

# AVIATION WEEK

## & SPACE TECHNOLOGY

### VIEWPOINT

BY JON B. KUTLER

Perhaps U.S. defense contractors should be cheering the high price of oil. While not directly relevant to their business models, the political and media obsession with oil company windfall profits has delayed attention from an inevitable shift to the record profits of defense contractors during a period of unprecedented cost overruns on major weapon system developments.

That battle is definitely coming and two results are certain: the reaction will be triggered more by media accounts of the problem than its root cause and the solution will be politically expedient rather than correct. Both can be pre-empted by dusting off a previously successful solution: FFRDCs. Federally Funded Research and Development Centers were born in response to a Cold War threat. The advantages of these national assets have been lost on a generation of government policy makers who have accepted the institutionalization of cost overruns in procurement.

Most overruns can be traced to technological maturation and changing requirements. With respect to the former, a march "Back to Basics" is currently the preferred solution. When Apple Computer had the inevitable development problems rushing iPod to market, it is doubtful anyone in the board room said "let's go back to basics and ship a CD player but with advanced packaging". If they settled, a competitor would have solved the problem. Pushing the envelope on technology means risk and the occasional failure. In the private sector, companies who do not risk and innovate go out of business. In government procurement, however, bad programs still get funded and fall dangerously short of mission requirements. While lowering the bar on acceptable developmental risk is good in theory, subtlety is lost on the procurement hierarchy. Because "Back to Basics" is being imposed in response to endemic overruns, the bureaucracy will instead internalize a message of "better second best than over budget".

Changing requirements, as we often see on programs like SBIRS (Space-Based Infrared System), become a self-inflicted wound. Changes cost money. When programs overrun budgets, funds come from less politically supported programs. Cutting those programs pushes their requirements to the surviving platforms, exacerbating program cost and delay problems. While NASA is evolving from its "better, faster, cheaper" mantra of the '90s, it did serve a function. DoD has not pursued that strategy believing that unlike unmanned space probes, lives are at stake with its programs. As we found in Iraq, lives are also at stake when we send troops into battle with equipment that does not address a current threat. Development cycles are too long, and technology and threats are evolving too quickly, to maintain the procurement status quo. Locking in requirements and technology early and then fielding fewer numbers but more generations of a system will win both operationally and economically. Someone has to say "enough" in the development process and turn to production. Asking a contractor to fill that role is not the right place to look.

With the country at war, it is a particularly bad time for defense contractors to be the lightning rod for this issue. They should ultimately be happier with more definable production contracts than the ever changing research, development and integration phases that have generated the overruns. The government pushed them in that direction after downsizing its acquisitions staffs. If the Pentagon does not want this work, and the contractors cannot push back in managing their customer, returning this work to the FFRDCs is a logical solution.

FFRDCs were created after World War II to ensure government had a unique talent pool to take early stage technology and developmental risks. Despite successfully playing that role in a wide range of important programs from ICBMs to GPS, they are at risk as much of this work has been transferred to the private sector. The recent IPO of QinetiQ, the equivalent British organization, illustrates just how far the pendulum has swung in blurring the roles of government facilities and private enterprise. FFRDCs as currently structured have an important part to play in returning to their original role in the procurement process.

With FFRDCs as intermediaries, there would be more requirements discipline between customer and contractor. The disaggregation of developmental and production interests will improve both schedule and cost performance. Overruns are not new and while constrainable by this process, will not go away. The press of overruns, however, has the potential to create more damage than the overruns themselves. Here FFRDCs have two unique additional advantages. Costs are likely to be less visibly associated with specific programs and federal agencies are better positioned to weather a media storm than contractors with front page stories attempting to link overruns to executive pay or company profits.

As an investor I am a firm believer in outsourcing and the ability of private enterprise to more efficiently reduce system costs than the government can. That assumes an efficient market. Because of the politics of federal spending such as decisions based upon employment by Congressional district, it is a fallacy to believe there is a level playing field where executives speak their mind and the best performance is always rewarded. We cannot change the system, but we can win by playing within its constraints. Assumption of risk is hard-wired into most great American advancements and we should not try to legislate it out of the procurement process. FFRDCs were developed to assume that risk. They can address many root causes of today's overruns as well as play a major role in providing political air cover for remaining issues. We should remember our history better than the gas lines of the 1970s, and let them. ●

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## Contract Overruns: New Relevance For An Old Playbook