2003 Munitions Summit

The Good, The Bad, and…. Cooperation

The Organic Base
Bill Holmes
Day & Zimmermann
First – The Bad

The Rand Study

Rand Recommendation: Privatize GOCO Ammo Plants

- Cancel current contracts
- Divest facilities
- Renegotiate production contracts
- Didn’t include GOGO supply depots
The Bad (cont.)

The Rand Study - Privatization

Well, OK – *But*….

- Environmental Remediation Cost and Timing
- Local, State and Federal Tax Implications
- Effect On Buying Power of Ammo Budget
Next – The Good

ASA (ALT) Charged AMC To Assess The Rand Study

• Develop implementation plan – maximum privatization practicable
• Tasked rolled downhill to CG, OSC/JMC
• MG McManus enlisted ICAP to help
Industry Input

• Must have reasonable opportunity/potential for Return on Investment
• Government responsible for pre-existing conditions (environmental is a major factor)
• There would be non-incumbent interest
• Cost of capital forecasted to be higher than other capital investments
• The more visibility the Government gives into the long-term plan, the better the price
• Without contractual requirements/funding – contractors will only maintain economic capacity/capability for peacetime buys
• Government indemnification/insurance against catastrophic loss must be evaluated on a case-by-case basis
• Enough unknowns – must proceed with caution
Options Developed

• Privatization – complete divestiture
  ➢ Installation Becomes COCO

• Public Private Partnership
  ➢ No Government Oversight
  ➢ Reduction/Elimination of Government Staff
  ➢ Commercial Investment
  ➢ Government Initially Owns the Land
  ➢ Environmental Bill Not Due Immediately
Business Case Analysis

• BCA Element Definitions

- Facility Sales Value - Estimated sales value for land & equipment, based on discounted cash flow from operations (e.g. ammunition sales, ARMS revenue)

- Facility Revenue – Average annual revenue the facility will receive after privatization (ammunition sales, ARMS revenue). Excludes PBS revenue after sale.

- Environmental Liability –
  - Installation Restoration Program (IRP) – Liabilities associated with the CERCLA (Superfund). These liabilities are now programmed, and remediation is on-going.
  - Resource Conservation and Recovery Act (RCRA) – On-going liabilities associated with compliance with RCRA permitted areas on a facility. The majority of these costs are not currently programmed, and may be accelerated when status of a facility changes

• BCA Result Definitions

- CUM NPV – Cumulative Net Present Value. Cash flow for each alternative is discounted over the 20 year economic life.

- NPV Savings – The difference between the CUM NPV for each alternative and the baseline.

- Ammo Unit Price Increase – The average unit increase in PAA hardware, 2005 to 2009.

- Total Impact Near Term Budget – The total impact to budget, 2003 to 2009, from all BCA elements studied.
Summary of Analysis

- Privatization or Public Private Partnership does not yield same economies of scale as current course of action.
- The most broad-reaching aspects of this analysis are the impacts on price of product and POM budgets:
  - Product price increases from 7 to 36 percent
  - $900M to $1.5B POM impact
- Execution of a POM time line may not be affordable.
View of Industrial Base Risks

Likelihood of Success
- Political Risk
- Soft landing for losers
- Legislative risks

Sustainable Readiness
- Market Risk:
  - Demand from DoD
  - Ability to support all services
  - Reserve Capacity

Technology Trends:
- Product obsolescence
- Process obsolescence
- Ability to adapt to new technology

Impact on Ammunition
- Operational performance/cost
  - Predictability
  - Staff costs/availability
  - Facility/plant obsolescence
  - Cost of product

Security of Supply
- Competitive/monopoly
- Overseas suppliers
- Peacetime vs. Reserve Capacity

Economics & Facility performance/costs
- Operating cost
- Obsolescence
- Recapitalization
- Alternative use/tenants
- Insurance costs/Indemnification
- Impacts to Near Term Budget

EVALUATING THE RISKS

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Finally - Cooperation

• Concerned Industry
  ➢ ICAP
  ➢ MIBTF

• Industry – Government
  ➢ ICAP Participation

• Internal Government
  ➢ PEO – OSC/JMC

I’m Encouraged...