having to cut DD-250s and are no longer having to cut invoices, and you get paid right away.

But there come obligations with that — obligations of confidence, internal controls, of working together. So I think this is another avenue we're going to be exploring with you in the next couple of months.

Why Not Less Source Acceptance?

Third is this issue of source acceptance of goods. I personally think we, the Department of Defense, have to think/rethink our whole basis for source acceptance. This is one area where there are probably some of the starkest differences between how the government does business with vendors and how the private sector does business with vendors — this area of source acceptance. It's not uniform. It's not at all uniform, but it is startlingly different.

We may have to adopt in the Department more flexibility in our approach to the area of source acceptance, but currently we have 200,000 items for which we require source acceptance. Far too many of those items are there because of relatively minor issues that occurred early

on in receipt of that product; then we have embedded [source acceptance] and never gone back to think about it again.

We have under way right now a systemic review to look at our source acceptance procedures. I think it's going to take us another six or eight months before we can get a final bead on it, and we will review — we are committed to doing a 100-percent review — of source acceptance goods over the next three years.

What we have attempted to do in our business, of course, is ignore the transaction costs associated with source acceptance because they were never paid by the customer who ultimately was getting the goods. Source acceptance was a free commodity in the Department of Defense, and of course, any time you get something that's free, you either tend to abuse it, overuse it, or ignore it. So finding ways of bringing the transaction costs associated with source acceptance into the acquisition process is going to be a high-priority for us over the next year.

Why Not Fix the GFE Default Mechanism

Finally, an issue that probably is going to have some impact on all of you, and that is, what is going to be our approach to government-furnished equipment [GFE]? We have an enormous amount of government-furnished equipment in the custodial care of contractors. It is, frankly, being poorly managed. As a large-scale process/business practice, it's being poorly managed. I'm not saying that you, as companies, are doing a poor job; or us, the government, we're doing a poor job. It isn't that. I'm not saying there are any venal or wicked people that are doing bad things; I'm saying that the process is one that is not systemic toward thoughtful management.

And so invariably we end up repeatedly buying things that we don't need, or we tend to keep things and keep them on the books much longer than their economic utility. The default mechanism is always save it, and that's certainly not the mode that you have in your world. (You know, at all costs, save that 286 processor. I don't know where

we're going to put it, but we're going to have it.)

The default mechanism is all wrong in government-furnished equipment. This is a very complex problem to solve. It's going to require that we change the starting position on how we treat new things with new contracts as well as how we systematically go about the process of liquidating what's there. It's a very complicated problem; and, again, we have tended to ignore this because the transaction costs were relatively invisible in our system. So finding a way to make them explicit is going to have to be our criteria/part of our action plan over the next year.

Trust, Mutual Interdependency, Open Venues

I hope what comes across to you is that we are taking a very far-ranging look at this area, and in all honesty, cannot accomplish what we need to get done by ourselves. It will be impossible to do these things without, frankly, the active participation and support of our private-sector partners. We really do have to think about ourselves in quite different ways — no longer as adversaries in every dimension, but frankly as partners, as we together try to reconcile the inherent contradiction of the two large, political pressures we're all facing: We don't want any mistakes, and we don't want to spend anything on having no mistakes. To try to reconcile that means we're going to have to be working together on all of these things.

I'm very open to your suggestions, to your comments. I think we want to create open venues to hear these problems out. Five years ago, FacNet was the solution to everything. We now know that's not the solution to everything. Three years ago, EC-EDI was the answer to everything. We now know that isn't the answer to everything. We're going to have to break up this problem into pieces, and we're going to have to find ways with you where it makes sense to accomplish a goal all of us are interested in — to make as seamless as possible the interdependency of our mutual systems so we can trust each other, use each other's information, and carry out our business.