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Testimony before the House Armed Services Committee Assessing Progress and Identifying Future Opportunities in Defense Reform

Michèle Flournoy, Co-Founder and Chief Executive Officer of the Center for a New American Security

Chairman Thornberry, Ranking Member Smith, distinguished members of the House Armed Services Committee, it is truly an honor to testify before you today on the critical topic of defense reform.

It is hard to remember a time when the need for defense reform was more acute. The growing challenges the U.S. armed forces face in protecting American interests, values, and allies in the coming years are truly daunting: the spread of the Islamic State, al Qaeda, and other violent extremist groups; the turmoil in the Middle East; the resurgence of a more aggressive Russia; the rise of a more capable and assertive China that is challenging the rules-based international order in Asia; persistent threats from states like Iran and North Korea; the continued proliferation of deadly technologies to both state and non-state actors; and the emergence of new threats in the cyber and space domains – just to name a few. With strong leadership on defense issues in both the Senate and the House and a sitting Secretary of Defense who is willing to pursue fundamental reforms, now is the time to develop and implement a plan of action to ensure we get the most out of every taxpayer dollar invested in defense. I am glad to see that the members of this committee, Republican and Democrat, share this sense of urgency.

Over the past few years, this committee has lead the charge to reform how the Department of Defense does business in an effort to strengthen the U.S. military and deliver greater value to the American taxpayer. Creating a more agile and cost-effective DoD acquisition system has been a top priority, with this committee formulating a number of the critical reforms that were the hallmark of last year's defense authorization bill. Given the scope and complexity of the changes DoD must now make to its acquisition organization, culture, and practices, I would advocate that the committee give the new Secretary of Defense and his team this year for implementation and consolidation, with close consultation with this committee to ensure the desired impacts and benefits are realized. In the meantime, this committee has an opportunity to use this legislative cycle to examine and advance a number of other critical defense reform initiatives.

Even in a period when the defense budget is likely to increase, I would urge this committee to continue to be aggressive in pursuing a robust defense reform agenda. Although our military is more capable than ever before, its current cost curve is not sustainable. Fundamental defense reforms are needed to free up resources for reinvestment in the people, concepts of operations, and capabilities that will enable us to maintain our military-technological edge in the face of a much more challenging future security environment. Even in an era of modestly higher defense budgets, fundamental trade-offs will have to be made. That is why it is so important that Secretary of Defense Mattis and this committee partner to drive strategy-driven choices and continued progress on defense reform.

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Defense reform is, as they say, a “target rich environment.” There is a wealth of opportunities to improve the performance and cost-effectiveness of the defense enterprise. They are not necessarily easy, but they are plentiful. Knowing that my fellow witnesses on this panel may focus on other areas such as reform of the military compensation and retirement system, financial and cost-accounting reforms, acquisition reform, or reforms to the military personnel system, I have chosen to focus on four other areas that I believe should be priorities in any defense reform agenda because they meet two key criteria: they have high potential to improve DoD’s performance and they are likely to free up substantial resources that can be reinvested in higher priority areas. My four areas of focus today are: rightsizing headquarters and transforming defense agencies; reducing excess infrastructure; reshaping and reinvigorating the civilian work force; and improving the quality and cost-effectiveness of military health care.

Rightsizing DoD Headquarters and Transforming the Defense Agencies

Since the Goldwater-Nichols amendment, headquarters staffs – namely the Office of the Secretary of Defense, the Joint Staff, the combatant commands, the service headquarters, and the defense agencies – have all grown substantially, even as the size of the active duty military has shrunk. Many functions are distributed or replicated across multiple entities. While some functional duplication may be appropriate and necessary, I believe that much of it is not. Today, the COCOM staffs have grown to almost 38,000 people, the Office of the Secretary of Defense to more than 5,000 people, and the Joint Staff to nearly 4,000, not to mention the headquarters staffs of the military services, which collectively dwarf all three. As Arnold Punaro has previously testified, the Office of the Secretary of Defense, the Joint Staff, the Combatant Commands, and the Defense Agencies now account for some 240,000 people (excluding contractors) and nearly 20 percent of the DoD budget.¹ Some attribute this growth to the increasing complexity of the security environment, the proliferation of tasks assigned to the Department, and the reallocation of work from the services to the agencies. While these factors may account for some of the growth, I suspect that other, more worrisome factors are also to blame: namely, the natural tendency of bureaucracies to expand over time, a lack of role clarity and accountability that fosters duplication of effort across staffs, and lack of leadership focus and authorities to fundamentally re-baseline and reshape headquarters staffs and DoD infrastructure.

This problem is not just a matter of inefficiency; it is also an issue of effectiveness. In the private sector, bloated headquarters staffs have been documented to slow decision-making, push too many decisions to higher levels, incentivize risk-averse behaviors, undermine organizational performance, and compromise agility. The same is certainly true in government. What’s more, in the DoD context, oversized staffs consume precious resources that could otherwise be invested in strengthening our warfighting capabilities. Consequently, this problem should be addressed as a matter of priority.

Perhaps the greatest opportunity for potential savings lies with the defense agencies, which account for the vast majority of the people and resources in DoD Headquarters. On paper, each agency is overseen by an Undersecretary of Defense; in practice, however, this oversight is rarely as rigorous as it should be given the size and complexity of the agencies and the other competing responsibilities of the undersecretaries. A thorough management review of the defense agencies to identify how they could leverage best business practices and new technologies to improve performance and reduce costs is long overdue. Congress should task the Secretary of Defense to undertake a review of the defense agencies to identify and prioritize opportunities for improving mission effectiveness, increasing productivity, eliminating unnecessary functions and layers in the organization, and reducing costs.

Highest priority should be given to those defense agencies that operate most like civilian businesses, to include the Defense Logistics Agency (DLA), the Defense Information Systems Agency (DISA), the Defense Health Agency (DHA), and the Defense Finance and Accounting Service (DFAS). These account for roughly \$134 billion of DoD's \$587 billion budget. Congress should require the Secretary of Defense to undertake a management assessment of these agencies to examine how a combination of best practices from the private sector, new technologies, and automation might improve the performance of these agencies and create cost savings that could be reinvested in core DoD mission areas. For example, automation is already beginning to take over many routine cognitive tasks in fields such as finance and accounting, allowing potentially significant cost savings. A report by McKinsey Global Institute that evaluated 800 occupations found that 45 percent of work activities could be automated using existing technology. DoD could save significant taxpayer dollars by taking advantage of these trends, piggybacking off private sector developments in automation and importing best practices into government. Successful reform of even one of the major defense agencies would provide significant savings to the department writ large as well as proof of concept for how defense reform can be scaled up across the enterprise.

Beyond this focus on defense agencies, Congress should also provide the Secretary of Defense with the necessary flexibility and "breathing room" to assess the degree of functional and organizational duplication across DoD headquarters writ large and to potentially restructure or consolidate entities, reassign personnel, and eliminate unnecessary functions or offices. Such flexibility should be paired with mutual agreement on expected cost savings and improvements in mission effectiveness and efficiency.

In order to facilitate the streamlining of DoD headquarters and agencies, Congress should give the Secretary authorities he needs to reshape the civilian workforce for the 21st century (as described in more detail below) and the ability to eliminate or consolidate organizations and infrastructure as needed. While it is certainly true that DoD has not made full use of some of the authorities Congress has recently provided (particularly in the acquisition arena), the current Secretary of Defense has not been given the types of authorities that some of his predecessors were given to reshape the DoD enterprise for new realities. For example, after the end of the Cold War, Secretary of Defense William Perry was given a broad range of authorities, including Reduction in Force authority, Base Realignment and Closure authority, and meaningful retirement and voluntary separation incentive pays, to reshape the DoD workforce and infrastructure amidst a substantial drawdown. Today's Secretary of Defense will need a comparable set of authorities – and more – to reshape the Department for the demands of a rapidly evolving, increasingly complex and challenging 21st century security environment.

Base Realignment and Closure

The Department of Defense is in desperate need of another round of Base Realignment and Closure (BRAC). DoD estimates that 22 percent of its current infrastructure capacity is excess to need, and the Service Chiefs have testified that this infrastructure overhang is diverting money from critical priorities like strengthening military readiness and investing in critical future warfighting capabilities. Based on past experience, the department estimates that it could save at least \$2 billion a year, and perhaps substantially more, if it were allowed to eliminate this excess infrastructure. Furthermore, such facilities are a low priority for the Department in an era of squeezed Operations and Maintenance budgets, and maintaining "keep the lights on" bases to a standard that preserves their value to the local community has become increasingly difficult. End strength reductions since the last BRAC round in 2005 have only exacerbated the gap between force structure and facilities; but even a modest increase in the size of the force would still leave a significant infrastructure overhang. The waiting game is likewise challenging for

local communities, limiting their ability to plan for and invest in the future. Lessons can certainly be learned from past BRAC processes to strengthen transparency, prioritize cost saving, enhance community support, and more clearly define military requirements in line with current and future challenges. But further delay will not make this any easier, and in some cases may actually make it more costly and more harmful to local communities.

Although the Obama administration repeatedly asked for authorization to begin planning for BRAC, Congress has, to date, rejected this request. Politically, BRAC has long been seen as a political “third rail” because of the job losses that are assumed to accompany the closure of bases and facilities. However, a number of analyses of past base closures have concluded that most jobs are replaced and most affected communities recover quite well. For example, a 2005 study by the Government Accountability Office looked back at the first four rounds of BRAC, which ended in 1995 and affected 73 bases, and found that about three-quarters of all lost jobs had been replaced. And in 1 in 3 of the bases, redevelopment after BRAC created more jobs than were lost. If Congress passes a nationwide infrastructure spending bill this year, directing some of this investment to affected communities might also help them through the transition and mitigate job losses associated with BRAC. The time for studying this issue has long past; what’s needed now is congressional action. Every dollar we spend on unneeded infrastructure is a dollar less to support the men and women who serve in harm’s way. I would urge Congress to provide the new administration with the authority to pursue another round of BRAC.

Reshaping and Reinvigorating the Civilian Workforce

Today, DoD employs 1.4 million military personnel and 770,000 civilian employees plus more than 800,000 part-time reserve personnel. DoD employees are augmented by a large number of contractors as well. DoD has launched multiple initiatives over the last 15 years to achieve cost savings and improve organizational effectiveness by downsizing personnel, streamlining bureaucracy, and reducing institutional redundancy. These efforts have met with some success. But many of the results have been short-lived, fallen short of original goals, or failed to achieve their full potential. Some of the requisite blame lies with DoD leadership for establishing metrics and targets for downsizing and delayering without an overarching strategy for reform – a critical step for the new administration. But Congress also has the opportunity to significantly enhance the new Secretary’s ability to enact permanent reforms and generate savings. The Trump administration’s current approach of instituting an across-the-board hiring freeze amounts to using a “meat axe” when one needs a scalpel: it effectively starves the Pentagon of new civilian talent even in areas deemed critical to the mission and creates a gap in the talent pipeline that is both harmful and costly over time.

There is a better way. Offering a package of authorities to streamline personnel, organizations, and infrastructure will provide much-needed flexibility to the Secretary of Defense.

Several key assumptions should inform this effort:

- Permanent savings are best achieved by eliminating work/functions, not just eliminating billets.
- Across-the-board percentage cuts to personnel are a blunt instrument that can be as harmful to the DoD human capital strategy as sequestration is to defense more broadly. But if targets must be applied, annual personnel costs rather than personnel numbers are a more effective metric to drive sustainable savings.

- Maintaining the ability to preserve and enhance value is as important as having the authority to eliminate waste.
- Savings may not be immediately realized – achieving permanent savings may require some up-front investment and take time to implement.

The following recommendations would enable the Secretary to comprehensively address known concerns about the size, cost, management layers, and duplicative organizations in the Department. Several of these authorities could be temporarily authorized for a limited period associated with DoD streamlining objectives.

Human Capital Strategy: Congress should direct the Secretary of Defense to develop a comprehensive human capital strategy for the Department, supported by strategies for each component across DoD, addressing how the civilian workforce will be recruited, developed and managed over the next five years. This is particularly important in a political climate in which many civil servants feel undervalued or even under attack. This should include an assessment of the optimal mix of military, civilian, and contractor personnel across the department and by function. (Of note, a recent study by the Congressional Budget Office found that shifting 80,000 positions from military to civilian personnel, and eliminating the military positions, could save the federal government \$3.1 billion to \$5.7 billion a year once fully implemented. Optimizing the mix of contractors and civilian employees would undoubtedly save money as well.) A Secretary-directed Human Capital Strategy that would inform DoD's planning, programming, budgeting, and evaluation process and determine the optimal mix of military, civilian, and contractor personnel would be a powerful enabler for reshaping the Department for the future.

Savings Targets: In consultation with the Secretary of Defense, Congress should establish targets for personnel cost reductions across the Five Year Defense Plan, offering the Secretary the flexibility to apply these across the organization based on requirements (rather than across the board cuts). Focusing on cutting cost, rather than percentage cuts in billets, incentivizes the Department to manage to the optimal mix of entry-level/mid-career/senior personnel, rather than preserving an imbalanced and expensive staff and severely limiting cost savings over time.

VSIP Reform: Significantly increase Voluntary Separation Incentive Pay (VSIP) and empower managers to offer this incentive directly to specific employees as an inducement to leave government service. Last year, Congress temporarily increased VSIP from a maximum of \$25,000 (which had been set back in 1993) to \$40,000 through 2018. This was a positive step, but more is needed to make this an effective instrument. Currently, a supervisor may deny VSIP, but may not offer it to specific employees based on their performance and the relative priority of their function. In addition to extending the broadly available VSIP beyond 2018, Congress should also create a much more substantial, targeted-VSIP authority that permits supervisors to offer – with leadership approval – up to one year of annual salary to induce specific employees to depart.

Encourage DoD to Use its Modified Reduction in Force Authority: Historically, attrition and other separation inducements generally prove too slow and astrategic to attain the desired mix of personnel based on functional requirements. But Reductions in Force (RIF) can be an equally blunt instrument. When generally applied, RIFs may not result in cost-savings, and can even result in few if any actual separations due to Priority Placement Programs. In the past, performance has weighed little in determining which employees are RIFed (tenure has been the top criterion). Fortunately, last year the Secretary of Defense was given a modified RIF authority that enables prioritizing the performance of

the individual among RIF criteria – a necessary component of allowing the Secretary the flexibility needed to dismiss lower-quality performers. To date, this authority has not been widely used. Congress should strongly encourage DoD to use this modified authority to help reshape and strengthen the civilian workforce for the 21st century.

Reassignment and Hiring Flexibility: Congress should eliminate any statutory barriers to the Secretary of Defense reallocating and reassigning personnel to where mission need is greatest, and to authorizing the Department to hire and retain high-performing individuals as organizational changes are implemented. Congress took some initial steps in this area in the FY17 NDAA, but this may not be enough. There is a widespread view that the 66 different personnel systems currently being used in the DoD hamper the Department’s ability to adapt to today’s security environment and provide the best possible support to the military. Indeed, a recent report by the Bipartisan Policy Center recommends a wholesale transition to a Title 10 hiring authority “to allow the defense secretary to customize a system to control hiring, management, compensation, and retention policies for the defense-civilian workforce.” While the particulars of this far-reaching step deserve more analysis, the rationale for doing so is compelling: “The Defense Department needs a comprehensive set of hiring and personnel-management authorities that enable it to acquire, develop, and retain its civilian workforce” – and today’s are not up to the task, regardless of whether the civilian workforce grows larger or smaller.”ⁱⁱ

Preserve flexibility for new hires, rewarding talent, and professional development: Cost-saving objectives should not constrain the Department’s ability to bring on new talent in high priority areas or use its resources to develop and reward high-performing talent. Of note, younger workers are already underrepresented in the defense workforce compared with the American workforce. It is, therefore, imperative to preserve the authority and resources for DoD to make targeted new hires in priority areas and to continue to invest in priority professional development efforts. Organization-wide hiring freezes should be avoided like the plague.

Allow DoD to reallocate a portion of savings from reform and business transformation efforts to invest in high-priority areas, such as innovation. As the Secretary drives reform and business transformation throughout the department, assigning accountability to business units, tracking cost data, and changing the “budget culture” (in which organizations throughout DoD are incentivized to spend down their budgets at the end of a fiscal year lest they face a pared-down budget the following year), the process should yield savings for the Department. Congress can both incentivize efficiency and drive innovation by expanding reprogramming authorities for DoD to redistribute a portion of demonstrated savings toward high-priority areas like innovation and modernization.

Over the coming years, Congress should also examine more fundamental changes to the DoD civilian personnel system to enhance recruitment and professional development of the next generation of civil servants, tie pay and promotion opportunities more closely to performance, allow for greater flexibility in career paths, and create more effective measures to reward high performers and dismiss low performers.

Improving the Quality of Health Care while Reducing Costs

The costs of the Military Health System have nearly doubled over the past decade, with the Congressional Budget Office estimating an additional \$40 billion in costs by 2030. What’s more, survey data suggests that the quality of care received by military personnel and their families remains uneven and customer satisfaction is below the civilian benchmark in key areas. DoD should, therefore, explore

and implement ways of improving the quality of care while also reducing costs where possible, leveraging approaches such as value-based health care.

Former DoD Comptroller Bob Hale recently published an excellent CNAS report on defense reform in which he identified five priority areas of health care reform that should be considered, including wartime readiness, value-based reimbursement, utilization of services, productivity, and availability of choice.ⁱⁱⁱ

Wartime readiness. The Military Compensation and Retirement Modernization (MRCM) Commission concluded that the types of medical care in highest demand in peacetime (such as maternity and newborn care) do not allow DoD doctors to develop and hone the trauma skills they need on the battlefield. The commission recommended both organizational changes and a new law requiring that DoD maintain essential medical capabilities needed for war. This would almost certainly require DoD to pursue new approaches such as enabling more of its doctors to do rotations in civilian medical trauma centers.

Value-based reimbursement. Medicare and many private-sector health care insurance plans are moving toward provider reimbursements that are directly linked to the health and well-being of their patients rather than the volume of care provided. With value-based reimbursement, doctors are paid based on the health outcome rather than the number of office visits or tests provided. Given the positive results being achieved in civilian healthcare – better health outcomes at lower costs – DoD should be a “fast follower” and move expeditiously toward a value-based health care approach, as required in the Senate’s proposed authorization language for 2017.

Utilization of services. Utilization of medical services by military retirees and dependents under TRICARE exceeds civilian benchmarks by about 40 percent. This has created substantial and unsustainable growth in the government’s share of TRICARE costs. DoD has proposed modest increases in co-pays designed to reduce overutilization and help make this valuable program more sustainable. Congress should also consider legislation that would make TRICARE secondary insurance for beneficiaries who have access to health care insurance through an employer.

Productivity. A recent Senate Armed Services Committee report assessed that the productivity of military medical providers is unreasonably low compared with civilian providers. In addition, many medical studies have shown that doctors who undertake certain procedures with greater frequency achieve better outcomes for their patients, enhancing the quality of care. Increasing the productivity of military providers will likely require a combination of measures, from incentivizing greater use of military treatment facilities while also reducing and consolidating the number of facilities, realigning some while closing others and filling any resulting gaps with contracted care.

Availability and choice. The MCRM Commission and several surveys of service members have found that military health care beneficiaries want greater choice of providers and better availability of care. The commission recommended creating a menu of insurance choices for military beneficiaries who use private-sector care similar to the one now available to federal civilian employees.

High-quality, affordable military health care is critical to warfighting, maintaining satisfaction among military members and their families, limiting cost growth, and “keeping faith” with those who serve. Continued reform of the military health care system should be a top priority on the defense reform agenda.

Conclusion

The ability of this Secretary of Defense to be more effective in reforming the DoD enterprise will depend in large part on the authorities, flexibility, resources, and political support provided by this Congress. Now is the time to provide the new Secretary of Defense with the tools and support needed to enhance the Department's performance and free up resources to reinvest in the priority capabilities the U.S. military will need to protect this nation in the future.

But as you assess various options and develop the next chapter of your reform plan, I would urge you to heed three notes of caution. First, it is imperative that we think through the second and third order effects of any changes proposed. In the balance hangs the people, capabilities, and performance of the finest military the world has ever known and our ability to secure our nation going forward. Great care should be taken to hear the full range of views and consider the unintended consequences of proposed reforms.

Second, based on my experience in both government and the private sector, I would warn against assuming that every problem can or should be solved by organizational change. Too often we jump to redrawing the lines on an organizational chart when a more powerful solution might lie in clarifying roles and responsibilities, better aligning authorities, or strengthening incentives and accountability to change behavior.

Third, however successful future reform efforts may be, they are unlikely to yield enough cost savings to bring U.S. defense spending to the levels required to protect this nation given the nature of the security environment we face. It is my hope that, in addition to pursuing critical defense reforms in the coming year, Congress will also consider how to establish more predictable and robust levels of defense spending over the coming 5-10 years without gutting diplomacy and development accounts that are also critical to our national security.

This period of investment could not be more important: it will determine whether the United States can maintain its technological edge and its military superiority over increasingly capable state and non-state actors who are determined to constrain our ability to project power and maintain freedom of action in regions vital to our national security. The Department of Defense simply cannot afford to return to the type of budget uncertainty that has wreaked havoc in recent years – living within the constraints of continuing resolutions, under the threat of sequestration, and with the risk of government shutdowns. The costs of this uncertainty are enormous and they have challenged the Department's ability to set and maintain a strategic course. In short, reaching a comprehensive budget deal that includes all of the obvious elements – tax reform, entitlement reform, and smart investment in the drivers of U.S. economic vitality and growth – is not only an economic imperative, it has become a national security imperative.

Finally, I hope that through the dialogue that this committee is fostering, the Congress and the executive branch will be able to partner more closely to make the hard choices and undertake the reforms that will be necessary to ensure that we keep faith with the men and women who serve in the best trained, best equipped fighting force in the world. They deserve nothing less.

Thank you.

ⁱ Major General Arnold L. Punaro, USMC, Ret., “The Urgent Need To Reform And Reduce DoD’s Overhead And Infrastructure,” Statement to The Senate Armed Services Committee, November 17, 2015, 9, 13, https://www.armed-services.senate.gov/imo/media/doc/Punaro_11-17-15.pdf.

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“Building a F.A.S.T. Force: A Flexible Personnel System for a Modern Military Recommendations from the Task Force on Defense Personnel,” (Bipartisan Policy Center, March 2017), 62, <https://cdn.bipartisanpolicy.org/wp-content/uploads/2017/03/BPC-Defense-Building-A-FAST-Force.pdf>.

ⁱⁱⁱ Robert F. Hale, “Business Reform in the Department of Defense: An Agenda for the Next Administration,” (Center for a New American Security, November 30, 2016) ,<https://www.cnas.org/publications/reports/business-reform-in-the-department-of-defense>.



MICHÈLE FLOURNOY is Co-Founder and Chief Executive Officer of the Center for a New American Security (CNAS).

She served as the Under Secretary of Defense for Policy from February 2009 to February 2012. She was the principal adviser to the Secretary of Defense in the formulation of national security and defense policy, oversight of military plans and operations, and in National Security Council deliberations. She led the development of DoD's 2012 Strategic Guidance and represented the Department in dozens of foreign engagements, in the media and before Congress.

Prior to confirmation, Ms. Flournoy co-led President Obama's transition team at DoD.

In January 2007, Ms. Flournoy co-founded CNAS, a non-partisan think tank dedicated to developing strong, pragmatic and principled national security policies. She served as CNAS' President until 2009.

Previously, she was senior adviser at the Center for Strategic and International Studies for several years and, prior to that, a distinguished research professor at the Institute for National Strategic Studies at the National Defense University (NDU).

In the mid-1990s, she served as Principal Deputy Assistant Secretary of Defense for Strategy and Threat Reduction and Deputy Assistant Secretary of Defense for Strategy. She has received several awards from the Secretary of Defense and the Chairman of the Joint Chiefs of Staff.

Ms. Flournoy is a former member of the President's Intelligence Advisory Board, the Defense Policy Board, and the DCIA's External Advisory Board, and a current member of the Council on Foreign Relations and the Aspen Strategy Group. She is also a Senior Fellow at Harvard's Belfer Center for Science and International Affairs, serves on the boards of The Mitre Corporation, CSRA, Amida Technology Solutions, The Mission Continues, and CARE, and is a Senior Advisor at the Boston Consulting Group.

Ms. Flournoy earned a bachelor's degree in social studies from Harvard University and a master's degree in international relations from Balliol College, Oxford University, where she was a Newton-Tatum scholar.