

TRANSFORMATION *Challenges*



**The Honorable
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Comptroller General
of the United States

Defense Business
Transformation Forum
Wye River
Conference Center
Queenstown, MD
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GAO's Strategic Plan

SERVING THE CONGRESS AND THE NATION GAO'S STRATEGIC PLAN FRAMEWORK



MISSION

GAO exists to support the Congress in meeting its constitutional responsibilities and to help improve the performance and ensure the accountability of the federal government for the benefit of the American people.

THEMES



Long-Term Fiscal Imbalance

National Security

Global Interdependence

Changing Economy

Demographics

Science and Technology

Quality of Life

Governance

GOALS & OBJECTIVES



Provide Timely, Quality Service to the Congress and the Federal Government to ...

Address Current and Emerging Challenges to the Well-Being and Financial Security of the American People *related to ...*

- Health care needs and financing
- Education and protection of children
- Work opportunities and worker protection
- Retirement income security
- Effective system of justice
- Viable communities
- Natural resources use and environmental protection
- Physical infrastructure

Respond to Changing Security Threats and the Challenges of Global Interdependence *involving ...*

- Emerging threats
- Military capabilities and readiness
- Advancement of U.S. interests
- Global market forces

Help Transform the Federal Government's Role and How It Does Business to Meet 21st Century Challenges *by assessing ...*

- Roles in achieving federal objectives
- Government transformation
- Key management challenges and program risks
- Fiscal position and financing of the government

Maximize the Value of GAO by Being a Model Federal Agency and a World-Class Professional Services Organization *in the areas of ...*

- Client and customer satisfaction
- Strategic leadership
- Institutional knowledge and experience
- Process improvement
- Employer of choice

CORE VALUES

Accountability

Integrity

Reliability

GAO's High-Risk List

2005

| High-Risk Areas | Designated High Risk |
|----------------------------------------------------------------------------------------------------|----------------------|
| Addressing Challenges in Broad-based Transformations | |
| Protecting the Federal Government's Information Systems and the Nation's Critical Infrastructures | 1997 |
| Strategic Human Capital Management ^a | 2001 |
| U.S. Postal Service Transformation Efforts and Long-Term Outlook ^a | 2001 |
| Managing Federal Real Property ^a | 2003 |
| Implementing and Transforming the Department of Homeland Security | 2003 |
| Establishing Appropriate and Effective Information-Sharing Mechanisms to Improve Homeland Security | 2005 |
| DOD Approach to Business Transformation ^a | 2005 |
| DOD Supply Chain Management (formerly Inventory Management) | 1990 |
| DOD Weapon Systems Acquisition | 1990 |
| DOD Business Systems Modernization | 1995 |
| DOD Financial Management | 1995 |
| DOD Support Infrastructure Management | 1997 |
| DOD Personnel Security Clearance Program | 2005 |
| Managing Federal Contracting More Effectively | |
| DOE Contract Management | 1990 |
| NASA Contract Management | 1990 |
| DOD Contract Management | 1992 |
| Management of Interagency Contracting | 2005 |
| Assessing the Efficiency and Effectiveness of Tax Law Administration | |
| Enforcement of Tax Laws ^{a, b} | 1990 |
| IRS Business Systems Modernization ^c | 1995 |
| Modernizing and Safeguarding Insurance and Benefit Programs | |
| Medicare Program ^a | 1990 |
| HUD Single-Family Mortgage Insurance and Rental Housing Assistance Programs | 1994 |
| Medicaid Program ^a | 2003 |
| Modernizing Federal Disability Programs ^a | 2003 |
| Pension Benefit Guaranty Corporation Single-Employer Insurance Program ^a | 2003 |
| Other | |
| FAA Air Traffic Control Modernization | 1995 |

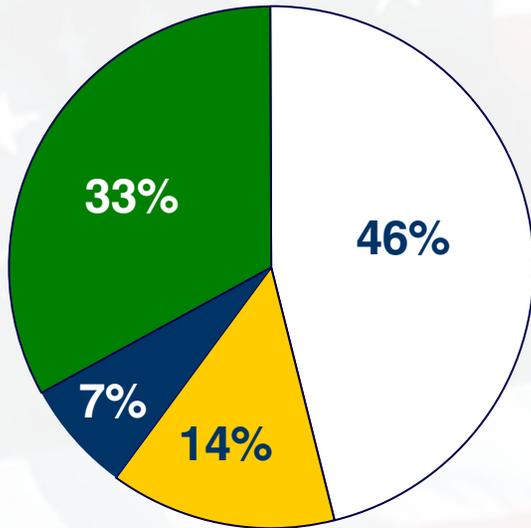
^a Legislation is likely to be necessary, as a supplement to actions by the executive branch, in order to effectively address this high-risk area.

^b Two high-risk areas—Collection of Unpaid Taxes and Earned Income Credit Noncompliance—have been consolidated to make this area.

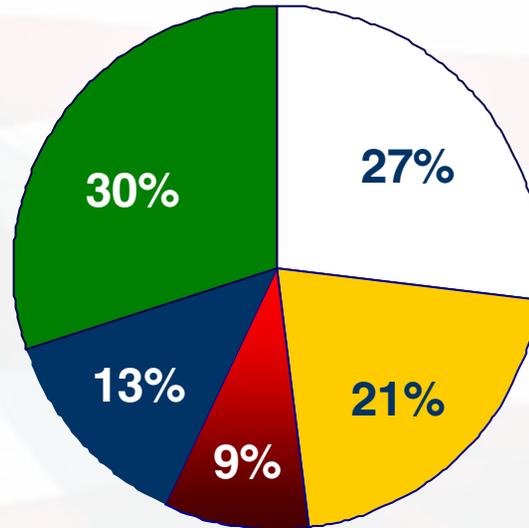
^c The IRS Financial Management high-risk area has been incorporated into this high-risk area.

Composition of Federal Spending

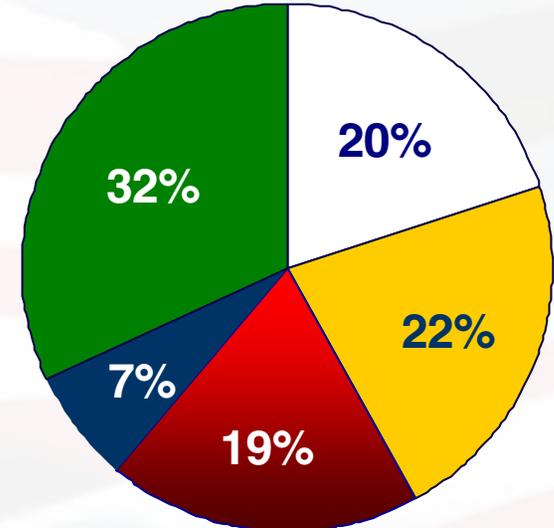
1964



1984



2004



Defense
Net interest

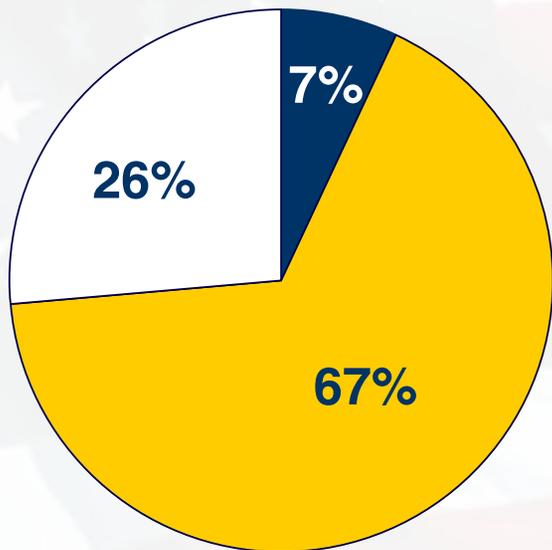
Social Security
All other spending

Medicare & Medicaid

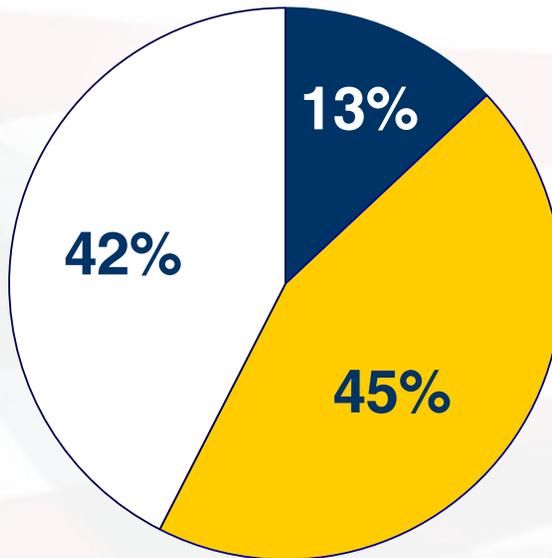
Source: Office of Management and Budget.

Federal Spending for Mandatory and Discretionary Programs

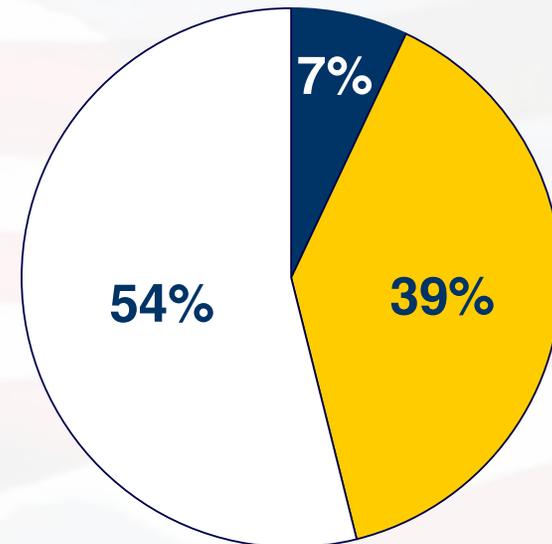
1964



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2004



Net Interest

Discretionary

Mandatory

Source: Office of Management and Budget.

Fiscal Year 2004 Deficit Numbers

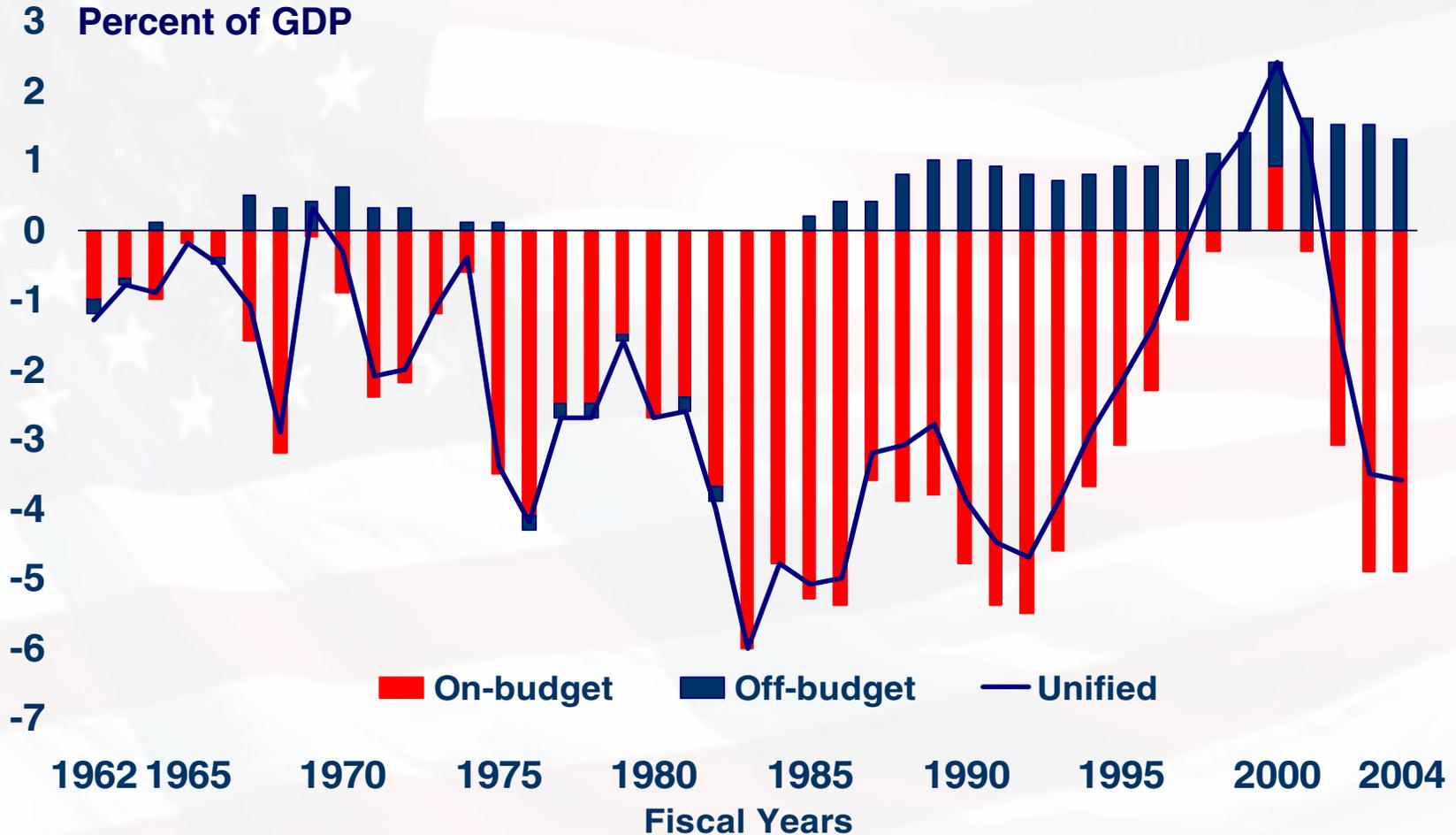
| | \$ Billion | % of GDP |
|--------------------|-------------------|-----------------|
| On-Budget Deficit | (567) | (4.9) |
| Off-Budget Surplus | 155* | 1.3 |
| Unified Deficit | (412) | (3.6) |

*Includes the \$151 billion Social Security surplus and a \$4 billion surplus for the Postal Service

March 2005

Surplus or Deficit as a Share of GDP

Fiscal Years 1962-2004



Source: Office of Management and Budget and Congressional Budget Office.

Selected Fiscal Exposures: Sources and Examples 2005^a

| Type | Example (dollars in billions) |
|-------------------------------------------------------------------------------------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Explicit liabilities | Publicly held debt (\$4,297) Military and civilian pension and post-retirement health (\$3,059) Veterans benefits payable (\$925) Environmental and disposal liabilities (\$249) Loan guarantees (\$43) |
| Explicit financial commitments | Undelivered orders (\$596) Long-term leases (\$39) |
| Financial contingencies | Unadjudicated claims (\$4) Pension Benefit Guaranty Corporation (\$96) Other national insurance programs (\$1) Government corporations e.g., Ginnie Mae |
| Exposures implied by current policies or the public's expectations about the role of government | Debt held by government accounts (\$3,071) ^b Future Social Security benefit payments (\$4,017) ^c Future Medicare Part A benefit payments (\$8,561) ^c Future Medicare Part B benefit payments (\$12,384) ^c Future Medicare Part D benefit payments (\$8,686) ^c Life cycle cost including deferred and future maintenance and operating costs (amount unknown) Government Sponsored Enterprises e.g., Fannie Mae and Freddie Mac |

^a All figures are for end of fiscal year 2004, except Social Security and Medicare estimates, which are as of January 1, 2005.

^b This amount includes \$845 billion held by military and civilian pension and post-retirement health funds that would offset the explicit liabilities reported by those funds.

^c Figures for Social Security and Medicare are net of debt held by the trust funds (\$1,687 billion for Social Security, \$268 billion for Medicare Part A, and \$19 billion for Medicare Part B) and represent net present value estimates over a 75-year period. Over an infinite horizon, the estimate for Social Security would be \$11.1 trillion, \$24.1 trillion for Medicare Part A, \$25.8 trillion for Medicare Part B, and \$18.2 trillion for Medicare Part D.

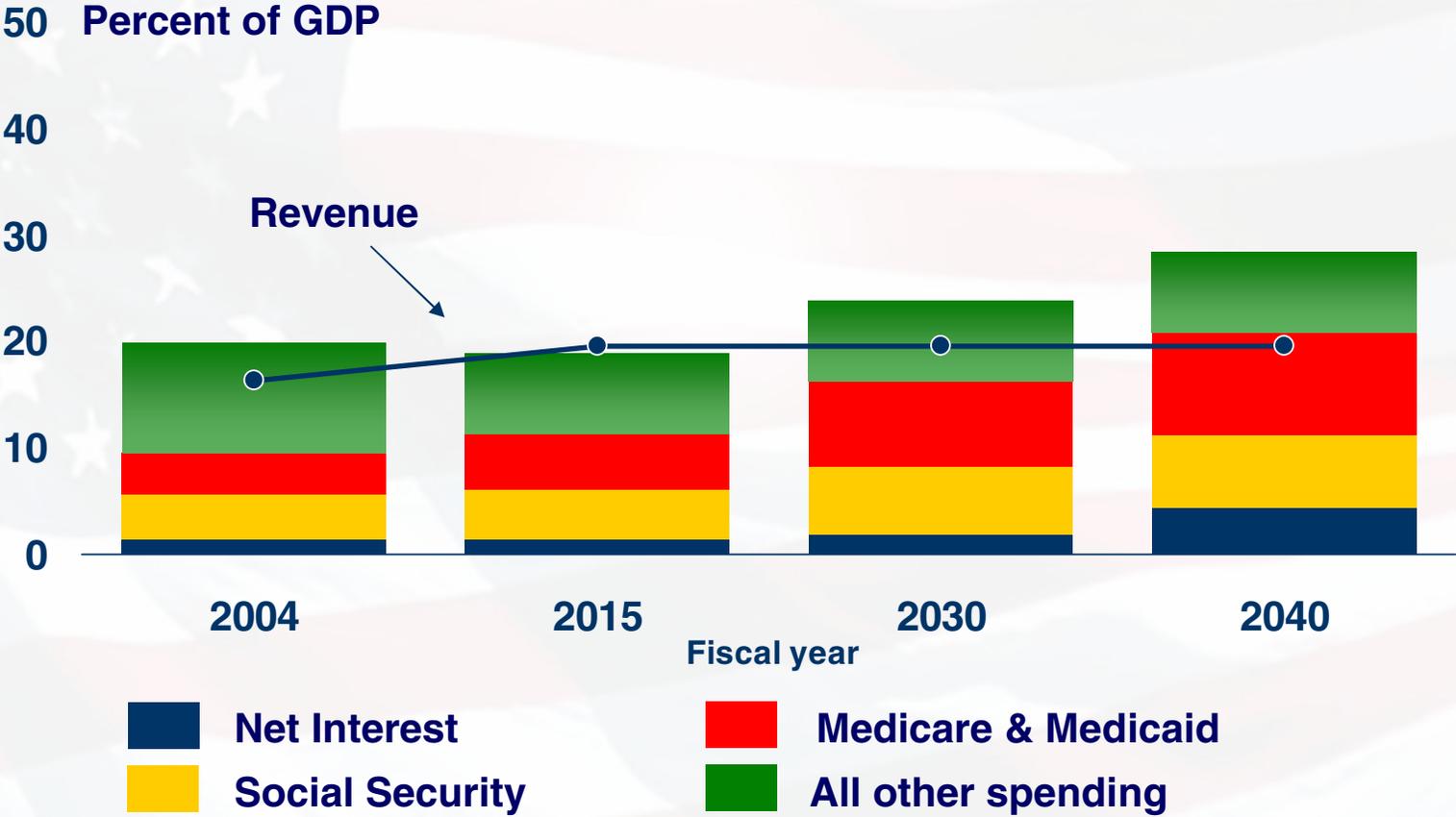
Source: GAO analysis of data from the Department of the Treasury, the Office of the Chief Actuary, Social Security Administration, and the Office of the Actuary, Centers for Medicare and Medicaid Services.

Another Way to Think About These Numbers

- Debt held by the public—\$4.3T
- Trust fund debt—\$3.1T
- Gross debt—\$7.4T
- Gross debt per person—about \$25,000
- If we add everything on the previous slide, the burden is more than \$150,000 per person or more than \$365,000 per full-time worker. Alternatively, it amounts to a total burden of more than \$45 trillion in current dollars, which is about 18 times the current annual federal budget or about 3.7 times the current annual GDP. This compares with an estimated \$48.5 trillion in total net worth, including home equity, for all Americans.

Note: The calculations are based on 75-year projections for Social Security and Medicare.

Composition of Spending as a Share of GDP Under Baseline Extended

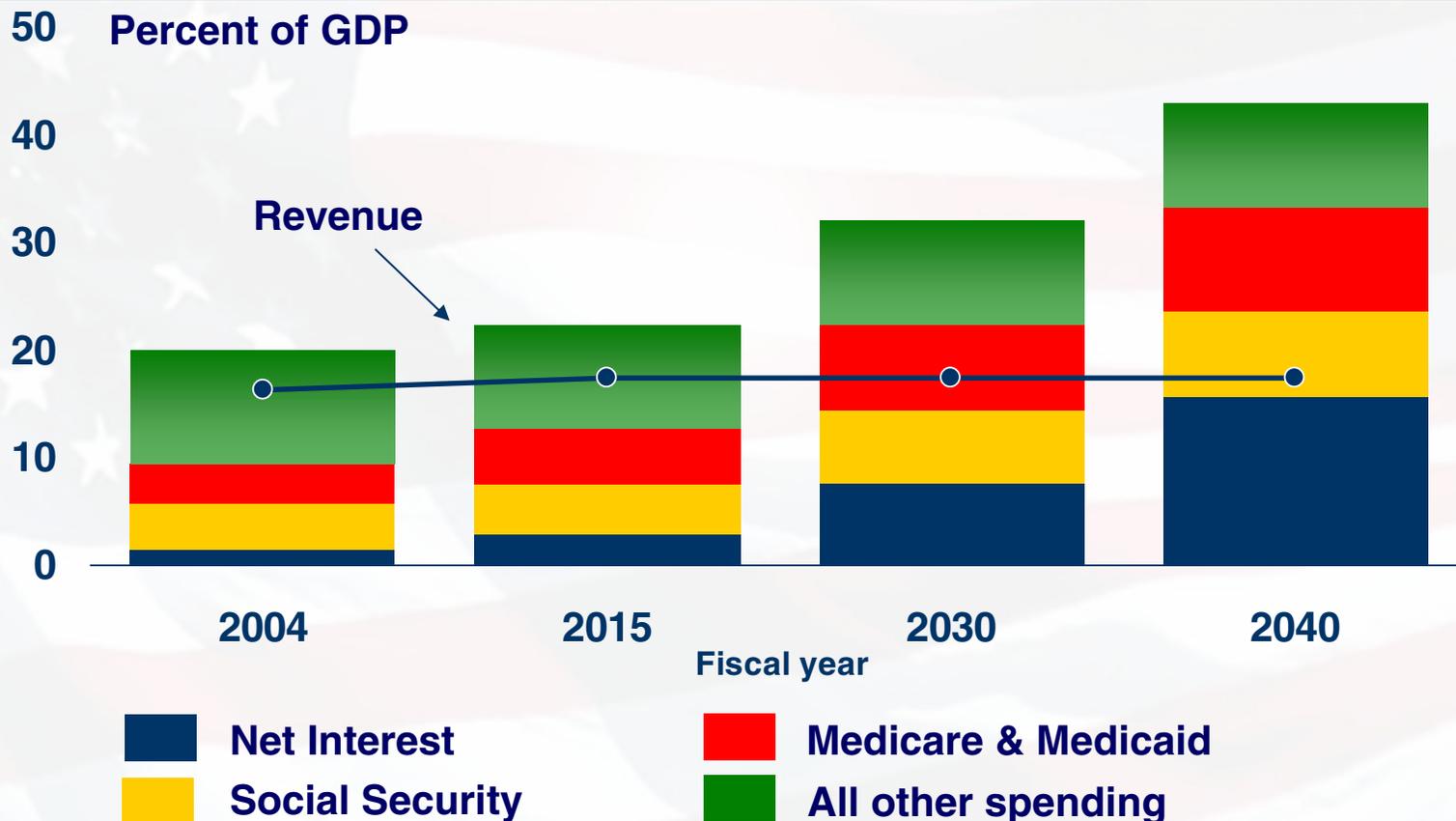


Notes: In addition to the expiration of tax cuts, revenue as a share of GDP increases through 2015 due to (1) real bracket creep, (2) more taxpayers becoming subject to the AMT, and (3) increased revenue from tax-deferred retirement accounts. After 2015, revenue as a share of GDP is held constant.

Source: GAO's March 2005 analysis.

Composition of Spending as a Share of GDP

Assuming Discretionary Spending Grows with GDP after 2005
and All Expiring Tax Provisions are Extended



Notes: Although expiring tax provisions are extended, revenue as a share of GDP increases through 2015 due to (1) real bracket creep, (2) more taxpayers becoming subject to the AMT, and (3) increased revenue from tax-deferred retirement accounts. After 2015, revenue as a share of GDP is held constant.

Source: GAO's March 2005 analysis.

Current Fiscal Policy Is Unsustainable

- **The “Status Quo” is Not an Option**
 - We face large and growing structural deficits largely due to known demographic trends and rising health care costs.
 - GAO’s simulations show that balancing the budget in 2040 could require actions as large as
 - Cutting total federal spending by about 60 percent or
 - Raising taxes to about 2.5 times today's level
- **Faster Economic Growth Can Help, but It Cannot Solve the Problem**
 - Closing the current long-term fiscal gap based on responsible assumptions would require real average annual economic growth in the double digit range every year for the next 75 years.
 - During the 1990s, the economy grew at an average 3.2 percent per year.
 - As a result, we cannot simply grow our way out of this problem. Tough choices will be required.
- **The Sooner We Get Started, the Better**
 - Less change would be needed, and there would be more time to make adjustments.
 - The miracle of compounding would work with us rather than against us.
 - Our demographic changes will serve to make reform more difficult over time.

The Way Forward

- Implement new accounting and reporting approaches and new budget control mechanisms for considering the impact of spending and tax policies and decisions over the long term
- Develop new metrics for measuring the impact of policies and decisions over the long term (e.g., key national indicators to measure our Nation's position and progress over time and in relation to other countries)
- Reexamine the base—question existing programs, policies and activities

Long-term Fiscal Challenges Demand New Metrics, Mechanisms, and Processes

- Accounting and reporting policies for trust funds, Social Security, Medicare, Veterans benefits, among other things, need to be reviewed and revised (e.g., possible fiscal burden statement with per capita and intergenerational figures).
- The current budget time horizon [2-year, 5-year, 10-year] does not capture many long-term costs—e.g., Social Security, Medicare, pension insurance—and other major tax and spending provisions
- Cash and obligations-based budgeting is misleading for insurance and some benefit programs
- Budget controls have expired—and we need to go beyond “holding the line” to “changing the base” in spending and tax policies

Improved Metrics, Measures and Processes: Some Ideas

- Provide information on long-term costs of major spending and tax proposals before they are voted on, including showing long-term costs even for proposals that sunset
- Establish an OMB annual report on fiscal exposures, including appropriate measures and how to address them
- Consider fiscal targets, triggers, sunset provisions and points of order with focus on limiting growth of long-term commitments
- Move to accrual budgeting for employee pension, retiree health; disclose “risk assumed” [missing premium] for insurance
- Reinstitute budget controls (caps & PAYGO)

We Need a Multifaceted Approach to Close the Long-Term Fiscal Gap

Policy:

- Restructure existing entitlement programs
- Reexamine the base of discretionary and other spending
- Review and revise our tax policy and enforcement programs

Operations:

- Reassess and revise how the government does business (e.g., management, planning and operational issues)
- Consider who should provide government services (e.g., sourcing strategy)

21st Century Challenges Report

- Report was issued February 16
- Based on GAO's work for the Congress
- Provides framework and questions to assist in reexamining the base
- Covers entitlements & other mandatory spending, discretionary spending, and tax policy and programs

Generic Reexamination Criteria and Sample Questions

Relevance of purpose and the federal role

Why did the federal government initiate this program and what was the government trying to accomplish?

Have there been significant changes in the country or the world that relate to the reason for initiating it?

Measuring success

Are there outcome-based measures? If not, why?

If there are outcome-based measures, how successful is it based on these measures?

Targeting benefits

Is it well targeted to those with the greatest needs and the least capacity to meet those needs?

Affordability and cost effectiveness

Is it using the most cost-effective or net beneficial approaches when compared to other tools and program designs?

Best practices

Is the responsible entity employing prevailing best practices to discharge its responsibilities and achieve its mission?

Twelve Reexamination Areas

MISSION AREAS

- Defense
- Education & Employment
- Financial Regulation & Housing
- Health Care
- Homeland Security
- International Affairs
- Natural Resources, Energy & Environment
- Retirement & Disability
- Science & Technology
- Transportation

CROSSCUTTING AREAS

- Improving Governance
- Reexamining the Tax System

Themes

- Changing Security Threats
- Increasing Global Interdependence
- Demographic Shifts—Aging Population
- Promoting Growth in a Knowledge-Based Economy
- Governance

Illustrative 21st Century Questions

National Defense

- **How should the historical allocation of resources across services and programs be changed to reflect the results of a forward-looking comprehensive threat/risk assessment as part of DOD's capabilities-based approach to determining defense needs?**
- **Given the growing encumbrance of pay and benefit costs, especially health care, within DOD's budget, how might DOD's recruitment, retention, and compensation strategies (including benefit programs) be reexamined and revised to ensure that DOD maintains a total military and civilian workforce with the mix of skills needed to execute the national security strategy while using resources in a more targeted, evidence-based, and cost-effective manner?**
- **Does DOD need to create a senior management position responsible and accountable for taking a strategic, integrated, and sustained approach to managing the day-to-day business operations of the department, including ongoing efforts to transform DOD's business operations and address the many related and longstanding high-risk areas? Should specific qualifications requirements and periods of tenure or terms be established for selected DOD positions related to key business operations?**

Trans **FORMATION**

Webster's definition

**An act, process, or instance of
change in structure appearance,
or character**

**A conversion, revolution,
makeover, alteration, or
renovation**

Transformation Has Different Dimensions

DOD

DHS

U. S. Postal Service

IRS

DOE

NASA

Human Capital Strategy

Financial Management

Information Technology

Sourcing Strategy

Disability Programs

Real Property Management

Note: All of the above are on GAO's High-Risk List to one extent or the other.

The Case for Change

- **Government is on a “burning platform,” and the status quo way of doing business is unacceptable for a variety of reasons, including:**
 - Past fiscal trends and significant long-range challenges
 - Rising public expectations for demonstrable results and enhanced responsiveness
 - Selected trends and challenges having no boundaries
 - Additional resource demands due to recent terrorism events in the United States
 - Government performance/accountability and high risk challenges, including the lack of effective human capital strategies

Transformation: A New Model for Government Organizations

Government organizations will need to:

- Become less hierarchical, process-oriented, stovepiped, and inwardly focused.
- Become more partnership-based, results-oriented, integrated, and externally focused.
- Achieve a better balance between results, customer, and employee focus.
- Work better with other governmental organizations, non-governmental organizations, and the private sector, both domestically and internationally, to achieve results.
- Focus on maximizing value, managing risk and enhancing responsiveness within current and expected resource levels.

Keys to Making Change Happen

- Commitment and sustained leadership (e.g., “leading by example” and “tone at the top”)
- Demonstrated need for change (i.e., burning platform)
- Start at the top and with the new people (transformation takes 7+ years)
- Process matters (e.g., employee involvement)—Don’t fight a two-front war
- 15-percent rule
- Identifiable and measurable progress over time
- Communication, communication, communication
- Figure out what’s right versus what’s popular
- Patience, persistence, perseverance to pain before you prevail

Key Transformation Elements

- People
- Process
- Partnerships
- Technology
- Environment

The most important of the five is **PEOPLE** — an agency's human capital.



Transformation is about
CREATING the future rather than
PERFECTING the past.
Effective **HUMAN CAPITAL**
strategy is key to any
SUCCESSFUL
transformation effort

Keys to Making Change Happen

Several other actions needed:

- Strategic Plan
- Core values
- Organizational alignment
- Recruiting, development, and succession planning strategies
- Modernizing and integrating institutional, unit and individualized performance measurement and reward systems
- Employee empowerment and effective communications

What Is DOD Transformation?

Creating the future of warfare and national defense while improving how the department, including all of its various component parts, does business in order to protect our national security and the nation's interests while maintaining our position as the world's preeminent military power within current and expected resource levels

Selected Cultural Challenges At DOD

- Past vs. future (e.g., threats)
- Today vs. tomorrow (e.g., budgets)
- Too many silos and layers
- Get the money and spend the money (e.g., use it or lose it)
- Plug-and-pray approach to weapons acquisitions
- Me vs. we (e.g., services)
- Approve vs. inform (e.g., deployments)

The Way Forward Selected Potential DOD Related Actions

- Revise the current approach to developing national military strategy (e.g., order, integration)
- Take a longer range approach to program planning and budget integration (e.g., life cycles, opportunity costs)
- Employ a total force management approach to planning and execution (e.g., military, civilian, contractors)
- Revise the process for developing and communicating key changes (e.g., DOD transformation, NSPS legislative proposal)
- Reduce the number of layers, silos and footprints
- Strengthen emphasis on horizontal and external activities (e.g., partnerships)
- Differentiate between war fighting and business systems development, implementation and maintenance (e.g., resource control, project approval)
- Make it okay to pull the plug or reduce quantities of weapon systems when the facts and circumstances warrant it

The Way Forward Selected Potential DOD Related Actions (cont.)

- Recognize the difference between approving and informing
- Create a Chief Management Officer to drive the business transformation process
- Get the design and implementation of the NSPS right, including modernizing and integrating the DOD, Service, domain, unit and individual performance measurement and reward systems
- Employ a more targeted and market based approach to compensation and other key human capital strategies
- Streamline yet strengthen current commercial contracts (e.g., incentives, transparency and accountability mechanisms)
- Provide for longer tours of duty in connection with key acquisitions and operations positions (e.g., responsibility and accountability)
- Focus on achieving real success in connection with financial management efforts (e.g., systems, controls, information, compliance and opinions)

Key Leadership Attributes For Success

- ***Courage***
- ***Integrity***
- ***Innovation***

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