

# DEFENSE BUSINESS BOARD



## Selecting Senior Acquisition Officials

Assessing the Current Processes and Practices for Recruiting, Confirming, and Retaining Senior Officials in the Acquisition Workforce

April 21, 2016

# Task Group

“[T]he committee directs the Chair of the Defense Business Board to conduct a study of the effects of current mandates and processes regarding the determination of suitability for the selection of senior officials in the acquisition workforce...[and] further directs [the Board]...to provide recommendations to improve the Department’s ability to recruit, develop, and retain highly qualified senior acquisition personnel while appropriately mitigating real and perceived conflicts of interest.”

*- Report 114-102 on H.R. 1735 (P.L. 114-92, signed 25 Nov 15)*

## Terms of Reference (TOR)

### ■ **Selection of Senior Officials in the Acquisition Workforce**

- Consider ethics rules, congressional committee rules, and other statutory requirements
- Recommendations to:
  - Improve the depth and breadth of skills within the civilians who execute and oversee the Department’s acquisitions process
  - Increase the appeal for private sector experts to accept Presidentially-appointed, Senate-confirmed Senior Acquisition positions
  - Re-validate the conflicts of interest and risk mitigation rules

# Task Group

## Problem Statement and Process

Numerous hurdles must be overcome in order for the Department of Defense to appoint individuals as Senior Acquisition Officials:

- Outdated ethics rules that no longer match the current environment
- Costly financial divestitures for the nominees
- A nomination and confirmation process that is imbued with excessive amounts of paperwork/lengthy reviews and uncertain outcomes

The result is a process that has become highly focused on selecting individuals who can get through it, rather than finding individuals who are the best qualified.

*How can these hurdles be reduced?*

*How can the Department increase the attractiveness of service in its acquisition workforce and enhance its capacity to conduct acquisitions?*

### ■ To fully explore this, the Task Group worked to:

- Understand the desired skillsets necessary for key confirmed positions
- Understand the hurdles to service (i.e. restrictions & financial disincentives, Executive recruitment & vetting, confirmation & appointment process, post-service restrictions, etc.)
- Assess/validate the current conflicts of interest rules and post service employment restrictions
- Formulate recommendations

### Task Group Members

- Mr. Michael Bayer (Chair)
- Mr. Jerry Hultin
- Mr. Arnold Punaro
- Capt James D'Itri, Jr., USMC (DBB staff)



# Previous Efforts

- ***Making Senior Government Service More Attractive***, Business Executives for National Security (BENS), May 2015
- ***Linking and Streamlining the Defense Requirements, Acquisition, and Budget Process***, Defense Business Board, April 2012
- ***The Federal Appointments Process: The Problem and Our Proposed Solutions***, The Aspen Institute, March 2012
- ***Strengthening Administrative Leadership: Fixing the Appointments Process***, National Academy of Public Administration, 2012
- ***A Half-Empty Government Can't Govern: Why Everyone Wants to Fix the Appointments Process, Why It Never Happens, and How We Can Get It Done***, The Brookings Institute, December 2010
- ***Waiting for Leadership: President Obama's Record in Staffing Key Agency Positions and How to Improve the Appointments Process***, The Center for American Progress, April 2010
- ***Ready to Govern: Improving the Presidential Transition***, Partnership for Public Service, January 2010
- ***Department of Defense Political Appointments***, RAND Corporation, 2001
- ***To Form a Government: A Bipartisan Plan to Improve the Presidential Appointment Process***, The Brookings Institute, 2001

# Bottom Line Up Front

- The nation is at the opening stages of two near-peer competitions whose long-term outcomes will be determined, in part, by ***the ability of the Department of Defense to deliver cutting-edge innovation to its warfighters far faster than it has ever done***
- Most crucial in this long competition is the Department's ***top Acquisition & Technology leadership***
- The type of individuals best suited to excel in these most senior Acquisition positions is ***fundamentally different than in the past, and near impossible to recruit given the current ethics and confirmation rules***
- There is a need to ***open the recruiting window to a broader group*** that will enable the Department to have the best people for these technology-dominant innovation and manufacturing jobs
- Further, there is a need to not just 'tune up' the ethics and conflicts process, but rather ***establish a separate enabling ethics and conflicts architecture***

# Key Observations

# Rapidly Changing Environment

## Technology:

### – 1960s / 1970s:

- An Industrial Age Department matched the Industrial Age private sector
- Similar, relatively modest pace of innovation and tech refresh cycles that exceeded peer enemy
- Comparatively understandable manufacturing methods

### – 2015 & beyond:

- An Industrial Age Department with an Information Age private sector – the Department is trailing the private sector
- 2<sup>nd</sup> and 3<sup>rd</sup> order implications of Moore's Law (exponential growth in technology's capability) disrupting conventional markets
- Delivering breakthroughs in: autonomous systems, synthetic biology, nano-technology, metamaterials, social behavior, etc.

## Key Observations

# Rapidly Changing Environment

- Two dissimilar peers have emerged in competitions with the U.S., ***the outcomes of which will be largely determined by the innovations of a very few***
- The U.S. response are initiatives like the ***Third Offset***
  - A series of strategies based on increasing ***our ability to create and more rapidly deploy complexity*** better than our enemies
  - Innovation-driven/enabled, with the aim to ***reassert*** America's military technological edge against more dynamic, influential opponents

**New skillsets are necessary to ensure the success of the Third Offset Strategy.**

# Key Observations

# Shifting Senior Acquisition Experience

## 1960s / 1970s

Physicists/scientists at Berkeley Radiation Laboratories  
Directors of Lawrence Livermore National Laboratories  
Physicists at Harvard's Radio Research Laboratories  
Member of Canadian Nuclear Power Project  
President & Founder of Electromagnetic Systems Lab, Inc.  
Director of Electronic Defense Lab of Sylvania/GTE  
Scientists at Beckman Instruments  
Earned Ph.D. in Physics at age 21  
Members of the Manhattan Project  
Mathematicians  
Nuclear Physicists  
Businessmen  
Engineers

## 2000s / 2010s

Deputy Asst. Secretary of Defense for Material Acquisition  
Asst. Director of Defense Research & Engineering  
VP of ITT  
Under Secretary / Secretary of the Air Force  
Director of the National Reconnaissance Lab  
President of Electronic Systems Company (McDonnell Douglas)  
CEO of Aerospace Corporation  
VP of International Paper  
Lockheed Martin Aeronautics  
SAC-D Professional Staffer  
Theoretical Physicist, Lawyers, Professors, Rhodes Scholars  
Asst. Secretary of Defense for International Policy  
Amnesty International, Human Rights First, Tahirih Justice Center



# Different Compensation for Different Times

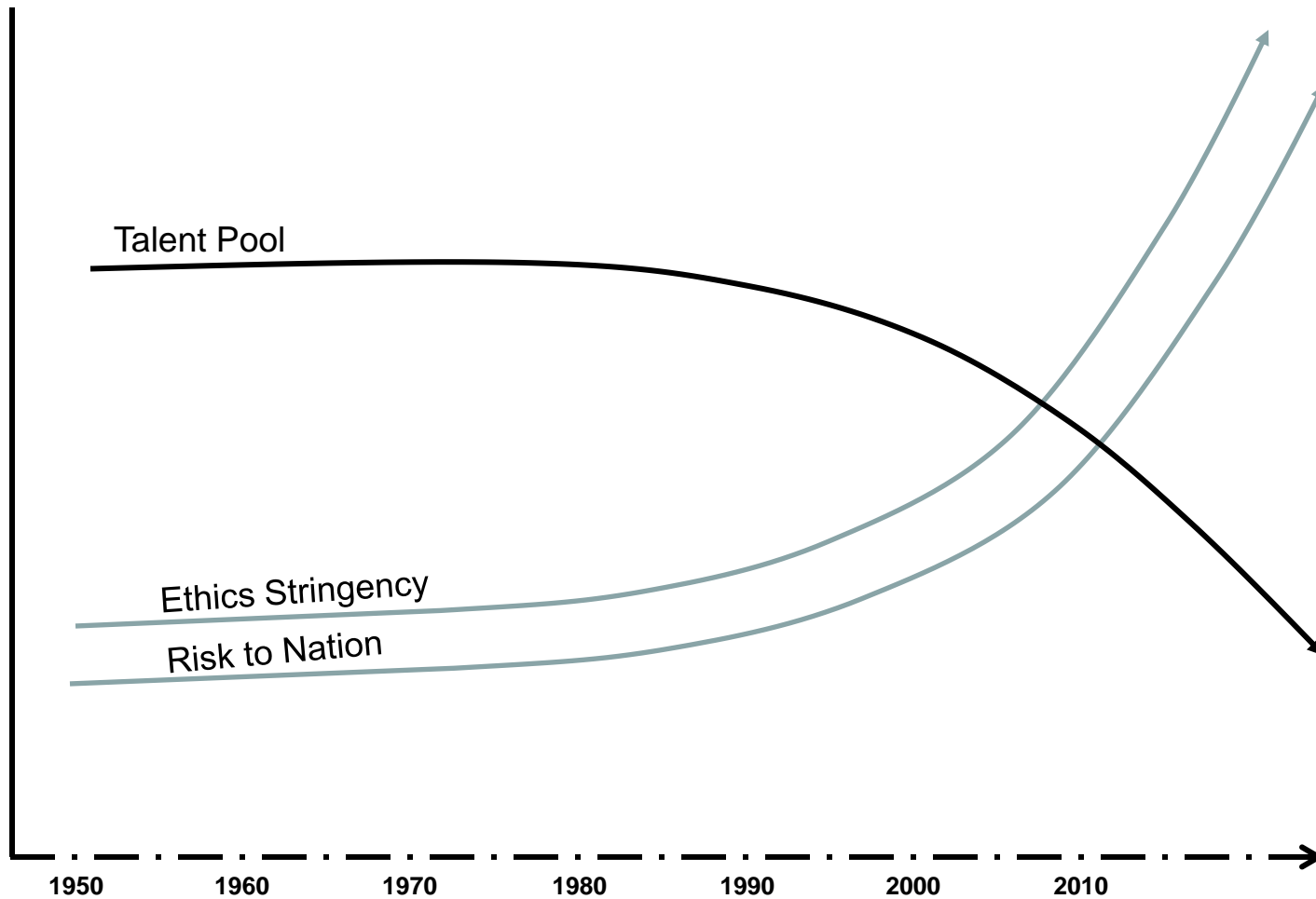
### Then...

- Focus primarily on productivity and profitability in a largely U.S.-dominant domestic marketplace
- Compensation composed mainly of cash that was largely tied to seniority and performance
- Deferred compensation not then best practice
- Existing equity awards were in vested stock, making divestiture easier and less painful

### Now...

- While productivity and profitability are still paramount for determining salary:
  - Total compensation is dramatically higher from performance incentives in deferred equity
  - Majority of compensation is now stock, options, or other long-term structured equity packages that frequently have vesting or 'hold' periods
  - Divestiture of non-vested/deferred equity is very complicated, and often results in a loss of significant personal and family wealth

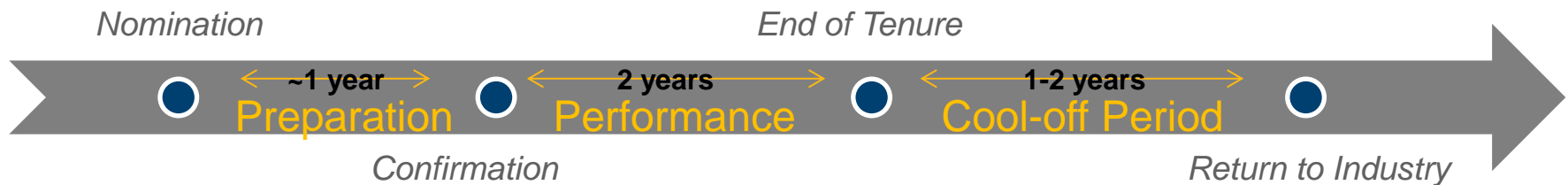
# Key Observations Trends in Defense Acquisition



# Key Observations

## Process Disincentives

- Average term of service for the USD in charge of Acquisition = 2 years
- Total impact of up to five years for an average of less than two years of service for an acquisition appointee
  - Preparation: White House Clearance, Confirmation
  - Performance: Time in the job
  - Cool-off Period: Post-employment restrictions
- Burdensome amount of paperwork in both Executive and Legislative processes
  - SF-86 for clearance, SF-278 (financial disclosure), tax returns, past speeches, written work, controversial electronic posts, travel documentation, Senate-required paperwork, Advance Policy Questions (APQs)
- Post-employment restrictions materially impact earnings potential and reduce the likelihood of repeat government service



**Highly qualified private sector personnel see too little return on investment for the time devoted, earnings sacrifice, and reputational risk.**

## Key Observations

# Financial Disincentives

- **Substantial pay-cut for private sector individuals with requisite experience**
  - The pay gap between senior executives in the best performing entities in the private sector has widened exponentially
  - The USD(AT&L) position is an Executive Level II, capped at \$185,100
  - Other DoD Highly Qualified Expert (HQE) positions are capped at Executive Level III or \$170,400
  - Government-wide Critical Position Pay Authority (CPPA) is authorized ***only in rare cases*** per 5 U.S. Code 5377, and is capped at \$205,700 (Executive Level I)

## Key Observations

# Financial Disincentives (continued)

- Substantial costs associated with the required complete divestiture
  - Need to hire lawyers at significant cost to deal with paperwork and complexities
  - Must dispose of stock or options in companies with DoD contract awards of \$25K or more (roughly 33,600 companies in FY 2015)
  - SASC restricts ability to use blind trusts
  - No ability to hold underwater stock or options
  - Immediate tax on capital gains, unless basis carried forward in a ‘diversified investment fund’ or U.S. treasuries
  - Divestiture results in a material reduction in personal and family net worth
- Potential loss in earned corporate retirement, and will not serve long enough to vest in any government retirement
- Onerous post-government restrictions that preclude covering/re-earning losses

**All are disincentives to attracting the best and brightest of private sector acquisition expertise.**

# Examples of Superfluous Divestiture

- **An annually updated list of companies with Defense contracts valued at or above \$25K details stocks that cannot be held by PAS officials**
  - The current list contains roughly 33,600 companies
  - Such a large number of prohibited companies produces some remarkable outcomes
  
- **Examples of mandated divestitures:**
  - **A Secretary of the Navy:**
    - Starwood Hotels
  - **An Assistant Secretary of Defense for International Security Affairs:**
    - Disney
  - **An Under Secretary of Defense for Policy:**
    - AT&T
  - **A Secretary of the Army:**
    - American International Group
    - Berkshire Hathaway
    - Citigroup
    - Coca-Cola
    - Pepsicola
    - Comcast Vodaphone
    - Viacom
    - Merck
    - Pfizer
    - Wells Fargo
    - AOL-Time Warner
  - **An Under Secretary of Defense for Comptroller:**
    - Berkshire Hathaway
    - Gillette
    - Wells Fargo
  - **A General Counsel of the Department of Defense:**
    - AOL-Time Warner
    - Coca-Cola
    - Disney

In recent Presidential transitions, an overwhelming number of nominees were required to divest stock – often resulting in loss of a bulk of their portfolios.

# Key Observations

## The Current Ruleset

- OGE guidelines provide narrow, ‘one-size-fits-all’ rules despite difference in responsibilities
  - **Criteria:** “Each officer or employee in the executive branch, including a special Government employee...whose position is classified above GS-15...or the rate of basic pay for which is fixed, other than under the General Schedule, at a rate equal to or greater than 120% of the minimum rate of basic pay for GS-15 of the General Schedule; each member of a uniformed service whose pay grade is at or in excess of O-7...and each officer or employee in any other position determined by the Director of the Office of Government Ethics to be of equal classification.” **Ethics in Government Act of 1978**, Title 5, U.S. Code, §2634.202
  - **Federal conflicts of interest and related ethics laws are part of Title 18, U.S. Code**



vs.

The rest of Federal Government

- DoD:
  - Requires extraordinary technical competency that only exists in industry
  - Leadership must have at-scale management experience
  - Outputs are of enormous consequence
- The rest primarily create policy and administer federal programs
  - **There is a difference in the ‘risk calculus’ between functions**

Today’s rules are solutions to yesterday’s problems.

# Risk Minimization in Acquisition

## Primary Sources:

- Government Ethics Rules
- Senate Rules

## But, there is also redundancy:

INTERNAL

- Defense Contract Audit Agency
- Defense Contract Management Agency
- Office of the Inspector General
- Program Managers

EXTERNAL

- Government Accountability Office
- Press



## Key Observations

# The Confirmation Process

- Anchored in precedent and tradition
  - Senate Armed Services Committee (SASC) strictures dating back to the 1970s are much more restrictive than the Office of Government Ethics
  - Does not allow recusals permitted under law
  - ‘No recusals’ requires total divestitures by the nominee and family
- No adjustments for today’s compensation packages or current market conditions
- Even when approved by the SASC, the Committee is unable to ‘control’ or ‘cajole’ fellow lawmakers out of ‘holds’ which can run from months to years to indeterminate

# Key Observations

## Post-employment Restrictions

- **Procurement Integrity Restrictions:**
  - Cannot accept compensation, for a period of one year from a designated date, from a DoD contractor that has been awarded a competitive or sole source contract in excess of \$10M, if the former official served or acted as:
    - Procuring contracting officer, source selection authority, source selection evaluation board, or chief of financial or technical evaluation team
    - Program Manager, Deputy Program Manager, or Administrative Contracting Officer
    - Officials who personally made the decision that impacted a contract in excess of \$10M
- **Ethics Commitments by Executive Branch Personnel:**
  - Executive Order 13490
  - Extends ‘cooling-off’ period for communications with former executive agency to **two years**
  - ‘Revolving door’ ban on lobbying any covered executive branch or non-career SES appointee for remainder of the Administration

**Previously, Senior Acquisition positions were commonly filled by older individuals near the end of their private sector career, having made a significant amount of money, and looking to ‘give back.’ Today’s most relevant, innovative ‘best and brightest’ may only be in their 40s or 50s, and have a substantial portion of their earnings potential ahead of them (post public service).**

# Key Observations

## Qualification Standards in Law

### The top jobs in Defense for Acquisition, Technology, and Logistics are spelled out in Title 10, U.S. Code

- The law does list complex, technical roles and responsibilities that the Under Secretary must fill (among other things):

“Establishing policies for acquisition (including procurement of goods and services, research and development, developmental testing, and contract administration)...”

“Establishing policies for logistics, maintenance, and sustaining support...for maintenance of the defense industrial base...”

“The authority to direct the Secretaries of the military departments and the heads of all other elements of the Department of Defense with regard to matters for which the Under Secretary has responsibility...”

“...is the Defense Acquisition Executive for purposes of regulations and procedures of the Department...”

“...exercises overall supervision of all personnel...in the Office of the Secretary of Defense with regard to matters for which the Under Secretary has responsibility...”

“...shall prescribe policies to ensure that audit and oversight of contractor activities are coordinated and carried out...”

- But, the law contains scarce guidance in necessary backgrounds/qualifications, particularly after being modified by the National Defense Authorization Act for Fiscal Year 2008 (P.L. 110-181):

*“The Under Secretary shall be appointed from among persons who have an extensive management background ~~in the private sector.~~”*

# Summary of Observations

- Salary differential
- Cost of compliance
- Loss of net worth
- Eight years of commitment for less than two years of service

***This results in the current available pool of executives being increasingly:***

- Current government employees
- Academics
- Lawyers

***While the pool shrinks for:***

- Innovators
- C-Suite experience
- High tech
- Large-scale operations

# Recommendation: Qualification Standards

## Identify the minimum baseline qualifications for key Acquisition positions.

- **Focus on:**
  - USD(AT&L) and PDUSD(AT&L)
  - 3x Service Acquisition Executives
- **Build from the Packard Commission as a baseline**
  - The 1986 Packard Commission Report identified the Department's need to "attract and retain the caliber of people necessary for a quality acquisition program"
- **Expand the population of the Department's senior leadership beyond just the Defense Industrial Base**

# Recommendation: Qualification Standards

## Qualification Examples: USD(AT&L)

**The following criteria shall be used as key qualifiers when considering appointments to the positions of USD(AT&L):**

- Significant experience in the management and oversight of large-scale manufacturing and/or acquisition in a highly technical sector of private industry
- Noted achievements in driving and gaining breakthroughs from cutting-edge innovation in areas such as: autonomous systems, synthetic biology, nanotechnology, metamaterials, social behavior, etc.
- An extensive management background and proven track record leading large-scale enterprises in innovation
- At the top of their “peer group”

# Recommendation: Pay and Compensation

**Implement an alternative pay and compensation structure to make the Senior Acquisition positions more attractive.**

- **Implement a similar calculation used by DHHS and VA for various Title 38, Health Care positions, which are capped at \$385,000 (aggregate pay), to offer an attractive and competitive rate of pay and compensation for Senior Acquisition positions**

# Recommendation: Rules Adjustment

**Mitigate complicated and costly financial divestment requirements that greatly reduce individual and family net wealth.**

- **Provide more options to allow avoidance of capital gains at time of appointment for sales of stocks when divestiture is required for appointment**
  - Current certificate of divestiture is helpful, but not desirable in some cases
  - The current rules provide no solution for the loss of value due to divestiture of ownership in options of closely-held and early-stage companies
- **Simplify the blind trust requirements**
  - Only *major* Defense stocks must be sold and over 5% holdings of possible non-traditional companies
  - Allow funds to be invested in government pension fund basket of stocks



# Recommendation: Rules Adjustment

**Establish a new set of rules and procedures that relate to today's ethics landscape, easing the ability to move between the public and private sector.**

- **Recognizing the existential nature of multiple peer competitions, the Nation needs a unique ethics construct that enables recruiting of the talent needed for peer-on-peer**
- **Recognizing that the 'revolving door' in this new world is indispensable for the Department to find, and later re-recruit, the very best talent we envisage necessary to win these peer competitions**
- **Recognizing there are multiple oversight regimes within the acquisition process and the Department writ large, establish a unique set of ethical standards for those acquisition positions that are best served by 'successful innovators and builders'**

# Recommendation: Rules Adjustment

## Employ a more balanced OGE approach for crucial jobs in DoD.

- **An alternative means of controlling risk is to employ policies and practices that mitigate/control such risk after the official is appointed – as conducted in the American judicial and prosecutorial systems, law firms, and investment banking firms of the U.S.**
- **The recusal process should include a method of obtaining advanced or prospective rulings as to whether the possible conflict is considered material and a suggested method of reducing/eliminating the conflict**
- **Create a practice of providing safe-harbor status to any matter that receives a prospective ruling**
- **Consider the combined use of full disclosure, Chinese walls, and compliance staff**

# Recommendation: Confirmation Process

**Adjust SASC requirements and procedures to make it more attractive to positions requiring highly experienced, technically qualified, proven senior leaders from the private sector.**

- **Minimize financial disincentives by reinstating the use of blind trusts, and simplifying blind pool requirements**
- **Manage capital gains from required divestiture by using a delayed procedure**
- **Alleviate restrictions on returning to industry**
- **The Senate should institute expedited procedures for acquisition-related nominees reported favorably by the SASC**

# Recommendations Summary

1. Identify the minimum baseline qualifications for key Acquisition positions
2. Implement an alternative pay and compensation structure to make the Senior Acquisition positions more attractive
3. Mitigate complicated and costly financial divestment requirements that greatly reduce individual and family net wealth
4. Establish a new set of rules and procedures that relate to today's ethics landscape, easing the ability to move between the public and private sector
5. Employ a more balanced OGE approach for crucial jobs in DoD
6. Adjust SASC requirements and procedures to make it more attractive to positions requiring highly experienced, technically qualified, proven senior leaders from the private sector

# The Results

- **The time to make these changes is now – we are already behind in the talent race**
- **This is a small number of recommendations, but they generate significant leverage**
- **With these adjustments in place, the Nation will be able to access the creative and managerial talent necessary to lead it through these long struggles of such consequence to America and the rest of the world**