REFORMING MILITARY INSTALLATIONS — CAN THEY OPERATE MORE LIKE THE PRIVATE SECTOR?
When Department of Defense (DoD) leaders invoke defense reform, what they often mean is that they want to get more for less, with the assumption that Federal budgets are inefficient and that the private sector could accomplish the same mission more effectively. It’s hard not to agree when you look across more than a trillion dollars of defense infrastructure and recognize that it is carrying a maintenance backlog in excess of $115 billion, with a third of all facilities in poor or failing condition and getting worse.¹

The bright spot is privatized housing. There are important issues regarding how the private sector providers are handling maintenance and repair, and, in response, Congress and DoD will address oversight of base housing and make tenants’ rights clear. However, family housing on our military bases is in far better condition than it was before DoD privatized. Part of the reason this program worked so well was that the market worked its will. No service member was required to live on base — the developers had to attract them with higher quality housing and invested in the housing accordingly.

Turning back to the rest of the base and that $115 billion maintenance backlog (which doesn’t include the long list of new facilities that never get construction funding), you find a management structure replete with misaligned incentives. The military forces that occupy facilities (“operating forces”) do not pay for them directly. Their demand for facilities is unconstrained by the need to pay the bill and to articulate their facility needs clearly. DoD’s facility organizations are resourced to maintain the current building stock based on square footage, not on military requirements, and that funding is purposefully budgeted at levels below projected requirements. Under this rubric, there is no clear link between the operating forces’ highest priority facility requirements and the facility organizations’ ability to provide them.

While some terrific facilities exist at many military installations to be sure, generally the results of the status quo arrangement produce a suboptimal facility portfolio that reduces

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¹ Understanding Market Incentives
readiness and degrades operations. By and large DoD has too many facilities, poorly utilized facilities and an unacceptable number of facilities in poor condition.

Outside the fence line, DoD does lease some facilities. The characterization most often made about these facilities is “expensive.” On base, DoD-owned facilities are cheaper, and often defense reform initiatives press for units to move back on base. Part of the reason they’re cheaper, however, is that DoD underfunds operations and maintenance of those facilities. The private sector understands that undermining the quality and condition of its assets is not an effective long-term business strategy. The cost of occupying leased facilities — the cost per square foot — incorporates the cost of maintenance and recapitalization.

**Adopting a Business-Inspired Approach**

What would happen if DoD adopted a business-inspired approach inside the fence line? Could it realign incentives? From a practical perspective, we don’t think it makes sense to privatize operational facilities, but some of those private sector practices could be used to reshape the relationship between those government entities that manage the Department’s real property assets and those that occupy them.

We propose that DoD consider a three-part strategy to transform facility management and better align budgets and facility requirements for DoD forces, all based on commercial and DoD best practices.

First, restructure the fiscal incentives by using Working Capital Funds to manage DoD facilities. The Secretary of Defense has existing authority to establish such funds, which offer flexibility not available under standard budget and spending arrangements. Instead of separately budgeting for facilities maintenance in operating accounts which are easily trimmed when budgets are tight, the funds would be provided to operators who would then decide which facilities they could afford — with the prices set so that the Department’s real property assets could be counted on to perform over the long term. The funds would be deposited into these working capital funds, from which maintenance and repairs would be funded. This approach has...
other advantages, such as the fact that working capital funds don’t expire at the end of the fiscal year, allowing facility managers to avoid the rush to obligate funds at the end of each fiscal year, often subjected to mark-up by those who know the funds will soon expire.

Second, establish landlord organizations within DoD to be the asset managers. They would set rental costs (ostensibly by the square foot) that tenants (operating forces) would pay to use the space. Facility organizations would have to become more savvy providers, maximizing the services they provide for the dollars available. Operating forces would have to become more savvy facility buyers. They would hold the purse strings and, through the marketplace created by the internal working capital funds, procure the facilities that best meet their military facility under a constrained budget. Market forces would begin to impact not only the quality of facilities, but the appetite for them.

Finally, in order to avoid the anxiety associated with loss of control, this approach would require each military service to retain control of its own facilities rather than cede them to an external entity. The Military Services each have their own unique operating and facility requirements, and ultimately, facilities managers would still be answerable to their Service leadership rather than to the bottom line.

The concepts behind this transformation are well established. DoD has operated working capital funds for decades. Landlord-tenant relationships, establishing service standards and pricing facility occupancy by-the-square-foot form the foundation of the General Services Administration’s approach to providing facilities for most non-Defense federal agencies, and, indeed, for the entire global commercial real estate market.

We acknowledge that there will be risks and complexities in executing the transformation. For example, the Military Services must get the
BY BETTER ALIGNING INCENTIVES, AVAILABLE FUNDING AND FACILITY SUPPLY AND DEMAND, DOD WILL MOVE TOWARD A FACILITY PROFILE THAT IS IN BETTER CONDITION, BETTER MEETS MILITARY REQUIREMENTS AND INCREASES READINESS.
per-square-foot costs and space standards right or the markets won’t work efficiently. And there are nuances around the new facility budgets for operating forces and other installation tenants. To address these risks, DoD would need to test this concept in both tabletop exercises and limited-scale pilots before implementing more broadly.

Without correcting today’s misaligned incentives, we fear that DoD facilities will continue on their current trajectory, with the attendant risks to readiness and mission degradation. The status quo is not good for our military, and some of the solutions frequently suggested, such as a new base closure round to foster efficiency or vastly increased facility budgets, are unlikely to materialize in the near term, if ever.

**Improving Outcomes**

We are confident that by implementing this arrangement to better align incentives, available funding and facility supply and demand, DoD will move toward a facility portfolio that is in better condition, better meets military requirements and increases readiness. As facility buyers, operating forces will be more selective about the facilities they occupy and use them more efficiently (because they are paying for each square foot they occupy). As facility providers, facility organizations will have to improve their responsiveness to their customers and maintain their facilities to agreed-upon standards.

This approach would appear to fly in the face of defense reform efforts that demand more for less, as inevitably in the short term it would provide fewer facilities for more expense. But that’s the short-sighted view. It would immediately drive increased quality. It would ensure more scrutiny of requirements. The long-term management of real property assets would, like in the private sector, be more cost-effective than willfully underfunding maintenance and driving down quality and capability. Just like you don’t really save money by skipping oil changes in your car, the Department isn’t really saving money by underfunding facility maintenance.

For decades, DoD has sought to integrate the best practices that the private sector has to offer into the defense acquisition process. The time is now to do the same for the defense facilities process.

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NOTES

   Apr. 26, 2018. 115th Cong. (statement of Honorable Lucian Niemeyer,  
   Assistant Secretary of Defense, Energy, Installations and Environment):  
   https://www.appropriations.senate.gov/imo/media/doc/042618%20-%20Niemeyer
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