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DEFENSE INFRASTRUCTURE

DOD's Planned Finance and Accounting Structure Is Larger and More Costly Than Necessary

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The Honorable Herbert H. Bateman
Chairman
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Ranking Minority Member
Subcommittee on Military Readiness
Committee on National Security
House of Representatives

On May 3, 1994, the Department of Defense (DOD) announced a plan to consolidate over 300 defense accounting offices into 5 large existing finance centers[1] and 20 new sites called operating locations during the next 5 to 7 years. The plan, which is expected to reduce DOD finance and accounting personnel from 46,000 to 23,000, is aimed at streamlining DOD's financial operations and setting the stage for future process enhancements and budgetary savings. In total, DOD expects the consolidation will save between $8 billion and $9 billion (present value) over the next 20 years.

On August 3, 1994, your Subcommittee asked us to evaluate this plan. Your Subcommittee wanted to know if the plan reflected leading-edge business practices that would result in substantial cost reductions and high-quality customer service and included a sound implementation strategy that was achievable within stated time frames. Your Subcommittee also wanted to know when DOD would begin to save money and if the potential for consolidating finance and accounting operations had been fully realized. This report assesses (1) the process DOD used to identify the number and locations of the finance and accounting centers and operating locations, (2) the potential impact of the consolidation on customer service, and (3) DOD's plan to include leading-edge business practices in the consolidation.

Results in Brief

We see DOD's plan to consolidate and reduce personnel as a necessary step toward a more effective and efficient finance and accounting service. Consolidating and reengineering finance and accounting functions while sustaining ongoing operations, however, is a difficult and complex task. In such an undertaking it is important to strike a balance between cost considerations and other factors important to maintaining customer service and improving business operations. Based on our analysis of the

[1]DOD's five large centers are located in Columbus, Ohio; Cleveland, Ohio; Denver, Colorado; Indianapolis, Indiana; and Kansas City, Missouri.

process DOD used to select the proper number of new operating locations and decide where they should be located, we do not believe DOD achieved that balance. Specifically, we found the following:

- DOD decided to open 20 new operating locations without first determining what finance and accounting functions they would perform or if 20 was the right number to support its operations. DOD's primary emphasis during the decision-making process was on maximizing short-term cost savings, not on determining what was best from a finance and accounting business perspective.
- DOD, in selecting the 20 specific operating locations, used a process that placed significant weight on using excess DOD facilities, primarily those on military bases closed or realigned during the base realignment and closure process. As a result, 15 of the 20 locations will be housed in excess DOD facilities, even though DOD considered several of them less desirable from a customer service, cost, or quality workforce standpoint. About $173 million of military construction funding will be needed during fiscal years 1997, 1998, and 1999 to bring these sites up to par.
- DOD, for the most part, has not reengineered the finance and accounting functions that will be performed at the 20 operating locations. Thus, the consolidation may reduce the number of locations performing finance and accounting functions, but it will not likely improve DOD's business operations. Once these functions are reengineered, DOD may be faced with the need to consolidate them once again.

Although DOD is opening 13 operating locations this fiscal year and 3 more in early 1996, it will be some time before they are fully staffed and operational. We believe this provides DOD time to reconsider its consolidation decisions. Accordingly, as DOD proceeds with this consolidation process, it needs to develop an updated estimate of the number of locations and personnel needed to meet current and future operating requirements and use this information to reassess its site selection decisions for new operating locations.

Background

The scope of DOD's finance and accounting network is extremely large and complex. The network pays about 6 million people (3 million uniformed men and women, 1 million civilians, and 2 million retirees and annuitants) and more than 15 million invoices annually charged to nearly 12 million contracts. The network disburses over $250 billion annually and is the source of financial information and thousands of reports used by executives and managers throughout DOD.

Prior to 1991, the military services managed this network. There were 5 large finance and accounting centers (one for each service plus a contractor pay center) and over 300 small defense accounting offices at various military bases and installations. This network was not only inefficient (each service had unique and often duplicative processes and systems) but was also unable to produce reliable financial information and reports. To help solve these problems, in January 1991, DOD created the Defense Finance and Accounting Service (DFAS). DFAS' mission was to strengthen DOD's financial management operations by standardizing, consolidating, and streamlining finance and accounting policies, procedures, and systems. It was given management control of the 5 large finance centers and some of the functions carried out at over 300 defense accounting offices. Of the estimated 46,000 people in the finance and accounting network at the time, DFAS eventually assumed organizational responsibility for about 27,000. The remaining 19,000 people stayed with their respective military service to perform managerial accounting and various installation-related and customer service functions.

DFAS is a Defense Business Operations Fund entity. It operates as a revolving fund and provides finance and accounting services to the military departments and defense agencies. DFAS recoups its costs through various fees and charges billed to those departments and agencies. DFAS' fiscal year 1995 operating budget, which is about $2.0 billion, comes primarily from operations and maintenance funds appropriated to the military departments and defense agencies. Therefore, by reducing its operating costs, DFAS will reduce the fees charged to the military services and demands on operations and maintenance funds.

The consolidation of financial operations is a major piece of DOD's plan for achieving much needed financial management reform. Although the planned consolidation is expected to provide a streamlined and less costly infrastructure, other pieces of DOD's plan will also need to be implemented before significant improvement in financial operations will be realized. Other pieces include reengineering its business and organizational practices, standardizing financial data and definitions, and improving financial systems so they allow DOD to comply with the requirements of the Chief Financial Officers Act. Collectively, the pieces of the plan could result in major improvements to DOD's financial operations. DOD hopes to implement its plan by the end of 1999.

DFAS' first attempt to consolidate and streamline its finance and accounting operations was done through a program known as the Opportunity for

Economic Growth. Under this program, which began in March 1992, 112 communities in 33 states submitted economic incentive packages and competed for the opportunity to house a large (4,000 to 7,000 person) finance center. DFAS evaluated their proposals[2] and recommended to the Secretary of Defense five "winners." Before these winners were announced, however, the new Secretary of Defense canceled the initiative in March 1993, believing it was not sound public policy. Rather, he believed it was an auction for public jobs that placed the cost of national defense on local communities rather than the nation as a whole. He was also concerned that moving large finance and accounting centers to new cities would seriously degrade customer service.

Shortly thereafter, the Secretary announced a new consolidation initiative. Under this initiative, the Secretary directed DFAS to select a small number of sites (from 5 to 15). DFAS subsequently evaluated 132 potential locations, including most of the cities that had competed under the Opportunity for Economic Growth process and 16 bases that had been closed or realigned. After this analysis was completed in May 1994, the Deputy Secretary of Defense announced that finance and accounting operations would be housed in the existing 5 large centers plus 20 new operating locations.[3]

Better Balance Is Needed Between Budgetary and Customer Service Goals

One of the more important aspects of the consolidation initiative was for DOD to determine the appropriate size and location of its finance and accounting network (e.g., how many offices and people are needed to meet not only today's requirements but also future requirements once new systems, processes, and technologies are introduced). Size and location are important because they help form the foundation upon which the new network will be built. Wrong decisions could cause the network to be mis-sized, leading to costly future reorganizations, consolidations, or realignments. In making its consolidation decision, however, DOD's primary emphasis was on achieving short-term budgetary gains rather than on establishing the best network for meeting current and future operational and customer needs. As a result, DOD may be establishing a larger than necessary finance and accounting network and increasing the risk of creating short-term customer service problems.

[2]DFAS' primary evaluation criterion was the extent communities were willing to subsidize the cost of facilities and operations. However, community and facility characteristics were also considered.

[3]On July 1, 1994, a 21st site was added to the network. Located at Ford Island, Hawaii, this site will support DOD's finance and accounting operations in the Pacific theater.

Planned DFAS Infrastructure May Be Larger Than Necessary

Throughout both DFAS consolidation initiatives, defense managers indicated that finance and accounting operations should be consolidated into as few sites as possible. Under the Opportunity for Economic Growth process, for example, all DFAS operations were to be brought into five large centers. This carried over to the second consolidation initiative when the Secretary of Defense (on June 7, 1993) directed DFAS to analyze options for 5 to 15 sites. According to testimony by DOD officials,[4] reducing the number of sites to "no more than a handful" was essential if DOD was to achieve the savings, operational improvements, and efficiencies envisioned from the consolidation.

Following this guidance, DFAS established the Consolidation Task Force to study alternatives and carry out the site-selection process. The Senior Review Council, made up of DFAS executives,[5] was also established to oversee the Task Force's work. During the first month of its study, the task force gathered information about how to properly size DOD's finance and accounting operations. It reviewed research conducted by academia and other DOD, federal, and private sector organizations and obtained the views of 25 senior DFAS officials. It concluded that there was no "right size" for consolidation sites but suggested that the existing 5 centers should have from 1,000 to 5,000 employees and new operating locations should have from 500 to 1,500 employees. During this time, the Review Council discussed potential organizational structures that would move DOD's finance and accounting operations toward a joint operations environment rather than a military service-oriented environment. The Review Council wanted to avoid managing a large number of small organizations and dividing finance and accounting functions among many sites.

Based on this work, DFAS, in conjunction with the DOD Comptroller's staff, completed a site-selection process plan in August 1993. This plan specified 5 to 15 sites as the acceptable number of sites and 750 as the minimum number of people at each site. The plan included an explicit assumption that "larger rather than smaller and fewer rather than a larger number of sites was preferable." During the next several months, the Task Force assessed various alternatives, analyzed cost information, and deliberated over different organizational structures. Based on input from the Senior Review Council in January 1994, the Task Force narrowed its assessment

[4]Statement by the Principal Deputy Assistant Secretary of Defense, Production and Logistics, and Principal Deputy, DOD Comptroller, before the Subcommittee on Military Installations and Facilities, House Committee on Armed Services, regarding DFAS consolidation (June 10, 1993).

[5]Membership included about one-half of DFAS' 27 Senior Executive Service members. Most DFAS headquarters' deputy directors and several finance center directors were represented on the Council.

to 2 primary alternatives, each involving a target population of 23,000 employees.

The first alternative would have placed 23,000 employees at the 5 existing centers. The 5 centers employ about 11,000 people, so some facilities would have required substantial modification to accommodate the growth. The second alternative would have expanded the 5 centers to about 13,000 people and assigned 10,000 people to 6 additional sites—4 sites with 1,500 employees and 2 sites with 2,000 employees. In terms of cost, the Task Force considered several factors (e.g., personnel costs, one-time transition costs for severance pay and relocation of employees, building renovation costs, rent, and utilities) and estimated that the 2 alternatives would save between $6.4 billion and $8.8 billion (present value) over the next 20 years.[6] According to Senior Review Council representatives, six sites was the preferred alternative because it would save more money and allow an optimum consolidation of finance and accounting functions.

After further review, however, DOD officials[7] decided on a different course of action. In May 1994, the Deputy Secretary of Defense announced that finance and accounting functions would be consolidated into the 5 existing centers and 20 additional operating locations. His decision was based primarily on two rationale:

1.The cost of activating and operating 20 smaller sites over 20 years is comparable to the cost of 6 additional operating locations.

2.Twenty sites, staffed with fewer people, can be activated quicker than either of the 2 alternatives studied by DFAS. This would allow DOD to close the 300 defense accounting offices sooner and begin reducing the number of employees in the finance and accounting network—the area where DOD expects to achieve the most budgetary savings.

We have several concerns with this decision. First, it was based on maximizing short-term cost savings, not on making the best business decisions. Although these two concepts are not mutually exclusive, we

[6]Present value analysis is a commonly used technique to quantify and compare costs for multiple alternatives. The analysis considers the time value of money. The Consolidation Task Force established costs in terms of 1993 dollars and escalated them to then-year dollars using approved DOD inflation factors. After establishing these costs, the Task Force conducted present value analyses using a discount factor of 6.4 percent.

[7]A high-level group of DOD managers met several times during March and April 1994 to review DFAS data and consider alternatives. This group included the DOD Comptroller and Deputy Comptroller, the DFAS Director, and other management and support personnel.

found no analysis that suggested that 20 operating locations was the appropriate infrastructure to support either current or future operating requirements or customer needs. DOD clearly decided on the number of locations first and then attempted to determine which finance and accounting functions they would perform.

Besides not being a good business practice, this action had a direct impact on previous DFAS planning initiatives and concept of operations. Since the beginning of the Opportunity for Economic Growth process, for example, DFAS management had been planning to consolidate finance and accounting functions either within the 5 large centers or at a limited number of other locations. According to DFAS officials, larger sites gives them greater flexibility to adjust and reorganize to meet future technological, workload, and customer service changes. Under this operating concept, the DFAS Indianapolis center, which handles accounting for the Army, was planning for two large operating locations. One location would have consolidated base-level finance and accounting functions for the training and combat commands; a second site would have consolidated finance and accounting functions for logistics and depot activities. Further, the DFAS Columbus center was planning to consolidate all vendor pay functions within the center; it did not see a need for any additional operating locations. When DOD announced its consolidation decision, however, it gave DFAS Indianapolis six operating locations and DFAS Columbus two. As of April 1995, these two centers still had not settled on the functions and workloads that would operate at these locations.

Our second concern is that DOD did not estimate the costs of a 20-site option and, consequently, does not know how those costs might compare with other alternatives. During the time DOD executives were considering DFAS alternatives, they did ask the Consolidation Task Force to analyze the cost savings associated with retaining the 5 large centers plus either 10 or 15 additional operating locations. The Task Force's analysis showed that the two options would save between $8.1 billion and $8.8 billion (present value).[8] Table 1 compares the cost estimates and potential savings of the various consolidation alternatives. As the table shows, 6 and 15 locations offer about the same amount of savings.

[8]As required by the Office of Management and Budget Circular A-94, "Guidelines and Discount Rates for Benefit-Cost Analysis of Federal Programs," the Task Force conducted a sensitivity analysis by varying the cost factors (plus/minus 10 percent) and applying the 1994 DOD discount rate of 5.75 percent.

Table 1: Cost Estimates and Savings of DFAS Consolidation Alternatives (20-Year Present Value)

Dollars in billions

Consolidation alternatives	Cost of alternatives	Cost of existing structure	Estimated savings
Five centers	$21.2	$27.6	$6.4
Five centers & 6 operating locations[a]	18.5 - 19.5	27.6	8.1 - 8.8
Five centers & 10 operating locations[a]	19.0 - 19.5	27.6	8.1 - 8.6
Five centers & 15 operating locations[a]	18.8 - 19.1	27.6	8.5 - 8.8

[a]The cost of these alternatives varied according to the sites evaluated. For example, for the six-site alternative, the sites that provided the lowest cost alternative of $18.8 billion were different than those that provided the best labor force alternative of $19.5 billion.

According to a Consolidation Task Force representative, the 15-location option offers as much or more cost savings than other options because DOD's analysis assumed that the transfer or addition of personnel at new operating locations was limited to 375 positions per year, per location. More locations, therefore, would allow the work to be transferred from the 300 Defense Accounting Offices more rapidly, resulting in a quicker drawdown of personnel and an earlier realization of savings. Although the infrastructure costs associated with 15 sites is more expensive than other options, DOD believed the additional cost would be more than offset by the early consolidation. Based on this premise, DOD assumed that 20 sites would result in a quicker drawdown of personnel and even more savings. No additional analysis was done to confirm this assumption.

To determine if this premise was accurate, we ran an analysis for a 20-site option, using the same parameters, assumptions, and discount rate as the Consolidation Task Force. This analysis showed that 20 operating locations, with a minimum of 750 people each, increases the target population of the operating locations from 11,500 to 15,000. Consequently, the workforce of the 5 existing centers and the 20 operating locations would total 26,500 people, or 3,500 more than DOD's target of 23,000 people. This increases the 20-year cost of the consolidation by at least $2.8 billion (present value).[9]

In discussing the results of this analysis with the DFAS Director and other DOD representatives, we were told that 750 people per site was not a

[9]The additional cost is only for personnel. It does not include costs for such items as training, equipment, and telecommunications that will be incurred with a larger workforce and infrastructure.

minimum but rather a target and they had no intention of retaining a population of more than 23,000 people. They explained that there is really no way to tell how many people will be at an operating location, but they would not arbitrarily increase the size just to reach a planning goal of 750.

Although we agree that DOD should not arbitrarily increase the size of its operating locations, these statements raise questions about whether 20 locations are needed. All DFAS analysis prior to the site selection, for example, was based on the need for at least 750 people per operating location. Potential sites, buildings, and renovation costs were analyzed and decisions were made with that in mind. Because DOD does not yet know how many people will be assigned to each location, it has no way of knowing whether its facility planning assumptions are accurate. Consequently, it may be over- or underestimating its facility needs at the various locations.

In addition, DOD does not have any specific analysis to support its position that the 20 sites could be activated sooner to support a faster drawdown of personnel. Although it seems logical that smaller sites can be activated sooner than larger sites, much depends on the condition of the available facilities; the time needed to make necessary renovations; the time required to establish a management structure to recruit, hire, and train new employees; the time required to transfer current employees and workloads from offices that will close; and the quality of the workforce available at the new location. As discussed later in this report, DOD considered some of these factors in selecting the 20 sites, but they had little impact on which sites were selected.

Site-Selection Process Placed a Lower Priority on Customer Service

In any consolidation initiative, it is important to consider the impact on the business operation—will the enterprise be able to provide uninterrupted service to customers? DOD recognized this when it made customer service one of four site-selection criteria. According to DFAS officials, the idea was to place a high value on sites with readily available, trained DFAS employees. Even though these employees might have to learn a new functional process or develop new skills, DOD assumed that a core group of DFAS employees who are familiar with DFAS' mission and possess a mix of supervisory and technical skills would help maintain customer service during the transition period.

This criterion, however, did not play a large part in DOD's site-selection decisions. An example relates to the Defense Commissary Agency's vendor pay functions. Currently, DFAS has two locations that perform this function: one in Hopewell, Virginia, where the Commissary Agency's headquarters is located, and the other in San Antonio, Texas. In fiscal year 1994, these two offices processed 2.8 million invoices totaling $4.8 billion. According to information provided to us by DFAS officials, there are two locations where a consolidation would appear to be reasonable: (1) Hopewell, Virginia, because it already performs vendor pay functions, is colocated with the Commissary Agency's headquarters, and is the home of the vendor pay computer system and (2) the DFAS center in Columbus, Ohio, because it already has people trained in vendor pay functions and does accounting and disbursing for the Commissary Agency. DFAS Columbus, prior to the site-selection process, was planning to bring Commissary Agency vendor pay functions into its center.

Under the 20-site option, the plan is to consolidate this function in Pensacola, Florida. Because fewer than 20 percent of the people are expected to transfer to Pensacola, new staff will have to be hired and trained. If not properly managed, such consolidations can result in significant problems. In 1991, for example, the Commissary Agency went through a consolidation that was not well-managed. It resulted in late vendor payments, prompt pay penalties,[10] and companies going out of business because they could not get paid.

The same potential for customer service problems exists with nonappropriated fund accounting. DFAS has already consolidated most of the Army's nonappropriated fund accounting at the Red River Army Depot in Texas, but the Air Force and Navy are still doing their accounting in decentralized field offices around the world. As part of the consolidation initiative, DFAS plans to consolidate all of nonappropriated fund accounting at one location. The location for nonappropriated fund accounting (Chanute Air Force Base in Rantoul, Illinois) was not determined until after the site-selection process was completed. According to DFAS officials, it will be difficult to transfer the Army's consolidated operation to Chanute while DFAS is trying to bring Air Force and Navy operations on line. Few people are expected to transfer from Red River Depot to the Chanute location. Because DFAS has no employees in the Chanute area, almost an entirely new workforce will have to be hired and trained.

[10]The Prompt Payment Act (31 U.S.C. 3901-3906) requires the federal government to pay interest on late payments to vendors.

DOD's Site-Selection Process Favored Excess DOD Facilities Over Other Factors

Once DOD decided to consolidate finance and accounting functions at the 5 existing centers and 20 operating locations, it then had to decide where to locate these activities. Since the Opportunity for Economic Growth program was canceled, it was clear that the location of the five large centers would not change. There were many options, however, for selecting the sites for operating locations. During the evaluation and scoring process, for example, DOD used 4 criteria to evaluate sites in 132 communities: (1) cost to the government, (2) maintenance of customer service, (3) availability of a good labor supply, and (4) use of excess defense assets. It assigned each of the selection criteria a value of between 0 and 100 points. We have two basic concerns with the site-selection and scoring process.

First, before DOD conducted the scoring and evaluation process, it did not determine the relative importance of and assign corresponding weights to each criteria—each was initially given equal weight. Once the initial scoring process was completed, DOD arrayed the data using nine different weighting schemes, sometimes, for example, giving more weight to cost and at other times giving cost a relatively low priority. This scheme resulted in 10 different priority listings. Finally, DOD arrayed all 10 lists and counted the number of times each site showed up in the top 20. This became the 11th list. All 11 lists were then given to the Deputy Secretary of Defense as potential selection options. He selected list number 11.

We question the soundness of this process. Determining the relative importance of the four criteria during the selection process rather than before the process begins may not lead to sound decision-making. DOD recently stated this position during base closure and realignment hearings. Specifically, DOD said that predetermining the rules, including weighting factors, was absolutely necessary in order to be as objective and fair as possible.[11]

Second, the process, in effect, guaranteed that base closure and realignment sites or other excess DOD facilities would be selected, even if they were more costly to modify and operate and were ranked lower from a customer service and labor supply standpoint. Scores for three of the criteria, for example, provided a relative ranking of the communities using a wide spectrum of points: customer service scores ranged from 15 points to 100 points; quality labor force scores ranged from 58.5 points to 100 points; and cost-to-the-government scores ranged from 0 to 100 points.

[11]Statement by the Assistant Secretary of Defense (Economic Security), before the Base Closure and Realignment Commission (Mar. 1, 1995).

However, for the use of excess defense assets, there were only two possible scores. Excess defense sites received the full 100 points while nondefense sites received 0 points. Using this scoring method, 15 of 16 communities with excess DOD assets were selected as operating locations. The 16th community ranked 21st.

We conducted a sensitivity analysis to determine how locations would have fared if no credit or points had been given for the availability of excess DOD assets. Our analysis assigned equal weights to cost, customer service, and availability of a good labor force. It also assumed that DOD had adequately considered the economic merits of using excess DOD facilities during its evaluation of costs. This analysis showed that the rankings of the sites changed significantly when no points were given for excess DOD assets. Only three of the base closure and realignment sites would have been ranked among the top 20 sites.

A factor that affected the relative ranking of the base closure sites was the cost to renovate and make them useful for finance and accounting operations. During the cost analysis of potential sites, $115 million was the estimated cost to renovate the 15 excess DOD facilities. DFAS now estimates it will need $173 million in military construction money during fiscal years 1997, 1998, and 1999 to complete renovations at these sites. Appendix II describes the results of DOD's architectural and engineering assessment. It shows that 8 of the 15 facilities were considered good, 5 were characterized fair, 1 was rated poor, and 1 was sold by DOD before it could be activated. A variety of problems need to be corrected at the facilities rated fair or poor.

The Oakland Naval Supply Center, for example, will need $18 million to improve seismic characteristics, remove asbestos, and expand parking at the facility. This is $136 per square foot, which is less than new construction cost but more than the estimated cost to lease administrative space in the Oakland area. The facility at Fort Ord, a hospital building built in 1972, needs about $20 million for extensive interior renovations to provide suitable office space. It also needs a major modification to its heating and cooling system. At Chanute Air Force Base in Rantoul, Illinois, the original building selected by DFAS would have cost about $26 million to renovate, but it was subsequently sold by DOD to a private developer. DFAS expects that an alternative site on base, which it has not yet finished evaluating, will cost about $18 million to renovate.

Funding for these renovations will require the use of military construction appropriations. If approved, these funds will not be available until at least fiscal year 1996, and renovations will probably not begin until 1997 or later after design specifications are finalized and contracts are awarded. In the interim, the use and capacity of some facilities will be limited. For example, according to DFAS officials, the Fort Ord facility, an 8-story hospital building, cannot house more than about 200 DFAS employees until extensive renovations are complete.

Yet, DOD is moving ahead with its consolidation plans. On November 14, 1994, DOD announced that 43 defense accounting offices would close and 13 of the new operating locations would begin limited operations by the end of fiscal year 1995. On March 7, 1995, DOD announced plans to close another 32 defense accounting offices during the first half of fiscal year 1996. This is happening even though DFAS has not yet received congressional funding to renovate the sites and does not know what functions it will place at some of the facilities, and, therefore, what types of personnel it needs to recruit and hire.

DFAS Consolidation Precedes Most Reengineering Efforts

Business process reengineering is a quality improvement concept DOD introduced about 4 years ago as part of its Corporate Information Management initiative. Reengineering allows organizations to develop a baseline and critically evaluate their current business processes, eliminate unnecessary tasks, and, in some cases, reinvent the way they do business. It has been used successfully by many businesses over the past several years as they have attempted to downsize and become more competitive. More recently, the Secretary of Defense asked each defense organization to apply reengineering techniques to its high payoff processes and develop truly innovative approaches for reducing business-process cycle times. The ultimate goal is a 50-percent reduction by the year 2000.

DFAS has recognized the importance of reengineering in streamlining its operations and reducing the size of its finance and accounting workforce. Its consolidation planning documents, for example, refer to 30- to 50-percent productivity gains that might be possible through reengineering. For some processes that operate at its large finance centers, DFAS has implemented reengineering initiatives. For example, both its transportation payment process and its retiree and annuitant payment process have been consolidated and streamlined to gain efficiencies and improve customer service. In addition, DFAS is considering several additional center processes for reengineering. These include the contract payment process at the Columbus center and the garnishment process at the Cleveland center.

On the other hand, DFAS has not yet applied reengineering techniques to the finance and accounting processes it plans to place at the 20 operating locations. DFAS officials stated that reengineering its processes at the same time it was consolidating its operations would be difficult to manage and cause unnecessary risk to its operations. Instead, it plans to use existing systems and processes to perform many of the same basic functions at the new operating locations as it did at the smaller defense accounting offices: vendor pay, travel processing, general funds accounting, and Defense Business Operations Fund accounting. Once these functions are reengineered, it is likely that fewer personnel with different skills may be needed to carry out the new business processes.

For example, DOD reported that it spent $3.5 billion on temporary duty travel in fiscal year 1993. It also estimated that its processing costs may be at least 30 percent of the direct travel cost—well above the 10-percent average reported for private companies and the 6-percent rate that industry considers an efficient operation. In a recent report,[12] we estimated that DOD could save hundreds of millions of dollars in travel processing costs by following private industry best practices. Although DOD has chartered a task force to reengineer travel management and consider private industry best practices, it has not considered any of these practices in its consolidation plans. One best practice, for example, involves consolidating travel voucher processing at a single location. Under the DFAS consolidation, voucher processing will be done at almost all of the 20 new operating locations. Consequently, if DOD's travel task force concludes that one voucher processing site (or a small number of processing sites) is sufficient, DFAS will once again have to consolidate a portion of its financial operations.

Another example involves DOD's civilian pay functions. Currently, DFAS employees are responsible for paying DOD civilians handle about 684 pay accounts each. Under the consolidation initiative, DFAS intends to reduce the number of pay systems from 25 to 2 and reduce the number of locations responsible for processing civilian pay to 4. Once the system standardization and consolidation are finished, DFAS officials told us that each employee should be able to handle 1,600 pay accounts. Although this would be a substantial productivity gain, private sector companies that

[12]Travel Process Reengineering: DOD Faces Challenges in Using Industry Practices to Reduce Costs (GAO/AIMD/NSIAD-95-90, Mar. 2, 1995).

have aggressively reengineered their employee pay functions average about 3,000 pay accounts per person. If DFAS could achieve this level of productivity, it would need 470 fewer people than what it expects under its planned consolidated pay operation. This would save DFAS another $16 million in annual operating costs and might reduce the number of locations needed for civilian payroll operations.

Recommendations

As DOD proceeds with the consolidation and reengineering of finance and accounting functions and locations, we recommend that the Secretary of Defense direct the DOD Comptroller to

- develop an updated estimate of the number of locations and personnel required to perform finance and accounting functions. In developing this estimate, it is important that the Comptroller consider not only today's concept-of-operations but also how finance and accounting operations will be performed once DFAS has complied with DOD's business process reengineering goals and directives.
- use the updated information to reassess the site selection decisions for new operating locations. This reassessment should balance DOD's desire for short-term cost savings with the need to select sites that, from a business perspective, offer the greatest opportunity for maintaining or enhancing finance and accounting operations and service to DFAS' customers.

Matters for Congressional Consideration

Before approving military construction funds for renovating excess facilities for finance and accounting operations, the Congress may want to ensure that DOD has adequately assessed and justified the size and locations of its finance and accounting network.

Agency Comments and Our Evaluation

Following DOD's initial review of a draft of this report, we met with representatives of the Comptroller's Office and DFAS to discuss their preliminary comments. Although they generally agreed with the facts and contents of the report, they did not believe we had given DFAS adequate credit for some of the reengineering initiatives it had implemented at the large finance centers. They also did not believe we had adequately recognized that DFAS expects the consolidation will save between $8 billion and $9 billion over the next 20 years. We added information to the report in both these areas.

The major point raised by the DOD representatives, however, concerned our draft recommendation to stop the consolidation until the number of operating locations and sites was reevaluated. Although they agreed with the recommendation in principle, they said that stopping the consolidation at this point in time could be detrimental to current finance and accounting operations. They pointed out that several defense accounting offices had already been closed and 13 new operating locations opened or partially opened to pick up the workload. Stopping the buildup of these sites, in their view, could jeopardize DFAS' ability to support its military customers.

After considering DOD's position, we modified our recommendation to request that DOD reevaluate its consolidation and site-selection decisions concurrently with its ongoing consolidation efforts. Based on this change, DOD now concurs with the recommendations and has committed to reevaluate the number of locations and personnel required to perform finance and accounting functions by November 30 of 1995 and each year thereafter. Likewise, beginning on December 15, 1995, it has agreed to annually reassess its site-selection decisions and report its findings to the Secretary of Defense. (See app. III.)

We performed our review from August 1994 through July 1995 in accordance with generally accepted government auditing standards. (See app. I for details on our objectives, scope, and methodology.)

We are sending copies of this report to the Chairmen, Senate Committee on Governmental Affairs, Senate Committee on Armed Services, House Committee on Government Reform and Oversight, and Senate and House Committees on Appropriations; the Director, Office of Management and Budget; the Secretary of Defense; and other interested parties. We will make copies available to others on request.

If you have any questions on this report, please call me on (202) 512-8412. Major contributors to this report are listed in appendix IV.

David R. Warren
Director, Defense Management
and NASA Issues

Contents

Abbreviations

DFAS	Defense Finance and Accounting Service
DOD	Department of Defense

Objectives, Scope, and Methodology

The Subcommittee on Military Readiness, House Committee on National Security, asked us to address the following questions about the Department of Defense's (DOD) plan to consolidate its finance and accounting operations:

- Does the plan reflect leading-edge business practices that are likely to lead to substantial cost-reductions and high quality customer service?
- How will the planned structure achieve productivity gains that will enable DFAS to reduce its workforce from 46,000 to 23,000 people?
- Is the plan's implementation strategy sound and achievable within stated time frames?
- When will the military services begin to realize reductions in the prices they are charged for the Defense Finance and Accounting Service (DFAS)?

During this phase of our audit work, we focused on the consolidation implementation strategy and the use of leading-edge business practices to reduce costs and improve customer service. To determine the soundness of the implementation strategy, we reviewed DOD's site-selection process, which determined the infrastructure for finance and accounting operations and formed the basis for developing a consolidation implementation strategy.

To assess how DFAS determined the number of sites needed, we reviewed guidance and criteria prescribed by the Secretary of Defense, statements made by DOD officials to congressional oversight committees, documentation describing the Opportunity for Economic Growth, documentation of meetings held by DFAS' Senior Review Council, and efforts made by the Consolidation Task Force to determine how private sector organizations addressed the issue of organizational size. We also reviewed implementation plans to identify the functions and workloads that are planned for the various operating locations. During our review, we interviewed DOD officials, particularly Task Force members, about the costs and personnel requirements of organizational structures with 6, 10, 15, and 20 operating locations.

To determine how candidate sites were evaluated and selected, we reviewed DFAS' site-selection process plan to determine if it incorporated the Secretary of Defense's guidance, defined the selection criteria, specified the analytical processes and products, assigned weights to the selection criteria, and identified the responsibilities of the DFAS Director, the Senior Review Council, and the Consolidation Task Force. We reviewed the facts and assumptions used to analyze the candidate sites, the scoring process for each criterion, and the rankings and costs for organizational structures that included 6, 10, 15, and 20 operating locations. We also conducted a sensitivity analysis to determine the impact of one of the selection criteria—reuse of excess DOD assets—on the rankings of the 750-person candidate sites. Our analysis excluded this criterion and gave equal weight to the criteria of cost, customer service, and quality labor force. We then compared this ranking with DOD's rankings using all of the criteria. During our review, we met frequently with DOD officials, particularly Task Force members, about various aspects of the selection process.

To determine how excess DOD facilities were assessed, we reviewed DFAS' site-selection process plan to identify criteria used to qualify candidate facilities for consideration. We analyzed the results of an engineering and architectural company's assessments of DOD's excess facilities and cost estimates to renovate each facility. We compared DFAS' military construction estimates for renovating these facilities to the engineering and architectural company's estimates. We used this information to identify problems with the facilities and compare the estimated renovation costs of each facility. Using DFAS' planned square footage for renovation and planned staffing level of 750 people per site, we calculated the renovation costs on the basis of both cost per square foot and cost per person.

To determine how customer service would be affected by site-selection and activation decisions, we reviewed DFAS plans to determine how they addressed the Secretary of Defense's concerns about maintaining customer service and complied with the site-selection criterion that emphasized maintaining customer service. Accordingly, we analyzed DFAS' plans to maintain customer service when field offices are closed and their workloads and functions are transferred to operating locations. To the extent it was available, we analyzed data identifying where finance and accounting functions are currently operating and where they will be consolidated. We also analyzed documentation identifying the number of DFAS employees expected to transfer to operating locations, the number of current employees already located in metropolitan areas where operating locations will be established, and the number of employees expected to be hired. We also discussed with DFAS officials training requirements for employees who could be assigned to operating locations during fiscal year 1995. We obtained information about training classes for employees who are expected to be transferred or hired.

We performed our work at the Headquarters, Office of the Secretary of Defense (Comptroller); Headquarters, Defense Finance and Accounting Service; and DFAS finance centers located in Cleveland, Ohio; Columbus, Ohio; Denver, Colorado; Indianapolis, Indiana; and Kansas City, Missouri. We also contacted officials assigned to the District Office, Army Corps of Engineers, Louisville, Kentucky. We performed our review from August 1994 through March 1995 in accordance with generally accepted government auditing standards. We discussed our report with cognizant DOD officials and incorporated their views where appropriate.

Process DOD Used to Assess Excess Facilities

To consider the reuse of excess DOD facilities, the Consolidation Task Force first coordinated with the military services to identify available facilities. It then screened the facilities to identify those that would be available and would provide at least 125,000 square feet, the minimum amount of space needed to house 750 employees. Next, each facility was evaluated to determine its reuse potential. In total, 48 facilities were evaluated.

An architectural and engineering company, under contract with the Army Corps of Engineers, conducted the facility evaluations. The company was required to evaluate each facility for its suitability for finance and accounting operations and develop cost estimates for necessary renovations. Facility suitability was rated on numerous factors, including the amount of usable contiguous space available, the level of risk associated with redesign and construction, access to utilities, the availability of infrastructure support requirements, proximity to an airport, existence of environmental problems, and physical security of the facility. The contractor rated the suitability of each facility as good, fair, or poor and provided a relative ranking of all facilities.

Table II.1 summarizes the results of the architectural and engineering assessments and provides DFAS' updated renovation cost estimates for each facility.

Table II.1: Planned DFAS Operating Location Facilities

Dollars in millions

Operating location		Engineering assessment summary data			
Location	Bldg. no.	Area (sq. ft.)	Rehab cost	Suitability	Rank
Charleston Naval Supply Yard (Charleston, SC)	198	228,035	$ 2.7	Fair	7
Gentile Air Force Station (Dayton, OH)	45/46	447,632	14.6	Good	11
Ft. Sill (Lawton, OK)	4700	197,252	8.0	Good	21
Lexington-Blue Grass Army Depot (Lexington, KY)	4	138,360	2.7	Fair	9
Loring Air Force Base (Limestone, ME)	3502	142,400	4.4	Good	12
Memphis Naval Air Station (Memphis, TN)	787	128,000	2.8	Good	4
Newark Air Force Base (Newark, OH)	4	747,077	15.2	Poor	28
Oakland Naval Supply Center (Oakland, CA)	311	131,878	8.4	Fair	26
Offutt Air Force Base (Omaha, NE)	500	130,000	3.6	Good	5
Orlando Naval Training Center (Orlando, FL)	301	156,960	0.4	Good	1
Chanute Air Force Base (Rantoul, IL)	3	n/a	n/a	n/a	n/a
Rock Island Arsenal (Rock Island, IL)	62	155,409	7.4	Good	10
Griffis Air Force Base (Rome, NY)	1	195,332	8.6	Good	22

DFAS estimated renovation costs					
Date available	Remarks	Area (sq. ft.)	Rehab cost[a]	Cost per sq. ft.[b]	Cost per person[c]
N/A	Moderate demolition needed to create large floor areas suitable for offices. Contains some asbestos and has lead paint.	125,280	$5.9	$47	$ 7,900
Sept. 1996	Built in 1954/1956. Recently renovated. Probably has asbestos.	202,000	11.4	56	15,200
June 1994	Built in 1966 as a hospital. Extensive interior demolition. Some asbestos.	197,252	12.8	65	17,100
Jan. 1994	Built in 1943. Warehouse easily convertible to open office space. Has asbestos. Inadequate parking.	138,360	7.3	53	9,700
Sept. 1994	Hospital built in 1988. Costly demolition of hospital systems.	142,400	9.2	65	12,300
Jan. 1997	Newer facility. Easily modified to open office. Modern.	128,000	6.6	52	8,800
Sept. 1996	DFAS areas not contiguous. Poor internal configuration for offices. Built in 1954, extremely high roof, no windows, has asbestos. DFAS will have to treat potable water onsite.	166,566	8.2	49	10,900
Sept. 1995	Built in 1942. New entrance tower needed. Moderate interior demolition needed for office space. Parking lot needs major expansion. Seismic upgrade required. Asbestos present.	131,878	18.0	136	24,000
Dec. 1994	Built in 1955. Space on 3rd floor for DFAS. 5,000 sq. ft. also designated for storage.	125,000	7.4	59	9,900
Jan. 1994	New 3-story electronics training school, never occupied. If assumed parking expansion not possible, suitability then becomes fair.	156,960	4.2	27	5,600
n/a	Original assessment was completed on building 3. Subsequently, the building was sold to a private developer. Building 68 was chosen as an alternate site. DFAS' estimate is for building 68.	146,423	18.0	123	24,000
Oct. 1994	Now partially occupied. Built in 1878. Historic landmark. Has asbestos.	155,409	13.8	89	18,400
Dec. 1994	Built in 1942 as a warehouse. Partly converted to office space. Has some identified asbestos.	183,332	12.6	69	16,800

(continued)

Dollars in millions

Operating location		Engineering assessment summary data			
Location	Bldg. no.	Area (sq. ft.)	Rehab cost	Suitability	Rank
Norton Air Force Base (San Bernardino, CA)	951, 952, 953	189,168	10.3	Fair	25
Ft. Ord (Seaside, CA)	4385	360,060	19.4	Fair	24
Total		3.5(mil)	114.9		

DFAS estimated renovation costs

Date available	Remarks	Area (sq. ft.)	Rehab cost[a]	Cost per sq. ft.[b]	Cost per person[c]
Sept. 1996	Two-story office built in 1963. Probably contains asbestos. Needs seismic upgrade. Separated from main base, not part of closure.	189,168	17.5	93	23,300
July 1994	Built in 1972 as a hospital. Needs extensive interior demolition to create suitable office space. HVAC distribution will be difficult.	145,536	20.0	137	26,700
		2.3 (mil)	173.0		

Source: Defense Finance and Accounting Service (DFAS) military construction funding request and Corps of Engineers architectural and engineering assessments.

[a] Renovation cost estimate was taken from DFAS' request for military construction funding for fiscal years 1997-99. DFAS' estimate includes cost for building renovation and installation of wiring for telecommunication and ADP equipment.

[b] Cost per square foot was calculated using the following formula: cost to rehab/square footage.

[c] Cost per person was calculated using the following formula: cost to rehab/750 (planned staffing level at the operating locations)

Comments From the Department of Defense

UNDER SECRETARY OF DEFENSE
1100 DEFENSE PENTAGON
WASHINGTON, DC 20301-1100

COMPTROLLER

JUL 28 1995

Mr. Henry L. Hinton, Jr.
Assistant Comptroller General
U.S. General Accounting Office
Washington, D.C. 20548

Dear Mr. Hinton:

I have enclosed the Department of Defense (DoD) response to the General Accounting Office draft report, "DOD INFRASTRUCTURE: DOD's Planned Finance and Accounting Structure Is Not Well Justified," dated June 1995 (GAO Code 709088/OSD Case 9921). Based on the DoD review of the draft, we felt that the report did not adequately reflect the positive initiatives that are being accomplished. We note that you added additional information and recognition of the complex issues involved after discussions with GAO representatives. The Department, therefore, generally concurs with the revised draft report.

I appreciate that GAO recognized the significant reengineering initiatives underway throughout the Defense Finance and Accounting Service. As the Department proceeds with systems standardization and operational consolidation, additional reengineering efforts will take place.

The Department's detailed comments on the draft report recommendations are enclosed. The DoD appreciates the opportunity to comment on the draft report.

Sincerely,

John J. Hamre

Enclosure

GAO DRAFT REPORT OF JUNE 1995
(GAO CODE 709088) OSD CASE 9921

"DOD INFRASTRUCTURE: DOD'S PLANNED FINANCE AND ACCOUNTING STRUCTURE IS NOT WELL JUSTIFIED"

DEPARTMENT OF DEFENSE COMMENTS

RECOMMENDATION 1: As DoD proceeds with the consolidation and reengineering of finance and accounting functions and locations, we recommend that the Secretary of Defense direct the DoD Comptroller to develop an updated estimate of the number of locations and personnel required to perform finance and accounting functions. In developing this estimate, it is important that the Comptroller consider not only today's concept-of-operations but also how finance and accounting operations will be performed once DFAS has complied with DoD's business process reengineering goals and directives.

DoD RESPONSE: Concur. The Under Secretary of Defense (Comptroller) will develop an updated estimate of the number of locations and personnel required to perform finance and accounting functions. This estimate will be developed annually by November 30 until consolidation is completed.

RECOMMENDATION 2: As DoD proceeds with the consolidation and reengineering of finance and accounting functions and locations, we recommend that the Secretary of Defense direct the DoD Comptroller to use the updated information to reassess the site selection decisions for new operating locations. This reassessment should balance DoD's desire for short-term cost savings with the need to select sites that, from a business perspective, offer the greatest opportunity for maintaining or enhancing finance and accounting operations and services to DFAS' customers.

DoD RESPONSE: Concur. The Under Secretary of Defense (Comptroller) will use the updated information to reassess the site selection decisions for new operating locations and report annually to the Secretary of Defense by December 15.

MATTER FOR CONGRESSIONAL CONSIDERATION: Before approving military construction funds for renovating excess facilities for finance and accounting operations, the Congress may want to ensure that DOD has adequately assessed and justified the size and locations of its finance and accounting network.

DoD RESPONSE: Partially concur. As indicated in the DoD responses to the GAO recommendations, the Department will develop an updated estimate of the number of locations and personnel required and will reassess the site selection decisions for new operating locations by providing an annual report to the Secretary of Defense. This information would be available to the Congress in connection with any military construction requirements arising out of such updates and reassessments.

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Related GAO Products

Defense Infrastructure: Enhancing Performance Through Better Business Practices (GAO/T-NSIAD/AIMD-95-126, Mar. 23, 1995).

DOD Procurement: Overpayments and Underpayments at Selected Contractors Show Major Problem (GAO/NSIAD-94-245, Aug. 5, 1994).

Defense Business Operations Fund: Improved Pricing Practices and Financial Reports Are Needed to Set Accurate Prices (GAO/AIMD-94-132, June 22, 1994).

Financial Management: DOD's Efforts to Improve Operations of the Defense Business Operations Fund (GAO/T-AIMD/NSIAD-94-146, Mar. 24, 1994).

DOD Procurement: Millions in Overpayments Returned by DOD Contractors (GAO/NSIAD-94-106, Mar. 14, 1994).

Financial Management: Status of the Defense Business Operations Fund (GAO/AIMD-94-80, Mar. 9, 1994).

Financial Management: Strong Leadership Needed to Improve Army's Financial Accountability (GAO/AIMD-94-12, Dec. 22, 1993).

Letter to the Deputy Secretary of Defense (GAO/AIMD-94-7R, Oct. 12, 1993).

Financial Management: Opportunities to Strengthen Management of the Defense Business Operations Fund (GAO/T-AFMD-93-6, June 16, 1993).

Financial Management: Navy Records Contain Billions of Dollars in Unmatched Disbursements (GAO/AFMD-93-21, June 9, 1993).

Military Bases: Analysis of DOD's Recommendations and Selection Process for Closures and Realignments (GAO/NSIAD-93-173, Apr. 15, 1993).

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