PRELIMINARY WORKING GROUP DRAFT
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ACQUISITION ADVISORY PANEL
PERFORMANCE-BASED CONTRACTING SUBPANEL REPORT

Ensuring Effective and Appropriate Use of Performance-Based Contracting

10/13/2005

A. Introduction to Performance-based Contracting

Performance-Based Contracting (PBC)[1] is a collection of strategies, methods and techniques for acquiring services that focuses on describing **end results** (rather than dictating the manner in which the services are to be provided) and measuring whether or not those results were obtained.

The present provisions of the Federal Acquisition Regulation include a general definition of performance-based contracting (FAR 2.101), a conditional mandate for use of performance-based contracting (FAR 37.102), and more concrete guidance as to the mechanics of performance-based contracting (FAR 37.601).

Initially, FAR 2.101 defines the category of performance-based contracting as follows:

> Performance-based contracting means structuring all aspects of an acquisition around the purpose of the work to be performed with the contract requirements set forth, in clear, specific, and objective terms with measurable outcomes as opposed to either the manner by which the work is to be performed or broad and imprecise statements of work.

Several facets of this definition should be noted:

- The requirement that contract requirements be specified in terms that are both specific and objectively measurable.

- PBC is defined as a method of contracting that focuses contract requirements on the objectives to be achieved by the contract services rather than the methods by which they are to be achieved or other inputs by the contractor.

The Panel understands that the current FAR definition of PBSA is being revised. The Panel will address it when it is released, or may articulate a definition of its own in advance.

B. Relevant Statutory, Regulatory and Policy Guidance

PBC was developed as part of an overall movement in government management toward commercial business practices resulting from the perception that the existing acquisition system was characterized by:

- A lack of opportunity for innovation.
- A focus on process not results, and,
- Costs higher than necessary.

[1] "Performance-based service acquisition (PBSA)" has generally replaced "performance-based contracting (PBC)" as the current terminology to be applied to this acquisition approach. However, for purposes of consistency, this report will continue to use PBC to describe the contracting technique.

PBC is also consistent with the Government Performance and Results Act of 1993 (GPRA) that seeks to shift the focus of Government management from more traditional concerns such as staffing and activity levels to a focus on business outcomes or results.

What are the proposed benefits of using PBC? The following list provides some of the arguments for adopting this acquisition technique:

- Increased likelihood of meeting mission needs
- Focus on intended results, not process
- Better value and enhanced performance
- Less performance risk
- No detailed specification or process description needed
- Contractor flexibility in proposing solution
- Better competition: not just contractors, but solutions
- Contractor buy-in and shared interests
- Shared incentives permit innovation and cost effectiveness
- Less likelihood of a successful protest
- Surveillance: less frequent, more meaningful
- Results documented for Government Performance and Results Act reporting, as by-product of acquisition
- Variety of solutions from which to choose[2]

Panel Mandate:

According to Section 1423 of the National Defense Authorization Act of 2004 the panel's responsibilities include a review of "laws and regulations regarding the use of performance-based contracting." The panel's objectives include making recommendations "with a view toward ensuring effective and appropriate use of . . . performance-based contracting."

Administration Initiatives:

The use of PBSA has been encouraged by OMB and the Office of Federal Procurement Policy (OFPP) since its inception. However the current administration was the first to elevate it to a Presidential initiative and assign specific implementation goals. In 2001,

[2] From Seven Steps to Performance-Based Services Acquisition http://www.arnet.gov/Library/OFPP/BestPractices/pbsc/introduction.html

OMB directed that agencies use performance-based techniques on a specific percentage of the total eligible service contracting dollars each fiscal year as follows:

Fiscal Year	Percent
2002	20
2003	30
2004	40
2005	40 (changed from original 50% by OFPP[3])

Government-wide PBC policy was first contained in Office of Federal Procurement Policy (OFPP) Letter 91-2 on service contracting that was issued on April 9, 1991. This OFPP letter was prompted by internal agency investigations, Government Accountability Office (GAO) reports and OFPP studies. These documented numerous instances of unsatisfactory performance and contract administration problems that coincided with an increase in the Government's acquisition of services

In addition to these relatively general arguments for shifting to a performance-based acquisition approach, OFPP in a May 1998 study entitled *A Report on the Performance-Based Service Contracting Pilot Project* cited specific cost and program gains from this approach. OFPP reviewed 26 different contracts from 15 agencies with a combined award value of $585 million. The contracts ranged in value from $100,000 to $325 million. On average, as a result of the shift to PBC, contract price decreased by 15 percent. In addition, customer satisfaction improved over 18 percent, from 3.3 to 3.9 on a scale of 1 to 5. The report cited other benefits as well. For example, the number of offers increased from 5.3 to 7.3 when PBC was introduced and the total number of contract audits decreased 93 percent. On the negative side, the average total procurement lead time increased by 38 days, from 237 to 275. Unfortunately there is no more recent analysis that attempts to examine and document this type of information from a cross agency perspective.

FAR PBC Provisions:

The FAR also contains a mandate, within boundaries, for the use of PBC, "to the maximum extent practicable."

FAR 37.102 provides:

(a) Performance-based contracting (see Subpart 37.6) is the preferred method for acquiring services (Public Law 106-398, section 821). When acquiring services, including those acquired under supply contracts, agencies must --

[3] Memorandum for Chief Acquisition Officers and Senior Procurement Executives, Increasing the Use of Performance-Based Service Acquisition, 9/7/2004.

(1) Use performance-based contracting methods to the maximum extent practicable, except for [four excluded categories of contracting][4]

FAR 37.601 provides more concrete guidance as to the intended operation of performance-based services contracting. FAR 37.601(a) provides:

37.601 General.

(a) Performance-based contracting methods are intended to ensure that required performance quality levels are achieved and that total payment is related to the degree that services performed or outcomes achieved meet contract standards. Performance-based contracts or task orders --

(1) Describe the requirements in terms of results required rather than the methods of performance of the work;

(2) Use measurable performance standards (i.e., in terms of quality, timeliness, quantity, etc.) and quality assurance surveillance plans (see 46.103(a) and 46.401(a));

(3) Specify procedures for reductions of fee or for reductions to the price of a fixed-price contract when services are not performed or do not meet contract requirements (see 46.407); and

(4) Include performance incentives where appropriate.

Note several facets of this provision:

- This provision does not repeat, but does not eliminate the insistence on objective measurement found in FAR 2.101's definition of performance-based contracting

- It is fundamental to performance-based contracting <u>both</u>

  - That *in the contract formation process,* contract performance be prescribed in terms of the objectives to be achieved rather than methods of performance prescribed and

  - That *in the contract performance phase,* contract performance be measured in systematic fashion.

- The degree to which positive or negative performance incentives are required as opposed to discretionary appears to be somewhat obscure under the existing language. The intended relationship between the language on fee and price reductions and the language on discretionary performance incentives is certainly not clear.

Interagency Task Force Report

[4] The present exclusions are for contracts for: 1) architect-engineer services acquired under 40 U.S.C. 541 et seq., 2) construction contracts, 3) utility services, and 4) services incidental to supply purchases.

In July 2003 an Interagency Task Force on Performance-Based Services Acquisition established by OFPP issued its report designed to make recommendations for amendments to the FAR to address observed problems in implementing the mandate for performance-based services acquisition.[5] The following table summarizes these recommendations and highlights their status while the narrative below addresses the proposed FAR changes in further detail.

Status of OFPP Implementation Recommendations

Recommendation	Implementation Status
1. Modify the FAR Part 2 to include definitions for: 1) performance work statement, 2) quality assurance surveillance plan, 3) statement of objectives, and 4) statement of work to support changes to Part 37. Modify FAR Parts 11 and 37 to broaden the scope of PBSA and give agencies more flexibility in applying PBSA to contracts and orders of varying complexity.	Proposed rule in process.[6]
2. Modify the list of eligible service codes for PBSA, as articulated in the Federal Procurement Data System (FPDS) or FPDS B Next Generation (FPDS-NG) manual, to more accurately reflect services to which PBSA can be applied.	Implemented by OFPP Memorandum of 9/7/04 entitled "Increasing the Use of Performance-Based Acquisition."
3. Revise FPDS instructions to ensure agencies code contracts and orders as PBSA if more than 50 percent of the requirement is performance based, as opposed to the current 80 percent requirement.	Implemented by OFPP Memorandum of 9/7/04 entitled "Increasing the Use of Performance-Based Acquisition."
4. Allow agencies that do not input data to FPDS to submit supplemental reports in order to accurately reflect their progress toward meeting goals.	Implemented by OFPP Memorandum of 9/7/04 entitled "Increasing the Use of Performance-Based Acquisition."
5. Consider allowing agencies to establish interim goals but expect agencies to apply PBSA to 50 percent of their eligible service contracts (see recommendation 2 above) by 2005, in line with DOD policy.	Original target of 50% changed to 40% by OFPP Memorandum of 9/7/04 entitled "Increasing the Use of Performance-Based Acquisition."
6. OFPP should rescind its 1998 Best Practices Guide and consider developing web-based guidance to assist agencies in implementing PBSA. This guidance should be kept current and should include practical information, such as samples and templates that agencies would find useful. The website should include "The Seven-Steps to Performance-Based Services Acquisition Guide" and may include elements of existing guidance. The working group will explore the development of a web-based PBSA site for guidance, samples, and templates.	Implemented by OFPP Memorandum of 9/7/04 entitled "Increasing the Use of Performance-Based Acquisition."

[5] Interagency Task Force on Performance-Based Service Acquisition, PERFORMANCE-BASED SERVICE ACQUISITION: CONTRACTING FOR THE FUTURE (July 2003).

[6] FAR Case 2003-018, F.R./Vol. 69, No. 139, 7/21/04.

On July 21, 2004, the Civilian and Defense FAR Councils proposed amendments to the FAR to implement many, but not all of the Interagency Task Force recommendations.[7] The general thrust of the proposed FAR amendments was to give federal agencies more flexibility so as to encourage its consistent use where appropriate.

In the definitional provisions, the proposed FAR changes would recast the definition of performance-based contracting presently found in FAR 2.101 to a definition of performance-based acquisition. The acquisition of services through performance-based acquisition would be labeled performance-based services acquisition (PBSA). There do not appear to be material substantive changes in these provisions.

The definitional provisions of the FAR would also be supplemented by introducing definitions of "Performance Work Statement" and "Statement of Objectives" as follows:

> *Performance Work Statement (PWS)* means a statement that identifies the agency's requirements in clear, specific and objective terms that describe technical, functional and performance characteristics.
>
> *Statement of Objectives (SOO)* means a statement that identifies the agency's high-level requirements by summarizing key agency objectives, desired outcomes, or both.

? The relationship contemplated appears to be that the Performance Work Statement is contemplated to be the more detailed and objective statement of agency requirements, while the Statement of Objectives may be drawn at a higher level of generality.

? As defined, the Statement of Objectives does not insist on complete specification in objective terms of the results desired from contract performance.

Although the Interagency Task Force had recommended an amendment to FAR 37.102 to add term type contracts to the list of exclusions from the mandate for use of performance-based contracting techniques where practicable, that recommendation did not appear in the proposed FAR revisions.[8]

The pending proposal to amend the FAR provisions applicable to performance-based services acquisition would also make significant changes to FAR 37.601. The proposed revision of that section would provide:

> (a) The principal objective of PBSA is to obtain optimal performance by expressing Government needs in terms of required performance objectives and/or desired outcomes, rather than the method of performance, to encourage industry-driven, competitive solutions.

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[7] 69 Fed. Reg. 43712 (July 21, 2004).

[8] *Compare* 69 Fed. Reg. at 43712, Interagency Task Force on Performance-Based Service Acquisition, PERFORMANCE-BASED SERVICE ACQUISITION: CONTRACTING FOR THE FUTURE (July 2003), at 3.

(b) Solicitations for PBSA may use either a performance work statement (PWS) or a statement of objectives (see 37.602-1).

(c) PBSA contracts or orders shall include-

(1) A PWS (see 37.602-1); and

(2) Measurable performance standards. These standards may be objective (e.g., response time) or subjective (e.g., customer satisfaction), but shall reflect the level of service required by the Government to meet mission objectives. Standards shall enable assessment of contractor performance to determine whether performance objectives and/or desired outcomes are being met.

(d) PBSA contracts or orders may include performance incentives to promote contractor achievement of the desired outcomes and/or performance objectives articulated in the contract or order. Performance incentives may be of any type, including positive, negative, monetary, or non-monetary. Performance incentives, if used, shall correspond to the performance standards set forth in the contract or order.

Noteworthy aspects of the proposed language are as follows:

? First, the new language proposed to be introduced into FAR 37.601(a) appears to be designed to keep a sharp focus on the main point of PBSA: to enable the government to secure the benefit of competition among private sector providers as to the best means of achieving the objectives that government seeks to secure.

? Second, the new language proposed for FAR 37.601(b) allows the agency significant flexibility by allowing it to employ the less specific and less objectively framed Statement of Objectives as an alternative to a Performance Work Statement at the solicitation stage.

? Note, however, that full PWS is required to be included in contracts or task orders entered in the PBSA process.[9] This appears to be a departure from the recommendation made by the Interagency Task Force, which would have allowed agencies the choice of SOO or PWS throughout the contracting process, so long as the ultimate contract contained "measurable performance standards."[10] (See next bullet point.) In this respect, the proposed FAR changes offer less flexibility than the Interagency Task Force sought to achieve by its recommendations.

[9] Proposed FAR 37.602-1(a) would expressly authorize the creation of the PWS by the contractor starting from a SOO prepared by the agency. Although proposed FAR 37.602-1(c) would in that case require the agency to specify, in the SOO, the performance objectives or desired outcomes, the contractor apparently could be responsible for the detailed and objective specification of contract requirements necessary for the PWS to be included in the contract itself.

[10] Interagency Task Force on Performance-Based Service Acquisition, PERFORMANCE-BASED SERVICE ACQUISITION: CONTRACTING FOR THE FUTURE (July 2003), at 3.

- ? The proposed revision requires inclusion of "measurable performance standards" in contracts produced by PBSA. Significantly, and consistent with the recommendations of the Interagency Task Force, these provisions make clear that measurable performance standards may be either objective or subjective—and thus may be framed in terms of gauging the level of satisfaction of the governmental customer for services. If viewed in isolation, this aspect of the proposed FAR changes would achieve significant flexibility for agencies engaged in PBSA. It would be a mistake, however, to view this provision in isolation

- ? A significant ambiguity or source of confusion appears to arise from the framing of the proposed FAR 37.601(c) because of the requirement that a contract contain both a PWS and "measurable performance standards." As explained above, the measurable performance standards provision makes explicit that subjective measures of customer satisfaction with the results of contract performance can fulfill the measurable performance standard requirement. But the effect of that language apparently would be frustrated by harnessing it in tandem with the ironclad requirement for a PWS, which must be framed in objective terms. It is natural to surmise that the proposal reflects some effort to compromise on the recommendations of the Interagency Task Force, but it appears that the present language is a dysfunctional rhetorical compromise that literally seeks to have it both ways. This point appears to require clarification before the FAR changes are finalized.

- ? Finally, the proposed language of FAR 37.601 appears to make clear that the use of incentive payment provisions, whether positive or negative, is a discretionary, rather than a mandatory element of PBSA. If adopted, this would appear to offer a significant degree of clarification of the existing language of the FAR.

One additional feature of the proposed FAR revisions that should be mentioned here is the proposed revisions to FAR 37.602-2, governing quality assurance. The proposed language would:

- ? First, make clear the commonsense proposition that the level of quality assurance surveillance should be appropriate to the dollar value risk and complexity of the particular acquisition.

- ? Second, the proposed language would expressly introduce the philosophy of adherence to commercial practices, which would have to be followed, "to the maximum extent practicable" in framing quality assurance mechanisms

- ? Third, the proposal would make explicit that, in the case of some simplified acquisitions, no special quality assurance surveillance plan, beyond that inherent in the inspection provisions of the contract, is required.

This rule is as of this writing still under review at OMB. The panel will address it when it is finally promulgated.

C. Current Practices in Performance-based Contracting

As documented in the attached appendix, both the Administration and the Congress over the last decade and a half have continued to press agencies to make greater use of performance-based approaches for acquiring contractor support. However, various review organizations including the GAO have raised concerns about its implementation, calling into question whether there is adequate understanding among the agencies on how to successfully carry out PBC. A number of witnesses before the AAP have reinforced these concerns.

In September 2002, for example, the GAO released a study of a small sample of contracts that were identified as performance-based service contracts by the agencies involved. Notwithstanding the agency identification of the contracts as embodying PBC, GAO concluded that there was a wide range in the degree to which these contracts in fact exhibited the characteristics of PBC. For this reason, GAO concluded that the study "raise[s] concern as to whether agencies have a good understanding of performance based contracting and how to take full advantage of it."[11]

The GAO in its analysis reviewed 25 contracts designated as performance-based by the Department of Defense, the Department of Treasury, Department of Energy, National Aeronautics and Space Administration and GSA. Although most of the contracts exhibited at least one performance-based attribute, only nine possessed all of the required elements. Moreover, the GAO found that many of the contracts contained extremely restrictive work specifications. Nor is the problem as simple as agency resistance to a clear mandate. In roughly half the cases in which GAO found incomplete adherence to the elements of PBSA, GAO identified a recurring pattern: the contracts entailed "unique and complex services" which entailed such significant "safety, cost and/or technical risks" that the agencies "*appropriately*" concluded that they needed to be more "prescriptive" as to how the work was to be done, and exercise more oversight as to methods for achievement of objectives.[12]

This raises questions both as to the proper definition of performance-based services acquisition, and the proper scope of contracting that is subject to the mandate to employ performance-based acquisition. And it raises a specific question about the use of performance-based methods to the greatest extent appropriate in cases in which there may be legitimate constraints on complete adherence to the performance-based model.

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[11] United States General Accounting Office, CONTRACT MANAGEMENT: GUIDANCE NEEDED FOR USING PERFORMANCE-BASED SERVICE CONTRACTING (GAO-02-1049)(September 2002), at 2.

[12] United States General Accounting Office, CONTRACT MANAGEMENT: GUIDANCE NEEDED FOR USING PERFORMANCE-BASED SERVICE CONTRACTING (GAO-02-1049)(September 2002), at 2, 7.

As noted above, the FAR requires that agencies use PBSA "to the maximum extent practicable extent" with the exception of contracts for:

- Architect-engineer services acquired inaccordance with 40 U.S.C. 541-544 (FAR Part 36);
- Construction (FAR Part 36);
- Utility services (FAR Part 41); or
- Services that are incidental to supply purchases[13]

In addition, acquisition plans for service contracts or orders must describe the strategies for implementing performance-based contracting methods or the rationale for not using them.[14]

Initially, agency use of PBC was confined to basic non-technical and support services such as security, laundry, grounds maintenance, and facility maintenance. Today, use of PBC has expanded considerably (particularly in the information technology area). For example, the Department of Health and Human Services lists the following examples of services suitable for PBC on its website:[15]

- Facility support services e.g., security, laundry, grounds maintenance, facility maintenance, equipment repair, other than Information Technology (IT)
- Administrative and clerical support, e.g., data entry, court reporting, typing, editing, distribution
- Aircraft maintenance and test range support
- Transportation, travel and relocation services
- Logistics/conference support
- Medical services
- Research and Development
- Research support services
- Telephone call center operations
- Training
- Environmental remediation
- Information Technology (IT) and telecommunications services to include maintenance and support services
- Technical assistance
- Management support
- Studies and analyses
- Surveys

Current instructions for coding actions as "performance-based" in the Federal Procurement Data System (FPDS) require that more than 50 percent of the requirement, as measured in dollars, be performance-based.[16] This is a recent change from the 80

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[13] FAR 37.102
[14] FAR 7.105
[15] KNOWnet, the Acquisition SuperSite, http://www.knownet.hhs.gov/acquisition/performdr/LAI/UnitOne/program.htm

[16] Ibid. Previous coding instructions required 80% of the action to be performance-based.

percent factor that had been applied prior to September 2004. For purposes of determining eligible services contracting dollars, OFPP[17] has excluded the services exempted by the FAR noted above and the following:

- ? Research and development to include Basic Research, Applied Research, Advanced Technology Development, Demonstration and Validation and Engineering and Manufacturing Development (FPDS codes A**1-A**5);
- ? Professional Medical Services (not facility-related, Codes Q501-Q527); and,
- ? Tuition, Registration and Membership Fees (Code U005)

Agencies are seeking to comply with the Administration requirements. Frequently they are following the Seven Steps Guide whose web site is shown in Appendix One. The Seven Steps for conducting PBC are as follows:

1. Establish an integrated solutions team.
2. Describe the problem that needs solving.
3. Examine private sector and public sector solutions.
4. Develop a performance work statement (PWS) or statement of objectives (SOO).
5. Decide how to measure and manage performance.
6. Select the right contractor.
7. Manage performance.

Although agencies have attempted to follow these steps, reviews of selected contracts conducted by subpanel members have revealed that contracts asserted to be performance-based often lack one or more of the key elements included in the Federal Acquisition Guidelines for determining whether or not a contract meets the FAR requirements. This finding is very much in line with the GAO criticisms noted earlier. For example, while contracts may contain useful measures by which to assess successful performance, they often lack a Quality Assurance Surveillance Plan that is integral to qualifying the effort as performance-based.

The following chart offers an assessment of difficulty in implementing PBSA for various combinations of service and contracting types.

Degree of PBSA Implementation Difficulty by Contract Type

Type of Service	Current Contract Type	PBSA Implementation Difficulty Low/Moderate/High	Specific Challenges
Basic logistical and support	Firm fixed price	Low	✍ None.
	CPIF of CPAF	Low	✍ None.

[17] Ibid.

services	CPFF or Time and Materials	Moderate	✍ Overcoming reliance on buying hours in favor of developing performance standards. ✍ Linking performance to meaningful incentives/disincentives.
	Indefinite Quantity Contract (IQC)	Moderate	✍ Developing relevant performance standards in advance of specific requirements.
Complex professional and technical services	Firm fixed price	Moderate	✍ Establishing outcomes and performance standards attributable to the contractor's efforts.
	CPIF of CPAF	Moderate	✍ Establishing outcomes and performance standards attributable to the contractor's efforts.
	CPFF or Time and Materials	High	✍ Establishing outcomes and performance standards attributable to the contractor's efforts. ✍ Overcoming reliance on buying hours in favor of developing performance standards. ✍ Linking performance to meaningful incentives/disincentives.
	IQC	High	✍ Establishing outcomes and performance standards attributable to the contractor's efforts. ✍ Developing relevant performance standards in advance of specific requirements.

The Office of Federal Procurement Policy is in the process of completing a new report that will give much more data on the extent of agency-wide use of PBC. Key statistics from this report will be provided once they are received. The information will include both funding levels and distribution of performance-based contracting actions against various functional areas, as for example, information technology support services. This information should offer the working group a much better means for assessing the extent of agency wide implementation.

D. Statement of the Issue: Why has Performance-based Services Acquisition not been fully implemented in the federal government?

The Panel has selected this question as its overall statement of issue. From prior reviews of PBSA's implementation as well as testimony taken by the Panel, it is clear that the following implementation challenges hamper the full implementation of PBSA and the complete realization of PBSA's benefits to the taxpayer.

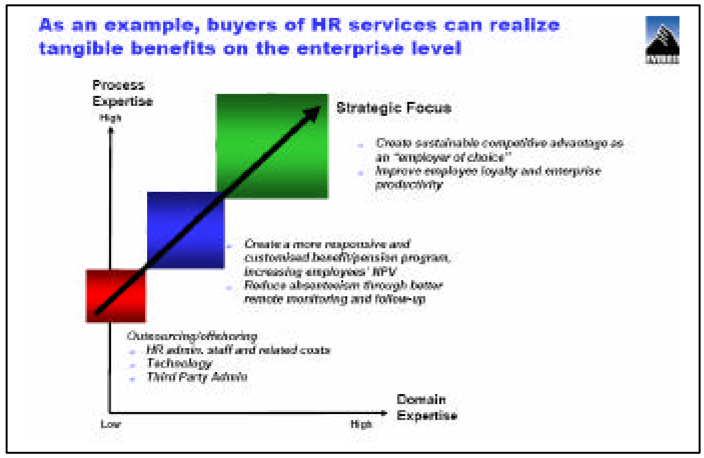
Challenge 1: Some PBSA Contracts Continue to Focus on Activities and Processes, Rather than Performance and Results

Performance-based contracting is supposed to focus on results, not effort or activities. Unfortunately, the Panel's witnesses reinforced earlier findings from the GAO PBSA Report that questioned the kinds of measures and the overly "work" focused nature of Statements of Work. Many witnesses before the panel stressed that PBSA contracts tend to add a veneer of "performance measures" on top of overly lengthy statements of work. According to testimony received from Robert Zahler of Pillsbury Winthrop Shaw and Pittman, "Classic RFPs in my industry--and I think probably in the Federal side, also--spend enormously too much time documenting historical facts: what did we do, how did we do it, what did it cost. They have some high-level stuff of maybe what they want in the future, but all too little of that. Rather, the RFP should say, "Here are my objectives. Here are my requirements. Here's how I want to interrelate with you. Come back and give me a solution."

In addition to changing the overall focus of the Statements of Work/Objective used, determining measures in the actual contracts that are clear and results-oriented are a challenge. In his testimony to the Panel, Brian Jones of the United States Coast Guard discussed his experience with measures for contracts, "People have a hard time doing that. I've been working in measurement and analysis for 15 years and the thing I find is people will sit there and they'll try to measure everything. They'll come up with 25 measures, which is, I think, is the wrong approach. We take a very simple approach, as few measures as possible, the ones that are really critical to your success."

Challenge 2: Lack of "Enterprise Sourcing" Strategy to Drive PBSA

Performance-based contracting is supposed to yield innovative solutions to the government's challenges. Several witnesses noted that the federal government does not establish a clear definition of enterprise objectives and open competitions to innovative solutions. Testimony provided by Todd Furniss of the Everest Group illustrated this point quite well. In discussing the graphic here, Furniss noted So you can see that if



you're focused on the myopic, you can actually do something quite counterproductive to corporate objectives. In fact, one of the terms that's frequently used in… the lower left is your mess for less. Here you're not focused on changing much; you're just talking about doing it less expensively. And the term that tends to be used in the upper right hand corner tends to be transformational in nature, meaning that the suppliers are focused on changing more and offering more feature function benefit with a different set of economic alignments in the interest of driving the business forward at the organizational level."

Reinforcing Furniss' point, several witnesses remarked that government is usually not open to a broader set of responses outside its original statement of work—and most contractors are fearful of losing business if they do not mimic the statement of work closely in their responses.

Challenge 3: Improvements Needed in Monitoring and Managing Contract Performance After Award

Performance-based contracting does not end with the award of the contract; it is an ongoing process of monitoring and managing existing contracts for improved performance. Multiple witnesses expressed concerns that the government does not adequately collect performance information for individual contracts, let alone review and provide ongoing feedback and corrective action on performance of vendors.

Use of the management and monitoring tools such as Quality Assurance Surveillance Plans (QASP) and Acceptable Quality Level (AQL) are not effectively being utilized to ensure performance. In testimony before the Panel, Ms. Barbara S. Kinosky from Centre Consulting stated, "Government needs to learn not to create overly burdensome surveillance plans that will ultimately create a bureaucracy of contractors, monitoring contractors, monitoring contractors for compliance, only evaluate what is necessary to accurately measure success." Another witness noted "there's no means to track whether we're successful in that or whether we're getting the objectives that we're putting on paper, so we need to get better in that area."

This challenge was also seen in the private sector's use of performance contracting. Robert Miller from Proctor and Gamble testified that "In reality, over a five to seven year term, or as people start to put a contract in place, what you sometimes find out is that the folks actually on the front line managing the interface don't often check the contract as they go through; sometimes, the deal is put on the shelf and largely forgotten, and actually, the vendors like to encourage this. That gives them more flexibility. Often, some of the people who are involved in managing the project were not involved in the negotiation of the transaction. They may not have a full knowledge of the contract. As events unfold, where there are departures from the agreement, sometimes, those aren't recognized by the people in the front line. Life being what it is, not everything is anticipated; even the best lawyers and people who work in the area substantively are not going to be able to anticipate everything, and so, there are going to be modifications, and sometimes, those just get executed. They're not in the agreements. There are often tools for monitoring the agreements that sometimes are not really utilized to the fullest by the people managing the arrangement."

Challenge 4: Most Contract Incentives Are Still Not Aligned to Maximize Performance and Continuous Improvement

A big element of PBSA is the use of financial and non-financial incentives to leverage improved results for the taxpayer. Many PBSA vehicles have used "fixed price" approaches to provide contractors incentives to improve performance. Nevertheless, many other avenues to provide incentives exist. In many cases, incentives are not fully aligned to encourage continuous improvement or innovation by the contractors for the government.

Barbara Kinosky of the Centre Consulting and the Federal Consulting Institute, commented to the panel, "That when acquisition professionals are working from limited templates, and using only financial penalties and disincentives to enforce the quality assurance surveillance plan, then that risk is understandably going to be priced by the contractor and included in the contract price. An adequate library and resource center will enable the acquisition team to think in terms of alternative approaches, such as the exercise of an option year as an incentive, rather than just disincentives. This approach will ultimately save the government money because it reduces the risk to the contractor."

Brian Jones of the United States Coast Guard testified, "one of the challenges that we face is the incentives and the disincentives, and when we get to that part of it, it's very challenging because we don't have any additional funding for incentives, so it ends up being, you know, putting those disincentives out there and sometimes they're just--they are inconsistent with what it is that we're trying to achieve. For instance, we just had a--we just had a failure on a contract, almost a failure. We almost went into termination. It was an IT contract. It was so ridiculous. It was like there was $500 per hour of downtime and it's down for weeks. It just didn't make sense."

Challenge 5: Within Federal Acquisition Functions, There Still Exists a Cultural Emphasis is on "Get to Award"

Many witnesses reinforced the notion that PBSA is a process that takes more time up front to clarify agency needs, engage in innovative solutions development, and craft the right measures and incentives. This increased up-front investment of time, training and resources flies in contrast to the traditional culture of most acquisition shops today that are under pressure from internal clients to get contracts awarded quickly. Chip Mather, from Acquisition Solutions met with the PBC workinggroup. In our discussion, Mr. Mather expressed his experience that the focus of most federal contracting shops is on "getting to award, over the process of due diligence."

Challenge 6: Questionable Data and Reporting of PBSA

The working group found securing and analyzing data from FPDS to be a major challenge. Months after our initial request for information was submitted by staff, the Panel is still awaiting reliable data. According to testimony from Ronne Rogin, "One of the things we're seeing now is agencies are really not able to figure out where they are in obtaining their goals. The Federal Procurement Data System, NG, the form that you fill out to do the data entry, really doesn't give you the chance to enter the data correctly…and so the data that you're getting is not accurate. That's a problem, to even figure out where we are."

APPENDIX ONE

PERFORMANCE-BASED CONTRACTING WORKING GROUP
PBC CHRONOLOGY

1. OFPP Policy Letter 91-2, "Service Contracting" April 9, 1991– rescinded in March 2000 FR, http://www.arnet.gov/Library/OFPP/PolicyLetters/Letters/PL91-2_4-9-91.html

2. "On March 15, 1993, the Office of Management and Budget (OMB) Director Leon Panetta requested that 17 major Executive Departments and agencies review their service contracting programs. The purpose of the review was to determine (1) if the service contracts were accomplishing what was intended; (2) whether the contracts were cost effective; and (3) whether inherently governmental functions were being performed by contractors. The results of the reviews indicated that service contracting practices and capabilities are uneven across the Executive branch and that various common management problems need to be addressed." (See intro to OFPP Policy Letter 93-1)

3. OFPP Policy Letter 93-1 "Management Oversight of Service contracting" http://www.acqnet.gov/Library/OFPP/PolicyLetters/Letters/PL93-1.html

4. Former VP Gore designated PBC as an integral aspect of the National Performance Review (http://govinfo.library.unt.edu/npr/library and then/nprrpt/annrpt/sysrpt93/reinven.html for the "Reinventing Federal Procurement" report. Pilot launched October 1994. Director Rivlin led the kick-off ceremony where executive official of the participating agencies signed a government wide pledge to participate in the project (Exhibit 5 of OFPP "A Report on the Performance-Based Service Contracting Pilot Project available at www.acqnet.gov under Virtual Library-Policy Documents).
www.acqnet.gov/Library/OFPP/PolicyDocs/pbscpilpro.html

5. OFPP Policy Letter "Performance-Based Service Contracting Solicitation/Contract/Task Order Review Checklist" August 9, 1997
www.acqnet.gov/Library/OFPP/PolicyDocs/pbscckls.html

6. FAC 97-01 (Item VII) – FAR Case 95-311, implementing OFPP Policy Letter 91-2 (see 1 above), by revising FAR Parts 7, 37, 42, 46, and 52. All FACs available at http://www.acqnet.gov/far

7. "A Report on the Performance-Based Service contracting Pilot Project" OFPP May 1998.
www.acqnet.gov/Library/OFPP/PolicyDocs/pbscpilpro.html

8. Federal Acquisition Streamlining Act of 1994. See, among others, 10 USC 2220 and 41 USC 263.

9. Government Performance and Results Act of 1993

10. Clinger-Cohen Act of 1996

11. "Guide to Best Practices for Performance-Based Service Contracting" 1998 [Laura can get a copy but not available today on web site]

12. Contract management: Trends and Challenges in Acquiring Services, May 22, 2001 GAO Testimony before the Subcommittee on Technology and Procurement Policy, Committee on Government Reform, House of Representatives. http://www.gao.gov/new.items/d01753t.pdf

13. GAO-02-179t Contract management: Improving Services Acquisitions, October 30, 2001 http://www.gao.gov/new.items/d02179t.pdf

14. "Guidance Needed for Using Performance-Based Service Contracting" GAO, September 20, 2002 http://www.gao.gov/new.items/d021049.pdf

15. President's Management Agenda http://www.whitehouse.gov/omb/budget/fy2002/mgmt.pdf

16. GAO Report 03-443 Federal Procurement: Spending and Workforce Trends. http://www.gao.gov/new.items/d03443.pdf

17. "Performance-Based Service Acquisition – Contracting for the Future" Interagency Task Force on Performance-Based Service Acquisition, July 2003 http://www.whitehouse.gov/omb/procurement/0703pbsat.pdf

18. Section 1431 of the Services Acquisition Reform Act of 2003, Additional Incentive for use of Performance-based Contracting for Services and Section 1433, Clarification of Commercial Services Definition (Title XIV of the National Defense Authorization Act for Fiscal Year 2004). http://reform.house.gov/UploadedFiles/Title%20XIV%20of%20H.R.%201588%20Conference%20Report.pdf

19. FAR Case 2004-004, Incentives for the Use of Performance-Based Contracting for Services. This case implements Section 1431 and 1433 of the Services Acquisition Reform Act of 2003 in 18 above. Go to the link and select FAC-05-04. The case is 2004-004, Item III.: http://205.130.237.11/far/facsframe.html

20. FAR Case 2003-018, Implementing the Task Force Report is, as of 9/7/05, still at OIRA (OMB).

21. GAO-04-715, Defense Management: Opportunities to Enhance the Implementation of Performance-Based Logistics, August 9, 2004 http://www.gao.gov/new.items/d04715.pdf and GAO-05-966, Defense Management: DOD Needs to Demonstrate That Performance-Based Logistics Contracts Are Achieving Expected Benefits, September 9, 2005 http://www.gao.gov/cgi-bin/getrpt?GAO-05-966

22. OFPP Memo, "Increasing the Use of Performance-Based Service Acquisitions," September 7, 2004 (see http://www.acqnet.gov and the memo is on the home page)

23. "Seven Steps to Performance-Based Services Acquisition Guide" linked to the OFPP site at http://www.acqnet.gov

24. Acquisition Center of Excellence (ACE) for Services linked to the OFPP site at http://www.acqnet.gov

25. OFPP Policy Letter 05-01 "Developing and Managing the Acquisition Workforce" linked to the OFPP site at http://www.acqnet.gov

Other GAO Reports:

Department of Energy: Lessons Learned Incorporated in Performance-Based Incentive, July 23, 1998 http://www.gao.gov/archive/1998/rc98223.pdf

National Laboratories: DOE Needs to Assess the Impact of Using Performance-Based Contracts, May 3, 1999 http://www.gao.gov/archive/1999/rc99141.pdf

Issue Area	Citation	Discussion
Requirements Definition Need for Objective Based Requirements	**Witness:** Robert Zahler, Partner, Pillsbury Winthrop Shaw Pittman **Hearing Date:** Tuesday, April 19, 2005 **Transcript Page:** 28	MR. ZAHLER: Too much time is spent focusing on the inputs to these processes, and not enough time on the outputs: what do you want from the result? And so, summarizing let me talk about the RFP here. Classic RFPs in my industry--and I think probably in the Federal side, also—spend enormously too much time documenting historical facts: what did we do, how did we do it, what did it cost. They have some high-level stuff of maybe what they want in the future, but all too little of that. Rather, the RFP should say, "Here are my objectives. Here are my requirements. Here's how I want to interrelate with you. Come back and give me a solution."
Requirements Definition Impact of Rigid Requirements on Changing Business Needs	**Witness:** Robert Zahler, Partner, Pillsbury Winthrop Shaw Pittman **Hearing Date:** Tuesday, April 19, 2005 **Transcript Page:** 12	MR. ZAHLER: [The] Second difference--which is a little bit unique in the sourcing area, but has general applicability, is that these services that my clients have purchased change and evolve over time. And it turns out it's very hard to specify a mechanism to both procure and price and measure and deal with services that evolve over time. I like to tell people that words of specificity can be words of limitation. So, whereas my clients' first reaction is, "Bob, let's write down absolutely everything we do, make sure the supplier does absolutely everything we do." That turns out to be a failed strategy. Because very quickly, change happens. And you really want them to do something else. And as soon as you say that, they say, "Not in the contract. Change order. Extra cost. More time--"--you know, procure the assay. And so the idea is to write the scope of services in a way that creates variability in a disciplined, structured, controlled manner.
Requirements Definition Clearly Defined Outputs	**Discussion:** Frank Anderson Robert Miller **Witness**: Robert Miller, General Counsel, Procter & Gamble **Hearing Date:** Wednesday, March 30, 2005 **Transcript Page:** 83	MR. ANDERSON: I'd like to summarize what I think I heard and then ask you if that is an industry practice or a company practice as a result of your experience. You basically said when you shape these contracts, you use a detailed statement of the work, and you kind of emphasized that when you went through; the structure of the statement of work, which was detailed: long-term agreements, and your preference would be 10, and five and seven would appear to be a backup; a declining price curve; and a structured termination agreement for poor performance. Is that a common integration of elements in the industry, or is that a derived practice in your organization? MR. MILLER: I think it's pretty common for the way a lot of this IT-type outsourcing is done. MR. ANDERSON: Would you comment on the detailed statement of work? How detailed? Because we tend to think in terms of getting out of the how business and leaving that up to the contractor, but you seem to have

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<td>emphasized that detailing what you expect them to do is important.

MR. MILLER: Yes and no… [W]hat needs to be detailed is the outcome of the work or what the specifications are…. You're best to leave to the experts how to do the work, and it may well be they've got some experienced trade secrets, some kind of competitive advantage that enables them to do that more effectively or efficiently than somebody who is not the expert does.

So when I say the detailed statements of work, think of detailed specifications for what you want the output to be. How they get there, though, I think is something that…you ought to rely on the vendors to figure out the how, within, again, certain limitations of, you know, in compliance with law and such.</td>
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<td>Requirements Definition

Strategic Objectives versus “My Mess for Less”</td>
<td>Witness:
Todd Furniss, Chief Operating Officer, the Everest Group, Inc.

Hearing Date:
Wednesday, March, 30, 2005

Transcript Page: 120</td>
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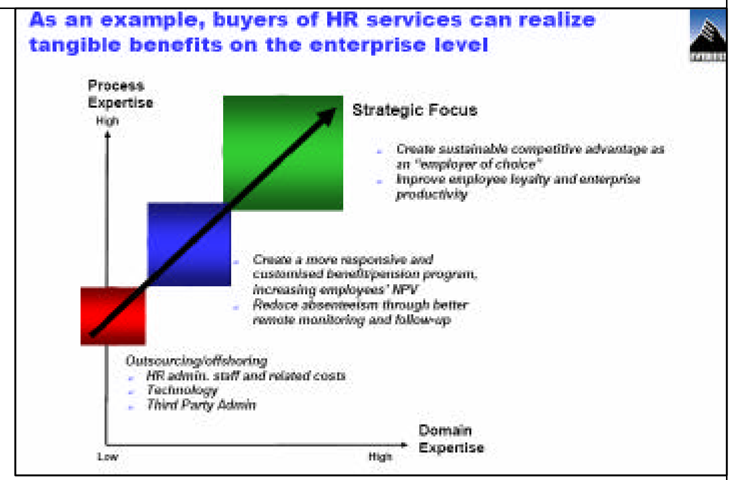

MR. FURNISS: …[R]ecognizing that this may be both somewhat heretical or oversimplified... I'll walk you through an example. If you were looking simply at outsourcing HR in this example, and you are simply focused on the unit costs of third-party administration for benefits at unit costs for technology, at unit costs for HR administrative staff and related costs, we would call that a red dot deal, something in the lower left-hand corner. (Image Reference: Furniss Presentation Slide #10)

However, …you may or may not be aligned with the corporate objectives if the corporate objectives include things like I want to be the employer of choice; I want to reduce employee attrition, okay? So the fact that you have the lowest benefit costs does not necessarily mean that you are inspiring your employees with good benefits.

So you can see that if you're focused on the myopic, you can actually do something quite counterproductive to corporate objectives. In fact, one of the terms that's frequently used in… the lower left is your mess for less, okay? You're not focused on changing much; you're just talking about doing it less expensively. And the term that tends to be used in the upper right hand corner tends to be transformational in nature, meaning that the suppliers are focused on changing more and offering more feature function benefit with a different set of economic alignments in the interest of driving the business forward at the organizational level; okay.</td>
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Requirements Definition Baseline Performance versus Cost, Strategic Objectives	**Discussion:** Carl DeMaio Todd Furniss **Witness:** Todd Furniss, Chief Operating Officer, the Everest Group, Inc. **Hearing Date:** Wednesday, March, 30, 2005 **Transcript Page:** 132	MR. DeMAIO: …Could you give me a little more detail on if we're talking about weighing costs versus performance, what are some of the things you would suggest we articulate as kind of standards or best practices? And second of all, I don't know if you're familiar with the term statement of objective, but in performance based contracting, we have the statement of work, which are the details of the activities, or statement of objective. And it sounds like that what we call statement of objective is what you're talking about in terms of the business case. What is the value? What is the outcome that the agency wants to achieve and then let the provider kind of look at the situation and propose the solution. Based on that definition of statement of objective, is that consistent with the model that you're finding successful in the corporate world? MR. FURNISS: Somewhat. Let me, if I may, develop that a little bit. We're not saying that you don't look at cost. We're saying that cost is simply one of many criteria by which we would evaluate the proposals being put forward. And so, what we're saying, and this, again, depends on the strategic objectives of the firm…. So the objective is how do you weight the criteria, and how are you managing the criteria to satisfy the objectives, right? And then, you kind of drive down that. Now, that's the hard part, and it's subject to a lot of contentious dialogue, debate, name calling and the like, because you have, quite honestly, legitimate interests that are competing, particularly when you get it at the right level, right? …The other thing is that…all corporations are different… for example, a Nike would be doing as primarily a marketing firm with virtually no manufacturing capabilities, they're going to approach the problem in a very different way than, say, General Motors, which tends to be more, although not nearly the way it used to be, more vertically integrated… So you have to really understand what the buyer's objectives are at the strategic level. It sounds like something a lot of folks would say, but you have to follow it all the way to the ground to understand how it really ties together. Your second question … is the statement of objectives. The business case is really sort of a quantitative and qualitative analysis of what's going on. It says look: we've done some preliminary work in the industry talking to suppliers. We understand what's going on with your financials; we understand what's going on with your business objectives. We understand where you want to go in terms of a high level or a preliminary view of a future state of operations at some point in the future, and given that collection of information, we recommend X…. So there's some of that qualitative and quantitative information that we call the business case, okay? It's not simply we think you can get, you know, a $10 million NPV given this term and this horizon and this discount rate. Does that help?

Requirements Definition Cost of Objective-Driven Transformation change	**Discussion:** Al Burman Todd Furniss **Witness:** Todd Furniss, Chief Operating Officer, the Everest Group, Inc. **Hearing Date:** Wednesday, March, 30, 2005 **Transcript Page:** 138	MR. BURMAN: When you're looking at trying to get these transformational results down the line as opposed to the tactical let's save a little money on doing what we're doing today, I would expect that there are probably some near term costs for the company in order to get from here to there. Is that something that you explicitly recognize in discussions with them and go through that-- … --so you say hey, over the life cycle, this is where we're going to go, but you have to understand that up front, you may well have these additional kinds of expenditures you have to deal with? MR. FURNISS: Absolutely. There will be a cost. There's a migration cost under any circumstance on virtually every transaction. There's a cost to migrate from the existing environment to the supplier's capabilities. Those costs will be expressed quite clearly in the proposals and the pricing structures that are set forward, and then, there is a lot of haggling, usually, that goes on around how you might pay for those costs. So one question is when? And another question might be how? The question as to whether or not they exist, that is seldom at issue. The question is usually when do you pay for them? …There are any number of mechanisms that you can choose to get there, but the question is right on target…. …And the same dialogue goes on with the transformation that happens with the migration: how are you going to pay for it, and when are you going to pay for it? The when has different operational implications, however, because you have some organizational readiness issues, right? To transform the organization requires that you prepare the organization in a different way, because services will fundamentally be delivered in a different way. Some stuff won't get delivered at all, and the remaining services will be delivered in a different fashion; some attributes of a process may not be followed because they can be [unsettled.] They are no longer relevant or important to the reengineered process, for example. MR. BURMAN: Can you ask the bidder to address that? MR. FURNISS: Absolutely, absolutely.
Relationship Management Understanding Vendor Motivations	**Witness:** Robert Zahler, Partner, Pillsbury Winthrop Shaw Pittman **Hearing Date:** Tuesday, April 19, 2005 **Transcript Page:** 14	MR. ZAHLER: You know, the proposition is: the likelihood that a supplier will do what's in the contract has nothing to do with whether it's in the contract. It has to do with whether their interests are aligned in doing that particular service, that particular function. And so the reality is--I mean, they'll pretend to comply with the contract. I'm not suggesting that people just ignore these documents. But, actually getting performance depends on aligning the interests of the purchaser and the supplier in ways that are very nuanced and very complicated, and not easily put down on paper.

Relationship Management Developing the Relationship	**Witness:** Peter Allen, Partner and Managing Director for Global Practices, Technology Partners, Inc. **Hearing Date:** Tuesday, April 19, 2005 **Transcript Page:** 159	MR. ALLEN: In our opinion--and based upon our 15 years of doing this in the industry--how the contractual agreement is achieved--the journey we take to get to an agreement between a buyer and a provider of services--is just as important--and some would argue, even more important--than what the final contract includes. It's all about developing a relationship. …[T]he early buyers of outsourcing were defense contractors…. And they were trying to apply the same sort of procurement-regulation approach--right?--we're going to write down all the requirements, going to issue our RFP, we're going to get our proposals back, we'll read them. And we found that that wasn't actually resulting in a relationship. It was resulting in a transaction. And so the industry has really moved over the last 15 years to focus on how we actually get alignment on what the services are, how they're going to be delivered, and at what price. This is all about defined services at defined prices. Without that, it's not an outsourcing relationship. It's got to be defined services at defined prices. And the process we use to actually get agreement on what those services are and what those prices are, and what it means to have the relationship is just as important as what the contract might say. So I test on some of these things; some of the "how" points that are critical for us. [Slide.] There needs to be, in our mind, and in the minds of every client that we're serving today, a focus on a vision and strategy for the functions that support the business strategy. There has to be a value-creation orientation.
Relationship Management Workforce Skills, Aligning Business Interests	**Discussion:** Carl DeMaio Marcia Madsen Peter Allen **Witness:** Peter Allen, Partner and Managing Director for Global Practices, Technology Partners, Inc. **Hearing Date:** Tuesday, April 19, 2005 **Transcript Page:** 203	MR. DeMAIO: Very quickly--all three presentations today have focused on relationships; that it's not the contract, it's the relationship that you're building. And so that the point does not get lost on the government audience—our culture in government typically is that you don't worry about the private sector, you're there to protect taxpayer interests and, frankly, there's a lot of distrust sometimes of the private sector. ….This is a pretty provocative, or simplistic, statement. Are you saying that our contracting officers might need some more emotional intelligence? That we really have to--as Josh's group is working on--look at the acquisition workforce skill set as more soft skills, not just the technical skills? MR. ALLEN: Yes, I would certainly think soft skills are very, very important to this. I can't tell you the number of problems… we got resolved at a local pub; you know, six o'clock at night, you know, "Let me explain to you what this really means to the business." And that's how business occurs. It's relationship based. Now, does that mean you have to give sort of soft-skills training to your contracting officers? I don't think that's anywhere near sufficient. I think it's about how you get to these relationships in the first place; less of a paper exchange and a price fly-off, and more of a focus on alignment of objectives and business expectations. MS. MADSEN: In terms of your last answer--how you start those relationships, how you align business interests--how do you do that and still have a competition?

		MR. ALLEN: This is great. This is actually where we have a lot of fun. I mean, it is very competitive, because everyone wants to compete for a relationship. And once they understand that this isn't about getting through a hoop, this is about forming a mutually beneficial, long-term relationship, all the dynamics change. All the dynamics change--still in a competitive setting. Still will you have four, down to two providers that are there trying to earn the right to serve the client. You get executive attention, you test the mettle of the organizations to really buy into it. It has a lot of good and beneficial effects in the competitive setting. MS. MADSEN: And you use it in a competitive setting. MR. ALLEN: Absolutely. Absolutely. If we do our job right, the providers have put their best foot forward. The clients have seen the best that the providers have to offer. They're in the same relative range of price so that the differences are understood, and they're able to make a selection based upon a relationship.
Managing and Monitoring Performance Process and Personnel	**Discussion:** Al Burman Neil Hassett **Witness:** Neil Hassett, Assistant General Counsel, United Technologies Corporation **Hearing Date:** Tuesday, April 19, 2005 **Transcript Page:** 132	MR. BURMAN: On the performance based, again, for the government, one of the issues been: how much time is spent up front defining surveillance plan, a quality assurance plan--a to monitor whether or not the contractor's successfully, and defining who does that job, and making sure there's somebody there that's paying attention. Who, in your environment--say, in the IT services, where you've outsourced those services--do you have somebody who's specifically tasked with monitoring whether or not they're performing well… [D]o you have a set of people who are trained in doing that role? Or who would be doing it? MR. HASSETT: In something that large, like our IT outsourcing that we utilize CSC--yes, we do have at least one individual, and perhaps support for that individual, who keeps track of performance. MR. BURMAN: And that's a defined role for that individual. That's their job--full-time job. MR. HASSETT: It's a defined role, but the full-time I'm not so certain about. But as one goes down in complexity—down in size of the business transaction--we wouldn't have a full-time person. …But we like the supplier to keep the data and actually, on their invoices, provide the credits on an ongoing basis.
Managing and Monitoring Performance Measuring the Right Things at a High Level	**Witness:** Robert Zahler, Partner, Pillsbury Winthrop Shaw Pittman **Hearing Date:** Tuesday, April 19, 2005 **Transcript Page:** 25	MR. ZAHLER: Lastly--you know, performance measurement, people tend to measure too many things at too low a level. It serves no purpose. Our clients universally tell us--universally the suppliers meet every since service level, yet my end-users say the service stinks. And the reason is because they're not measuring what the end-user sees as the relationship: the end-to-end result. To be able to measure the end-to-end result--not easy. I'm not going to say it's easy, but to be able to do it, you had to give the guy some end-to-end responsibility.

Managing and Monitoring Performance Metric Creation and Management	**Discussion:** Al Burman Robert Zahler **Witness:** Robert Zahler, Partner, Pillsbury Winthrop Shaw Pittman **Hearing Date:** Tuesday, April 19, 2005 **Transcript Page:** 76	MR. BURMAN; …On the metrics that you're using--once you've got the contract, people are performing the work, how flexible are you on those metrics, and do those metrics ever show up in contractual documents. MR. ZAHLER: The metrics always show up in the contractual documents, otherwise they don't serve any purpose. I mean, you can talk about hortatory type things, but it doesn't change people's actions, if you will. And so if it's not actually documented, it's not going to produce any results if it's actually measured… So our standard contract now says that whatever metric is there, you've got to put in place mechanisms to actually monitor and measure them. Business focused metrics are very, very difficult. I do not want to mislead you. Most of these deals do not have such metrics--okay? Very hard to come up with them; very hard for the client to even identify them; very hard for the supplier to even agree to them. What we try to do, though, is focus on things that are fairly objective. So one of the solutions is the supplier says, "We do customer satisfaction surveys." And they'll actually put proportions of their payment at risk based on customer satisfaction surveys. Not as great as you would think as a mechanism. It's okay. But, in fact, you actually get into fights about who you're surveying, what are their interests? What's the result? And the other thing is--and the government knows this well, from a lot of bad contracting--regardless of how the metrics come out, if the guy's actually been performing, you just cannot fail to give him something--okay? Because you'll death spiral a poor performance going back. If they think you're not being fair in using these performance-based metrics, it's like "game over," if you will. So, there's a lot of sophistication--I'm going to say nuance--forget sophistication--about how you apply this. One of the mistakes our clients make is they almost never follow the contract. But the other mistake is equally true: just holding the guy to the--we write contracts such that the supplier is in breach of the contract every day; impossible to perform literally to the contract. That doesn't mean that you call them on it. You need to understand when you call them and when you don't call them on it. I think our clients overreact--you know, their view the best contract is the one you put in a drawer and never look at again. But as soon as a client says that to me, I conclude they don't understand the sourcing paradigm. Because these contracts are constitutions that provide road maps for how conduct should take place. Contracts that you never look at again are one-time things. I sell a piece of property. The only reason I pull that out is because there's something wrong in the sale. Ongoing relationships, the contract specifies how the parties interact with each other, it provides guidance. If it's well constructed, it's a set of principles that say how you should act.

		Long-winded answer just to say: don't over assume that the commercial sector is doing any better than you are. I actually think the Federal government does better on performance-based contracts than the commercial sector. You have more of it, you apply it more, and you've spent more time thinking about it.
Managing and Monitoring Performance Measuring Customer Satisfaction	**Discussion:** Al Burman Marcia Madsen Peter Allen **Witness:** Peter Allen, Partner and Managing Director for Global Practices, Technology Partners, Inc. **Hearing Date:** Tuesday, April 19, 2005 **Transcript Page:** 159	MR. BURMAN: I'd be interested in your views on customer satisfaction as a metric. Do you find that being used much? Does it work, not work? Much experience with it? MR. ALLEN: It's used a lot, and it doesn't work. MR. BURMAN: And it does not? MR. ALLEN: Yes. It's used a lot and it doesn't work. MS. MADSEN: Why? MR. ALLEN: Yes. The science of customer satisfaction measurement just isn't there to result in actionable indices on outsourced services, in our opinion. We think that they should be used to get the general sense of satisfaction, and perhaps identify some high level issues. But other than in a case of immediate testing of the quality of service that you could take some immediate action on the service delivery model, it only causes--in our opinion--frustration on the side of the client that says, "I gave this feedback and nothing changed," because you didn't change fast enough, and confusion on the part of the service provider that says, "I don't know what all this input is telling me." So I think it's the science of--but it's always used. It's always used. You know, and a lot of the providers will tell you: "We're going to commit to continuous improvement in client satisfaction. We're going to measure it every day, or every hour--" whatever the heck it is --but does it actually take root in the services? Generally, no.
Managing and Monitoring Performance **Effective Use of Contract over Time**	**Witness**: Robert Miller, General Counsel, Procter & Gamble **Hearing Date:** Wednesday, March 30, 2005 **Transcript Page:** 83	MR. MILLER: ….In reality, over a five to seven year term, or as people start to put a contract in place, what you sometimes find out is that the folks actually on the front line managing the interface don't often check the contract as they go through; sometimes, the deal is put on the shelf and largely forgotten, and actually, the vendors like to encourage this. That gives them more flexibility. Often, some of the people who are involved in managing the project were not involved in the negotiation of the transaction. They may not have a full knowledge of the contract. As events unfold, where there are departures from the agreement, sometimes, those aren't recognized by the

		people in the front line. Life being what it is, not everything is anticipated; even the best lawyers and people who work in the area substantively are not going to be able to anticipate everything, and so, there are going to be modifications, and sometimes, those just get executed. They're not in the agreements. There are often tools for monitoring the agreements that sometimes are not really utilized to the fullest by the people managing the arrangement. Now, obviously, there are certain levers or advantages that a careful buyer tries to put into these types of contracts to enable a successful delivery of the services and the costs and also to remain competitive. One of the key ones is benchmarking; essentially, in many of these deals for IT services, the vendor has a right to go out and make sure on an annual basis that the vendor is delivering competitive service levels. Additionally, there's usually some kind of a negotiation that the price is going to continue to be competitive during the terms of the agreement. Obviously, it's a negotiation between the parties, but the example I use showed that they have to be competitive within the top 25th percentile of prices in the marketplace.
Managing and Monitoring Performance **Oversight Function – Organization and Staffing**	**Discussion:** **Al Burman** **Robert Miller** **Witness**: Robert Miller, General Counsel, Procter & Gamble **Hearing Date:** Wednesday, March 30, 2005 **Transcript Page:** 83	MR. BURMAN: One of the challenges that we're dealing with is contract management, contract administration, contract oversight, seeing that you're actually getting the results that you're asking for out of these kinds of deals. And the question I had was who does that kind of oversight for you? Do you have a special group of people who are designated to do that, they understand that is their role, and are they trained in some way to perform that function or is it sort of other duties as assigned kind of a role? One of our challenges is looking at the work force, their competencies, and how they deal with management on the government side when we're getting people to focus on outcomes and results. MR. MILLER: I'm not sure one size fits all, but I think what the experts in this industry will be, and I don't purport to be an industry expert, but what the advice we have gotten is that you do need a governance mechanism for the contract which is usually made up of a project executive and some experts in the field that if not their full time job, it's at least the majority part of their job to continue to monitor that the services are delivered, to work closely with the vendor, and so, it's a long way of saying usually there are dedicated people, obviously; it depends on the size of the deal and the complexity of the deal and, you know, a full-time job for somebody? But on something like this that goes on for five to seven years and involves several hundred million dollars in spending, then, that is generally a full-time job.
Managing and Monitoring Performance **Oversight Function – Organization and**	**Discussion:** Joshua Schwartz Robert Miller **Witness**: Robert Miller, General Counsel, Procter & Gamble	MR. SCHWARTZ: I wanted to jump on the question that Al Burman had asked you earlier but back it up and broaden it. Al had asked you about the contract management or surveillance function, but I wanted to ask about where in your organization all of the tasks that enter into outsourcing these services are performed. What kind of people are doing it? Where in the organization are they placed? Is there an acquisition department as opposed to the consumers within the company playing the primary role, qualifications for personnel? Because government faces all of these challenges…. And we're hoping to learn from your

Staffing	**Hearing Date:** Wednesday, March 30, 2005 **Transcript Page:** 98	experience. MR. MILLER: As it relates to the contract management, generally, a team from the people who are doing the work are the ones who are actually responsible for the contract administration. Call it the people that have some of the technical expertise of what goes in to delivering these services. They're familiar with, you know, how the thing ought to work and, you know, what's actually necessary for success under the operation of the agreement, and so, I would put them under the heading more of the technical experts do the ongoing management of the agreement. As it relates to actually cutting one of these deals, it's kind of a team that you need to get set up. You need somebody that's got the technical expertise. It's useful to have somebody who's got some transactional expertise to work on these matters also, because they are contract negotiation ultimately. It's not necessarily a normal acquisition or a divestiture where you have the same levers that you do in an M&A deal, but there are also some commonalities. MR. SCHWARTZ: Could I ask about the role that your lawyers play? MR. MILLER: Well, I guess there are two roles, if you will, one of which is these types of transactions, we have a team of both inside lawyers, and we hire some outside lawyers who are truly expert in the industry to help negotiate these agreements with us. And not only are, you know, they're good lawyers and all that, but what they also provide is an understanding of kind of the currency in the industry; you know, what is the norm? What's reasonable? When you look at some of these terms, some of the aspects of it in a vacuum as a general lawyer, you know, that's what I consider myself is more of a jack of all trades, because I have to do a lot of different things versus being an expert; you know, you look at some of the terms that are standard in the industry, and your initial reaction is, you know, I wouldn't agree to that if I were on the other side, but in fact, that is the currency in the industry. So an important perspective is brought as to how the industry works, and, you know, what is, you know, a fair assessment of where the risks should be and what the duties should be. And then, you have, you know, the normal legal functions of negotiating an agreement, doing the drafting, and then, what I call managing the management through most of these.

"Downselecting" The Right Number of Competitors	**Witness:** Robert Zahler, Partner, Pillsbury Winthrop Shaw Pittman **Hearing Date:** Tuesday, April 19, 2005 **Transcript Page:** 69	MR. ZAHLER: …The RFP or the requirements document needs to focus on both of those: what are their capabilities to do the work, and what are their commitments they're prepared to make to you. Once you've done that, then I really suggest you down-select to two. I have to tell you: three is exponentially more time consuming. And so I get pushed back all the time; "Bob, can't we do three?" And all I can tell you is: exponentially more time-consuming. And it's confusing, because it's very difficult to keep the deals separate in each parties mind. But then when you've got two, then you can drill down in both the capabilities and the commitments points to understand what it is that is actually being offered to you, and what is the price that you're going to get, what's the supplier's.
"Downselecting" The Right Number of Competitors, Selecting Competitors	**Discussion:** Dee Lee Robert Miller **Witness**: Robert Miller, General Counsel, Procter & Gamble **Hearing Date:** Wednesday, March 30, 2005 **Transcript Page:** 89	MR. MILLER: Going to what I'll call reliability, we had I think it was four vendors in the process. A lot of that was really driven by call it a first cut at the marketplace as to who would be able to deliver the services and who we would have confidence in partnering with for an extended period of time versus open it up to call it all bidders to try to determine who had the wherewithal and the capability to deliver the services we needed; also over that five to seven to 10 year contract period, be able to bring some technological innovation and change and more or less handle it out along the way. So there was some setting of requirements up front that, you know, I guess the government were buying a jet airplane, maybe--I don't if there is any prescreening of vendors, or it may well be just because there are only so many people who can build airplanes, you have a limited buy set. So we would do some screening up front to make sure that, at the end of the day, we would get something, and we would have the reliability involved.
"Downselecting" Ensuring Opportunities for New Market Entrants	**Discussion:** Marsha Madsen Robert Zahler **Witness:** Robert Zahler, Partner, Pillsbury Winthrop Shaw Pittman **Hearing Date:** Tuesday, April 19, 2005 **Transcript Page:** 88	MS. MADSEN: …You talked about competition, working with the vendors, down-selecting to two, negotiating the solution with two. How do you square that with getting new market entrants? MR. ZAHLER: Yes--so that goes to do factors: one, who are the initial people that are invited? And we spend a lot of time with our clients making sure they understand the market, and they understand what's available. And we then talk--you know, part of the tactical analysis is the end game, because we try to look ahead a number of steps and create foils, if you will. But I have a very clear principle: if you're not going to contract with this new entrant--even if they wow your socks off--let's not put them through the process. So you've got to get a commitment that, in fact, the process is going to have some aspect of fairness to it. Sometimes it doesn't always happen even after that commitment is made. But the second thing is: we do encourage this partnering type activity. And it's dicey. And what's dicey about it is, you actually do not want to be a marriage-maker. You don't want to force these guys together. You want

		them to see the attraction themselves, and sort of come to you and say, "This makes sense." And that's not always easy to pull off, quite frankly. And sometimes there are some back-channel discussions that take place to encourage that result. Again, these are things that may not always be appropriate or available in the government sector. There are lots of birdies who whisper at lots of people. The other thing that I've found is: the suppliers have incredible market intelligence themselves. Oftentimes it's wrong, but they spend lots of time with market intelligence about what they understand in a competitive procurement.
"Downselecting" Process for Downselecting	**Witness:** Neil Hassett, Assistant General Counsel, United Technologies Corporation **Hearing Date:** Tuesday, April 19, 2005 **Transcript Page: 109**	MR. HASSET: We issue the RFPs to, say, four organizations. Then we have a question-and-answer session, where the bidder asks questions--all four come in for usually five or six hours, and UTC, with its subject matter experts and its supply management people answer the questions. Then the proposals come in--four proposals. And they're voluminous. They're big--and it's got all the electronics. And then we get to ask the questions. These are usually sessions a day each--day-long--and we ask the questions, they provide the answers. [Slide.] From that process we down-select to two. And that down-select is a group of people--I mean, lots of people--and it's very analytical. I mean TPI has set up charts for us. So we fill in the charts, and a winner pops out analytically--not always, but we down-select to two and it's very rigorous. Then we negotiate with the two bidders. These are full negotiations.
"Downselecting" Process for Downselecting	**Discussion:** Ty Hughes Neil Hassett **Witness:** Neil Hassett, Assistant General Counsel, United Technologies Corporation **Hearing Date:** Tuesday, April 19, 2005 **Transcript Page: 127**	MR. HUGHES: [When] you down-select to the four in outsourcing, was it through the RFI process, or market research that you get the universe of four. MR. HASSETT: To date, we have used the RFI process, a relatively informal questionnaire relative to capabilities. And then we look at all of those, and decide who are the four we should go with. So we do use the RFI process.
"Downselecting" Commercial Best	**Discussion:** Ty Hughes Todd Furniss	MR. HUGHES: Could you talk a little bit about where you see the best commercial practices diverging from how the government outsources? You gave one example on information where we and the Government tend to put everything in writing and it tends to go out to everybody, and I think by implication, you're saying in a

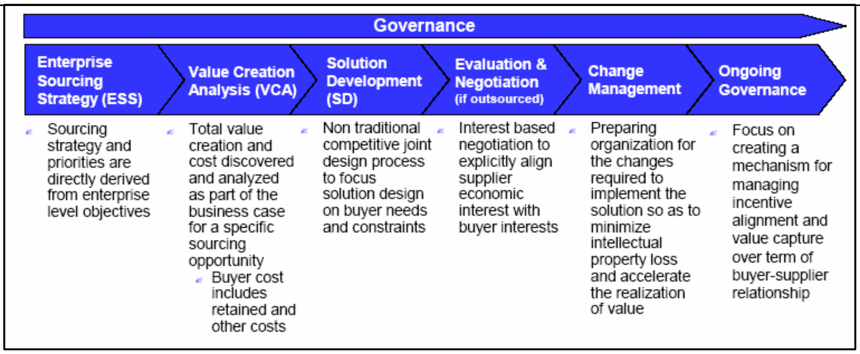
Practices for Procurements	**Witness:** Todd Furniss, Chief Operating Officer, the Everest Group, Inc. **Hearing Date:** Wednesday, March, 30, 2005 **Transcript Page:** 140	commercial outsourcing, maybe there's other way of communicating requirements. … And the status of the company. Are there other areas like that where the commercial practice diverges quite a bit from how the government outsources? MR. FURNISS: Yes, I think there are. I mean, there are a handful. I guess three or four would leap to the forefront, although I don't think that the government's objectives are unavailable using commercial best practices, although slightly altered. So, for example, you know, the idea around full and fair competition and allowing virtually anybody to bid, right? You can do that, but the way you get to the answer cannot include 70 suppliers. You just don't have the time to interact with them. Virtually everybody on these assignments who is on the buying side creates a project team. The project team usually has a full time job doing something else. When you get into things like negotiations, the tax on the project team is immense, okay? And many orders of magnitude on the supplier side, and I've seen like organizations developed on a project basis; you know, it's not uncommon to have 125, 150 people or more in a commercial transaction working on just this for some period of time. So the cost just to pursue the transaction is high. Now, there's limited time. Even if they are 100 percent dedicated to this activity, there's a limited amount of time that those people can interact with every supplier and give them the same amount of information. So we would agree that we want everybody to have the opportunity, but we would also agree that you would have to have a fairly acute funneling system to get it down to a much smaller number rapidly. It's impossible to go through a process like the one I've described with more than three or four suppliers. It's almost completely impossible to do negotiations with more than two. It's just too hard, too complex; returning the drafts, doing the economic analysis is just too hard. It means they're very large, complex activities. So one thing would be keep open and fair competition allowing everybody to play. I think that can be done, but it's not something that happens in the commercial sector, okay? The most I've heard because of so much political pressure being put on the board of a $6 billion to $10 billion organization, we started with 14; within three weeks, I think, we were down to three, okay? So a very rapid ramp down to the number of potential providers, because it's quite clear who can really do the work very quickly, and it really is unfair in the broadest sense; it's unfair to allow them to spend their money in futility. And then, they kind of feel like they have to do it, and you feel like everybody should have the chance, so let's go ahead and let them play. It's just a waste of money, because the probability of success is so limited. That would be one. The second is the RFP process in the commercial sector and the way that we do it starts off, you know, we tell the suppliers when we're doing the business case just give us two or three smart people, okay? We're going to spend some time whiteboarding a solution, okay? Just very, very cursory, let's kind of look at the problem; let's explain what we find in our current environment and tell you a little bit about what we want to do. Small

		workshop, few people, a cup of coffee and a whiteboard is all you need, okay? It's not sort of moving, you know, the entire left flank into the activity. The second thing is that we really work, and it's not all that uncommon for us to have a different RFP, in your terms, for every supplier, okay? And the reason for that is because we want the bids to reflect their strengths and weaknesses, okay? So what it does is that RFP reflects the discussions we've had with those suppliers to date. Now, that raises a separate issue, which is one around confidentiality. You know, you kind of have this balancing act that you always have in the Federal Government with everything being public and, you know, no horse trading going on in the smoke-filled rooms but also allowing for innovation, creativity, and proprietary approaches to be delivered in the best interests of the government as the case may be. So that would be a second issue that I see is at a tension point right now between governmental practices and commercial practices as I know them, limited as that knowledge might be. A third is the way that some of the public policy interests might unfold, things like small, disadvantaged business plans and the like, those are not very often done at all in the commercial sector, not to suggest that they shouldn't be done, but they just cannot be done virtually at all. There was a big push in the eighties and nineties to do it because it's kind of a flow-down operation from the Federal Government; it happens far less frequently now. And the other thing is that we can be much more aggressive in our arrangement of marriages, if you will, between the suppliers, so we can say look: individually, you don't have a very high chance of success here; however, if you team with this supplier to provide these services, there's a way that you can participate in this transaction or you might be able to participate in this transaction. At the end of the day, our obligation as advisors is to do what we can to do two things: one, make every supplier look as good as that supplier can look in providing a solution that solves the buyer's problem; and secondly, and this is maybe a little bit odd, we are in the business of comparing apples to oranges.
"Downselecting" Ensuring Competition among Limited Number of Bidders	**Discussion:** Marcia Madsen Todd Furniss **Witness:** Todd Furniss, Chief Operating Officer, the Everest Group, Inc. **Hearing Date:** Wednesday, March, 30,	CHAIRWOMAN MADSEN: … When you talked a few minutes ago about you get that group of 14 down to three, and then, you know, you focus on the strengths and weaknesses of the three, what kind of a competitive process is going on once you've got the three? Is it still a head to head competition? MR. FURNISS: Yes, and what we're doing, I want to emphasize that what we're doing is we're not competing only on price. We are actively investigating, examining the solutions that they're offering and how they're built, because we want to see is there something we can do to help change that cost structure, right? So let's give an IT example. Let's say we have a situation where there is a requirement that the data center have certain security measures implemented around it, right? You've got to have berms running around the perimeter; you've got to have barbed wire fences after you get to the berms. You've got to have biometric

	2005 **Transcript Page:** 146	scanning. You've got to have card readers. You've got to have armed guards at the gate, right, all of that stuff, and it has to be dedicated, okay, meaning it can only do the work of the particular buyer that you are serving, that one particular buyer, okay? So if you understand that the solution of all the suppliers is to, in fact, go with the dedicated data center, you then say, well, what happens if I relieve that constraint? What happens if I can satisfy all of your needs for that security regimen; however, you, Mr. Supplier, I'm going to allow you to provide it in a leveraged data center, meaning that other buyers will also have their work running out of that data center, all right? Now, all of that cost, a lot of that cost has gone away. It's a fraction of what it would have been originally, right? So you take a look at that, and you say well, what is the driver? Well, the driver is critical mass and scale. Well, in certain instances, that's not really a big driver. I can give you a case in point where a transaction I was working on back 100 years ago when I was with my former employer, the data center capability, the combined data center capability of this particular client was 75 percent as large as the company I worked for, the second largest in the industry. Well, they're not going to do that deal for leverage and scale, right? They're going to do it for other reasons. And so, relieving the constraint may not have been material in that instance. So it's really understanding what those things are, and generally, it's things like labor arbitrage, process disciplines, critical mass and scale, a handful of other things that you might look at and process. Does that help?
Cost Definition Commercial Observations – Myopic Focus on Unit Costs Reduces Overall Value	**Witness:** Todd Furniss, Chief Operating Officer, the Everest Group, Inc. **Hearing Date:** Wednesday, March, 30, 2005 **Transcript Page: 116**	MR FURNISS: …We observe certain commercial principles, and those kind of drive our procurement process, okay? And so, what I thought I would do is air those out so that we at least have them on the table. First of all is the total solution cost does not equal the total potential value for the buyer. One of the mistakes that we have commonly found is that the myopic perspective on unit costs or the sum of unit costs as being the answer to solution costs can drive the wrong behavior. And it can decidedly diminish or if not eliminate broader-based value for the buyers of these services.

"My Mess for Less" Commercial Observations – Need for External Supplier into Solution	**Witness:** Todd Furniss, Chief Operating Officer, the Everest Group, Inc. **Hearing Date:** Wednesday, March, 30, 2005 **Transcript Page: 116**	MR. FURNISS: We do believe that suppliers' commercial incentives drive continuous improvement in their core business. And what this means is that we should not, again, necessarily dictate the process, I mean, the solution to the client. Let me put this into perspective, if I may: when you think about it, the idea that a particular chief information officer, chief procurement officer, chief resources officer coupled with his internal team which have historically had a client universe of, in fact, one, the buying organization, would come up with the optimal solution to their particular problem seems to us on the face of it to be a fool's errand, and the reason that we take such a strong view on it is that it seems to us self-evident that you should at least tap into the insights of the supplier community, who have literally tens of thousands of institutionalized years of customer experience in the form of best practices, some of which certainly would apply to this customer's problem. So at least folding that into the thinking of the buyer is, on the face of it, a proper thing to do; engaging the community in an open dialogue and a transparent exchange of information is a critical aspect of the solution development process itself.
End-to-End Procurement Processes Commercial Observation - One Size Does Not Fit all	**Witness:** Todd Furniss, Chief Operating Officer, the Everest Group, Inc. **Hearing Date:** Wednesday, March, 30, 2005 **Transcript Page: 117**	MR. FURNISS: In many ways, it's kind of a tautology, but we do find that all buyers and all suppliers are, in fact, different. Now, if all buyers and all suppliers are different, then, it sort of begs the question why, in fact, would you have a standard approach to a buyer's problem, and second, why would you dictate the solution to the suppliers who are bidding on it? Inevitably, someone is going to have to do something unnatural. And it seems to follow to us to be something that is decidedly overlooked in the procurement process generally across the industry. So what that means is there necessarily may be a number of optimal, quote, optimal solutions for a particular problem.
End-to-End Procurement Processes Commercial Principals for Complex Services Procurement	**Witness:** Todd Furniss, Chief Operating Officer, the Everest Group, Inc. **Hearing Date:** Wednesday, March, 30, 2005 **Transcript Page: 122**	MR. FURNISS: So if you start to the left of this slide, you see the **enterprise sourcing strategy**, which is where we come in and help clients develop how they look at things broadly. … But the procurement decisions can oftentimes be made at a functional level without enterprise objectives being kept in mind, and what that does is it may suboptimize the activity at hand. There are tradeoffs even between legitimate interests, that dialogue is never had, because it doesn't reach the right kinds of decision makers. (Image Reference: Furniss Presentation Slide #10)

We do something called a **value creation analysis**, which you might use a different term called a business case development, which offers…both qualitative and quantitative points. We find that an incomplete business case with an excessive focus on unit cost reduction rather than total cost of ownership or the maximization of value can mislead the client, can create ill-targeted benefits, can cause the wrong purchasing decisions to be made or cause the solution to go in the wrong direction.



In the **solution development** area, we …spend a tremendous amount of time in the procurement process understanding the way that suppliers make money… If you understand what motivates a supplier to change their cost structure, then, you can … logically more likely align your economic incentives, and if you don't understand that, you're going to have a much more difficult time. We also … emphasize that understanding a supplier's capabilities in an intimate way is far more important when you're buying complex services…

In **evaluation and negotiation** if we do go down the outsourcing path with our clients, it tends to be focused on the normalization of supplier capabilities. So what happens in this instance traditionally is you're forcing a unit comparison; you're forcing a normalization of the supplier solution one-on-one. …[O]ne of the reasons that it's desirable … is … because it makes it easier to predict the outcome…. So what you see here is a trend towards getting an answer as opposed to understanding the problem and creating an answer that is derived from that understanding. I don't mean to be too esoteric, but … we believe … a lot of the traditional sourcing approaches tend to ask the wrong questions….

In **change management**, we find that traditional approaches tend to provide little or no focus on preparing the organization to incorporate the new supplier relationship and the services or the servicing game provided by that supplier. Communication tends to be poor, organizational preparation in terms of how you design the retained organization, what incentive structures you create for your retained organization, how you're going to retain intellectual property and reduce its seepage are all things that tend to get lost.

In **ongoing governance**, the traditional approach to ongoing governance is really to use sort of a contract management function or a contract administration function and be very, very tactful about whether or not the change order request has met the terms and conditions of the master contract rather than a comprehensive analysis of what the strategic direction is of the buyer and the supplier; is the direction of the buyer's business still headed in the same place?