10 Myths

About Performance Based Logistics

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Why This Conversation Today?

PBL implications for the war fighters, Services, taxpayers, ……industry

Trends in PBL adoption: 1998 – 2005

2005 – 2010

2010 – 2013

Myths and myths' impacts persist

Myth #1

PBLs fail to deliver advertised mission readiness and cost improvements

What the Evidence Indicates

Myth #1: PBLs fail to deliver advertised mission readiness and cost improvements

- Proof Point Analysis (2010-2011) provides compelling evidence regarding cost and performance improvements

- DoD's Activity Based Costing capabilities invariably understate pre-PBL sustainment costs, whereas (commercial) PBL costs are known precisely

- Secondary/tertiary effects associated with non-PBL sustainment not accounted for in savings calculus

Bottom line:

PBL performance improvements are significant and as advertised, …

Cost saving estimates are understated

Myth #2

PBLs must be developed and managed with precision

to achieve

significant cost and performance improvements

What the Evidence Indicates

Myth #2: PBLs must be developed and managed with precision to achieve significant cost and performance improvements

- ➢ Strength of PBLs can be determined by objectively measuring adherence to established PBL business model tenets

- ➢ <u>None</u> of the PBL arrangements examined in Proof Point Analysis exhibited strong adherence to all established PBL tenets

- ➢ Every PBL examined in Proof Point exhibiting at least moderate adherence to core PBL tenets experienced both cost and mission performance improvements *

Bottom line:

Moderate adherence to PBL tenets delivers success

Robust strategies deliver positive outcomes absent perfect execution, PBL is a robust business strategy

Myth #3

PBL and outsourcing are synonymous,…

negatively impacting Services' ability to comply with Core and 50/50 mandates

What the Evidence Indicates

Myth #3: PBL and outsourcing are synonymous, …negatively impacting Services' ability to comply with Core and 50/50 mandates

- PBL sustainment may be 100% organic, 100% commercial, shared
- PBLs can be leveraged to drive work into organic DoD activities
  - Industry behavior incentivized by potential for improved profit, Return on Invested Capital (ROIC) and assured revenue streams
- Decision to outsource organic work is the Services

Bottom line:

PBLs not synonymous with outsourcing
Profit and ROIC can incentivize increased organic workload, making Core and 50/50 compliance less challenging

Myth #4

Ensuring the "best deal" should be Services' criteria for executing a PBL arrangement

What the Evidence Indicates

Myth #4: Ensuring the "best deal" should be Services' criteria for executing a PBL arrangement

- Determining if a proposed arrangement is a "best deal" is not within the art of the doable, …seeking it is costly and futile
  - Lack of strong Activity Based Costing capabilities
  - Inability to cost second and third order effects of pre-PBL sustainment
  - Lack of trust, ….and therefore transparency

- Delaying in the hope of identifying and negotiating a "best deal" forestalls establishing conditions that facilitate identification of "better deals" in the future

- Cost estimate of delay for a typical subsystem =

(.2 x $ value of annual spend x # of years of delay)

Bottom line:

Prudent "speed to value" prevents excess, unrecoverable excess costs to the Services

Myth #5

Industry makes “excess profits” on PBL arrangements, …

which hurts the Services

What the Evidence Indicates

Myth #5: Industry makes "excess profits" on PBL arrangements which hurts the Services

- PBLs afford: Reduced costs and improved readiness for Services in exchange for potential industry profits above negotiated levels, improved ROIC, assured revenue streams

- The Key: A Firm Fixed Price contract of sufficient length to warrant investments in product quality and process improvements

- Acting to constrain industry's profits (excess or otherwise), reduces Services' cost and performance improvement potential

Bottom line:

PBLs incentivize "Win-Win" behavior, and drive down Service costs

Transactional logistics commands higher profit margins,
adding costs the Services pay, ….
for less performance

Myth #6

PBLs increase Services' mission and financial risk

What the Evidence Indicates

Myth #6: PBLs increase Services' mission and financial risk

- Complexity and uncertainty are risk drivers

- Over 30+ year life of a typical sub-system employing transactional sustainment, Services and DLA will integrate, synchronize and source myriad requirements and write/oversee 1000s of contract actions

- "Integration" PBLs reduce above complexity to <10 contracts

- A multi-year, Firm Fixed Price contract for a specified level of performance eliminates budget uncertainty

Bottom line:

PBLs reduce financial and performance risk

A single PBL is more difficult than a single transactional contract
Over a system's lifetime, PBLs are far less complex and uncertain

Myth #7

PBLs negatively impact

“year-of-execution” funding flexibility

What the Evidence Indicates

Myth #7: PBLs negatively impact "year-of-execution" funding flexibility

- "Year-of-execution funding flexibility":
  - Percent of total funds available to shift between accounts
  - Total amount of funds available to the Service

- PBLs reduce the percentage of total funds available to shift between accounts in the year of execution

- PBLs increase the total funds available to the Service by reducing the cost of sustainment by ~20%

Bottom line:

20% savings are 100% flexible

Transactional logistics effectively increase costs by ~20%
Reducing available discretionary funds by an equal amount

20% added cost is 0% flexible

Myth #8

Where only one commercial maintenance provider exists,

PBL cannot deliver

mission readiness and cost improvements

What the Evidence Indicates

Myth #8: Where only one commercial maintenance provider exists, PBL cannot deliver mission performance and cost improvements

- Distinguishing characteristic of PBL strategy: "Manufactures " competition" regardless of the competitive landscape
  - Firm Fixed Price contract with an appropriate Period of Performance and clearly defined requirements
  - Provides known revenue stream
  - Enables targeted investments in quality and process improvements
  - Provider improves profitability by "competing" against its product quality and process challenges

- Services share in improved profitability at contract renegotiation or through gain sharing during the Period of Performance

- Transactional logistics commands higher profit margins, incentivizes more repairs/sales and lacks investment incentives

Bottom line:

PBLs align Service and industry interests

Myth #9

Where Services do not own

maintenance-related data rights,

PBL arrangements cannot deliver

mission performance and cost improvements

What the Evidence Indicates

Myth #9: Where Services do not own maintenance-related data rights, PBLs arrangements cannot deliver mission performance and cost improvements

- Data-rights ownership a negotiation lever, …not the only one

- Industry highly incentivized by assured revenue streams
  - Influence on profit margins

- Industry highly incentivized by Return on Invested Capital
  - Influence on “where” the work is performed

- PBLs “manufacture” competition” regardless of data ownership

- Companies owning data rights have added negotiation leverage,
…they do not have all the leverage

Bottom line:

Industry won’t ignore opportunities to improve profit & ROIC

Myth #10

PBLs result in a loss of Service "control"

What the Evidence Indicates

Myth #10: PBLs result in a loss of Service "control"

- Transactional logistics arrangements where the government is the integrator often provide less real control than imagined

  - Disparate activities impact organic sustainment: operators, depots, Service supply & contracting activities, DLA, comptrollers, … and commercial service providers and suppliers

- Commercial PBL provider integration can significantly reduce the challenges present in the Department's sustainment value chains

  - Integrated planning, demand signal management, sourcing of services and supplies, financial controls, etc.

Bottom line:

PBLs can provide the Services greater real control over their sustainment operations

Myths #11 - #17

11. **PBL strategy dictates a one-size-fits-all approach.**

12. **Exhaustive and expensive BCAs are required to develop PBLs**

13. **PBLs lock Services into long term, inflexible contracts**

14. **PBLs can only be successful for sub-systems or components**

15. **All equipment should be maintained under a PBL arrangement**

16. **PBLs must be Firm Fixed Price**

17. **PBLs must have five year or more Periods of Performance**

In Summary

Properly structured and executed,
PBLs reduce the Services' cost per unit-of-performance
while simultaneously driving up absolute levels of
system, sub-system and component readiness

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