



ISSUE PAPER

Insourcing and the Defense Industrial Base: A Product Support Perspective

The United States is faced with a budget problem of staggering proportions that threatens our global leadership role. Any effort on the part of the government to resolve this crisis will have an impact on all sections of the defense industrial base. It is imperative that the government understands the consequences of any actions they may undertake including probable effects of their actions on the U.S. aerospace industry. Certainly, the government has a variety of constituencies it must support by its actions, but few of them have the same degree of impact on both the economic and military strength of our country as does the aerospace industry. Unfortunately, our government has been blindly pursuing a policy of industrial insourcing since early 2009 that is negatively impacting the overall health of the industrial base.

By definition, industrial insourcing is the effort on the part of the government to move product support services from the private sector into organic government activities. Most insourcing to date has been justified on the basis of cost savings or compliance with federal statute. The resultant cost savings have been largely illusory and certainly nowhere near the \$40 billion anticipated. In fact, then Secretary of Defense Robert Gates admitted in August 2010 that insourcing was not saving any money. As for federal statute, Chapter 146 of Title 10, U.S. Code, which regulates sourcing within DOD, contains little about efficiency or cost effectiveness, but does mandate that at least 50 percent of every dollar spent on depot repair must be spent in a government facility. The impact of this requirement, commonly referred to as the 50-50 rule, is exacerbated by the fact that spending is aggregated and compliance is judged on the individual service vice Department of Defense level with the result that any individual service could be out of compliance in any given year in spite of the fact that DOD at large remains fully compliant. The result of this anomaly is more losses of aerospace industry work every year as the services strive to

avoid breaching the 50-50 rule, in spite of the fact that at the DOD level the numbers are fully compliant with the law.

More recently, insourcing has slowed considerably in view of cost realism and civilian manpower limitations. That said, legislation and policy continue to favor the public sector and insourcing proponents continue to press to codify further protections. The precedence of this desire for insourcing over economic realism is troubling given the strategic importance of understanding cost drivers and the need for cost effectiveness in the face of our present economic straits. As former Joint Chiefs of Staff Admiral Mullen declared, “the single greatest threat to national security is the national debt.” It follows then that the most logical industrial sourcing policy is one based on a thorough cost analysis. However, such an analysis is dependent on accounting systems capable of reporting cost and a business case analysis process that accurately collects and fully accounts for all costs. Unfortunately, as reported in GAO report GAO-05-207, “DOD’s continuing, substantial financial management weaknesses adversely affect its ability to produce auditable financial information as well as provide accurate and timely information for management and the Congress to use in making informed decisions.”

Now that this country is embroiled in a budget crises, the question to ask is whether non-economic preferences serves our nation’s interests, or even have a place, when each dollar lost to inefficiency means one dollar taken from procurement or boots on the ground. AIA certainly agrees that it is “essential for the national defense that the Department of Defense maintain a core logistics capability,” but asserts it is not essential this capability be restricted to government employees. Indeed, the private sector, which alone can provide the warfighter his tools, must itself be healthy and protected. The essential requirement for the national defense

is that both government and industry be ready and capable in times of national emergency.

In defense, the U.S. government is the only customer that matters and the reality is that government depends on private industry for the basic tools needed for the public defense. Defense cuts are all but certain with a DOD budget impact in the hundreds of billions of dollars. Further, increases in the inherent reliability of newer weapon systems coupled with the rapidly expanding use of COTS and reductions in total number of platforms means a reduced product support workload for all sectors of the industrial base. If there is to be a rational path to maintain mission capability for the warfighter, while preserving the public and private industrial base, it must be through a rigorous financial analysis and shared respect.

In conclusion, AIA supports a national industrial policy that defines the desired core capability needed to fully maintain national skill and capability requirements for the assurance of a ready and controlled source of maintenance. However, non-economic preferences and supplementary requirements, such as the 50/50 rule that mandate the assignment of an arbitrary-fixed percentage of depot dollars to the public sector, do not account for the dynamic environment of the U.S. defense environment nor do they do anything to protect the private sector of the industrial base. The public sector of the industrial base is well protected by statute and any further arbitrary insourcing of depot workload without financial analysis weakens not only the industrial base and the economy as well as the entire nation.