SUSTAINING THE UK'S DEFENCE EFFORT

Contractor Support to Operations Market Dynamics

Henrik Heidenkamp

Royal United Services Institute

WHITEHALL REPORT 2-12

DEFENCE, INDUSTRIES AND SOCIETY SERIES

First Published April 2012

Whitehall Report Series
ISSN 1750-9432

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Printed in Great Britain by Stephen Austin & Sons Ltd for the
Royal United Services Institute, Whitehall, London, SW1A 2ET, United Kingdom

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Cover: A Warthog all-terrain protected-mobility vehicle on trial at ATDU Bovington before it replaced the Viking in-theatre in Afghanistan. In August 2009, Thales and ST Kinetics were awarded a £20 million MoD contract to modify the Singapore Army Bronco into the Warthog under the Urgent Operational Requirement (UOR) programme. *Photo courtesy of Andrew Linnett/Crown Copyright*.

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Henrik Heidenkamp

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Printed in the UK by Stephen Austin and Sons, Ltd.

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Acknowledgements

The author would like to thank Professor Trevor Taylor and Dr John Louth of RUSI for their long-term support of the research project and their considered remarks, which have been invaluable to the development of the report. In particular, the author wishes to express sincere appreciation to Andrew Higginson OBE (Managing Director, Higginson Associates Ltd) for his critical assessment of the report and the valuable insights he offered into the practical realities of CSO policy.

I. Introduction

The strategic environment at the beginning of the twenty-first century features various international challenges and potential conflicts that may require the use of military force as part of a comprehensive political approach.[1] Flexible and adaptable armed forces that can be used for different sorts of missions are an essential component of a modern nation-state's foreign, security and defence policy, reflecting its capability to act in the international system.[2] These missions will likely be a significant distance from the UK, undertaken at relatively short notice, and have specific operational requirements that may differ from previous deployments.[3]

Consequently, the UK needs rapidly deployable forces that can be sustained beyond national boundaries and potentially worldwide.[4] In this context, contractor support to operations (CSO) has become an essential component of the ability to both deploy and sustain the UK's military instrument. The future dynamics in the CSO market will not only determine the availability, quality, sustainability, affordability and commercial viability of CSO services, but also fundamentally affect the UK's ability to ensure the security of its citizens and its influence on the global stage. It is therefore crucial to assess the key drivers of the interactions between the demand and supply side of the CSO market – that is, the public and private sectors, respectively.

The core argument is that public and private CSO stakeholders have to effectively confront the tensions in the market, which originate from the tensions between the inherent dependence of the UK on CSO to conduct military operations abroad; the lack of a coherent strategic approach to CSO on the demand side; an emerging multinational CSO policy; the uncertain level of demand for CSO during future UK operations; and the commercial pressures for companies to sustain and advance their commercial viability in the CSO market at acceptable financial and reputational risks.

Setting the Scene

The use of contractors in the launch and sustainment of operations is nothing new. In February and March 2003, a team of sixty-five – comprised of military personnel and engineers from Alvis Vickers – deployed to Kuwait to modify Challenger 2 main battle tanks to adapt them to the requirements of Operation *Telic*. The cost of the contractor support to carry out the modifications, which in retrospect performed very well, was £3.6 million.[5] In total, about 1,500 civilian contractors were deployed into the Gulf region from 2003. The final MoD report on operations in Iraq states, with regard to the task of force generation, that:[6]

> The very considerable success in delivering equipment against very demanding time and performance criteria owed much to the excellent

> contribution of contractors in the face of relatively late changes to the force composition and constraints on early consultation with industry.

The involvement of contractors in the sustainment of defence efforts has grown in recent years and is now significant. Andrew Higginson estimates that UK CSO expenditure for 2010 was around £2.6 billion.[7] The net additional costs of UK operations in Afghanistan (£3.8 billion) and Iraq (£95 million) totalled approximately £3.9 billion in the fiscal year 2010/11, which ended on 31 March 2011,[8] suggesting by best estimate that CSO expenditure accounted for at least 60 per cent of the UK's overseas operational defence sustainment effort in 2010.

Further, during Operation *Herrick*, the number of companies supporting the UK in theatre rose from twenty-two (with 2,030 employees) in July 2008 to sixty-seven (with 4,867 employees) in July 2010.[9] In Afghanistan, contractors comprise around 35 per cent of the Ministry of Defence's (MoD) total workforce.[10]

The Aim of the Report

While a lot of research has been undertaken on CSO, much of it is on its political implications. As Trevor Taylor points out, the existing literature focuses on three questions: 'what is exactly going on, what are the drivers behind current developments, and what are the implications of these developments for the ways in which we analyse political and military power?' These questions are important to address, and the literature on them has provided valuable insights into the concept and operational conduct of CSO.

However, from the perspective of political decision-makers, military planners and practitioners – as well as industrialists – a key question concerns how the CSO market will develop in the short, medium and long term. Important questions that need to be answered include:

- What are the core determinants of the future development of the CSO market?
- What are the challenges and opportunities for public and private market actors?
- How will the political agenda and corporate decisions affect the availability, quality, sustainability, affordability and commercial viability of CSO services?

At the centre of the short-, medium- and long-term outlook for the CSO market lies the question of what direction the interactions between the forces of demand and supply will take. Both public and private CSO stakeholders (see Figure 1) have an intrinsic need for an in-depth understanding of these future dynamics, which are both the cornerstones of their professional environments and a crucial determinant of the UK's defence effort.

The timeliness of these questions is underlined by the UK government's intention to run down its military presence in Afghanistan by 2015. This presents today's CSO contractors with a strategic challenge: how can they survive the collapse in that element of demand for their services? For the UK government, there is the issue of which contractors and services can be relied on to be around in the event of an operation in the future. Both the commercial viability and the security of supply in the CSO market are the core issues at hand.

Figure 1: CSO market actors (not exhaustive).

Source: Heidenkamp, 2012.

In order to answer this complex set of questions, this report assesses the specifics of the CSO market structure, identifies the private and public CSO market actors, and examines the key drivers of future CSO market dynamics. The report concludes by describing the major implications for private and public CSO market actors.

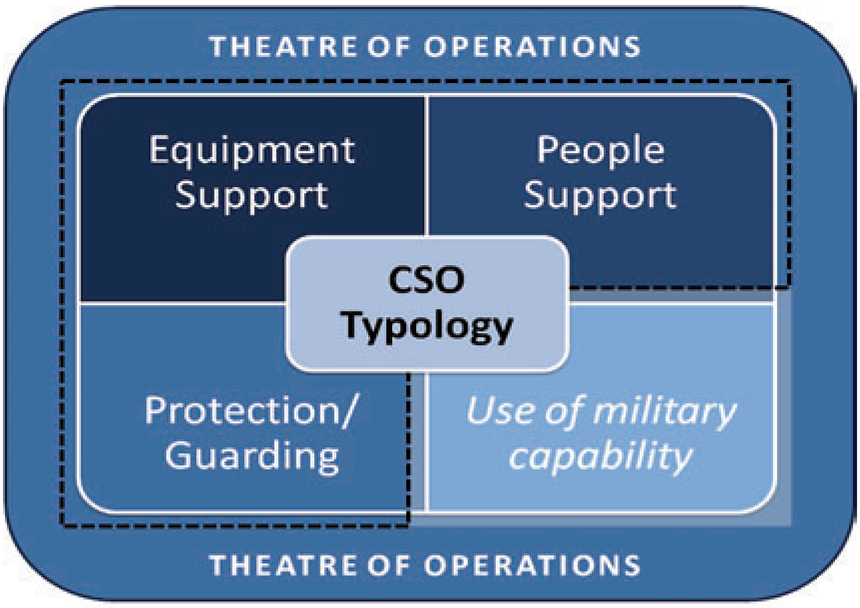
The report applies a qualitative-empirical methodological approach[11] that aims to identify the fundamental characteristics of the CSO market and to examine the implications of its key drivers on the interaction between the demand and supply side. This approach follows the hermeneutic premise[12] that a scientific explanation requires an accurate and sufficiently comprehensive description of the research object. Hereto, the report exploits the available public literature on the topic, including governmental policy and review papers on CSO and outsourcing, parliamentary reports and committee hearings, corporate publications (such as annual reports and contract announcements), academic publications and media coverage. The report also draws on the findings of interviews with senior experts on CSO in the public and private sectors.

A CSO Typology

This report focuses on private companies that are contracted by the UK government to provide non-offensive, in-theatre commercial services for deployed operations in the field of equipment support, people support, and static and mobile protection/guarding (see Figure 2).

The report uses three categories of services provided. First, equipment support: contractors provide servicing, maintenance and repair of items required for operational capability in theatre. Secondly, people support, including the provision of shelter, food and water, personal hygiene facilities, laundry services, mail and other communication services, medical support, recreation and entertainment facilities for troops on base. Thirdly, the provision of security to people and fixed assets, as well as transport of supplies to a theatre and within it.[13]

Figure 2: A CSO typology.



Source: Heidenkamp, 2012.

Although there is a fourth category, at present in the case of the UK there is little need to consider the role of companies that offer services directly related to operational effect.[14] The UK is reluctant to contract companies for services like interrogation, intelligence analysis, the operation of military equipment, training and offensive military operations. As an illustration of such possibilities, consider the companies Cubic Corporation and L-3 MPRI, which the US uses to provide operational and other kinds of training to its own and local armed forces around the world – in part as a substitute for deploying US forces.[15]

However, the UK does use contractors for a few non-kinetic operational roles. The most obvious group of people are translators who may accompany troops on patrol. Some specialised kit – for example, the Hermes 450 UAV – is operated by company personnel under the direction of military staff. Finally, in the particular context of Afghanistan, contractors have been used for the delivery of logistics, especially from Karachi through Pakistan.

The current British approach to CSOs, being dependent on political preferences, attitudes and decision-making, may change in the future and accordingly require a broader definition of CSO as a framework for analysis. David Cameron's announcement in October 2011 that ships sailing under the British flag would be permitted to carry armed guards on high-risk routes to combat the threat from pirates could be perceived as a sign of changing political preferences and attitudes regarding a more expanded use of armed contractor.

Notes and References

1. Hans J Giessmann, 'Bundeswehr zur Praevention', in Hans J Giessmann and Armin Wagner, *Armee im Einsatz: Grundlagen, Strategien und Ergebnisse einer Beteiligung der Bundeswehr*, DSF Volume 191 (Baden-Baden: Nomos, 2009), p. 59.

2. Franco Algieri et al., 'Militrärische Aspekte der Europäischen Sicherheits und Verteidigungspolitik im Lichte der europäischen Ratspräsidentschaft', *Schriftenreihe des Wissenschaftlichen Forums für Internationale Sicherheit e.V.* (Vol. 26, Edition Temmen, 2008), p. 23; Michael Howard, 'Military power and international order', *International Affairs* (Vol. 40, No. 3, July 1964), pp. 397–408.

3. The Defence Planning Assumptions (DPAs) of the 2010 Strategic Defence and Security Review (SDSR) 'envisage that the Armed Forces in the future will be sized and shaped to conduct: an enduring stabilisation operation at around brigade level (up to 6,500 personnel) with maritime and air support as required, while also conducting: one non-enduring complex intervention (up to 2,000 personnel), and one non-enduring simple intervention (up to 1,000 personnel); or alternatively: three non-enduring operations if we were not already engaged in an enduring operation; or: for a limited time, and with sufficient warning, committing all our effort to a one-off intervention of up to three brigades, with maritime and air support (around 30,000, two-thirds of the force deployed to Iraq in 2003).' HM Government, *Securing Britain in an Age of Uncertainty: The Strategic Defence and Security Review* (SDSR), Cm 7948 (London: The Stationery Office, October 2010), p. 19.

4. Ministry of Defence, 'British Defence Doctrine', Joint Doctrine Publication 0-01, 4th Edition, Development, Concepts and Doctrine Centre, Shrivenham, November 2011, pp. 1–8, <http://www.mod.uk/NR/rdonlyres/FDB67DF9-5835-47FD-897D-CA82C17EC7A5/0/20111130jdp001_bdd_Ed4.pdf >, accessed 19 April 2012.

5. National Audit Office, 'Operation TELIC: United Kingdom Military Operations in Iraq', 11 December 2003, p. 13.

6. Ministry of Defence, 'Operations in Iraq: Lessons for the Future', December 2003, p. 6.

7. Andrew Higginson, 'Contractor Support to Operations (CSO): Proactive or Reactive Support?', *RUSI Defence Systems* (Vol. 13, No. 2, October 2010), p. 16.

8. Ministry of Defence, *Annual Report and Accounts 2010-11: For the Year Ended 31 March 2011*, HC 992 (London: The Stationery Office, July 2011), p. 47.

9. House of Commons, 'Operations in Afghanistan', Defence Select Committee Written Evidence from the MoD, 2011, pp. 90–91. It should be stressed that the author regards these official figures on CSO spending and personnel to be conservative estimates. The author's interviews with senior CSO experts revealed doubt over the government's ability to provide accurate, updated figures on CSO. Therefore the existing official figures, as well as those provided by analysts and commentators, present a general trend but should be treated with caution.

10. Calculation by the author based on MoD force deployment figures. See Ministry of Defence, 'Operations in Afghanistan: British Forces', <http://www.mod.uk/DefenceInternet/FactSheets/OperationsFactsheets/OperationsInAfghanistanBritishForces.htm>, accessed 19 April 2012.

11. Volker Dreier, *Empirische Politikforschung* (Munich: Oldenbourg, 1997), pp. 69–80.

12. Ulrich von Alemann, *Politikwissenschaftliche Methoden* (Opladen: Westdeutscher Verlag, 1995), pp. 50–60.

13. Trevor Taylor, 'Review article: Private security companies in Iraq and beyond', *International Affairs* (Vol. 87, No. 2, March 2011), p. 448.

14. There is substantial literature on the private military and security companies (PMSCs) providing services in the operational space, where military capability is used. See, for example, Foreign and Commonwealth Office, *Private Military Companies: Options for Regulation*, HCP 577 (London: The Stationery Office, February 2002); Sam Perolo-Freeman and Elisabeth Sköns, *The Private Military Services Industry*, SIPRI Insights on Peace and Security, No. 2008/1 (Stockholm: SIPRI, 2008); Sarah K Cotton et al., *Hired Guns: Views about Armed Contractors in Operation Iraqi Freedom* (Santa Monica: RAND, 2010); Sabelo Gumedze, *Merchants of African conflict: More than just a pound of flesh*, Monograph 176 (Pretoria: Institute for Security Studies, 2011).

15. See <http://www.mpri.com/web/index.php/content/what_we_do/military_education> and <http://mss.cubic.com/MissionSupportServices/OperatingDivisions.aspx>, accessed 19 April 2012.

16. *CBSNews.com*, 'Britain to allow armed guards to combat sea piracy', 30 October 2011.

II. The CSO Market Structure

The interactions between public and private CSO actors need to be examined against the specific structure of the market in order to capture the complexity of its future development. The three main current British CSO sub-markets – the market for equipment support, people support and protection/guarding – each add a specific value to the UK's defence effort but also present specific challenges to public and private CSO players. The sub-markets differ with regard to their barriers to entry, the level of skills required to perform the contracted tasks and the exposure of contractor employees to danger (see Table 1).[1]

Table 1: Characteristics of CSO sub-markets.

CSO Sub-Market	Barriers to Market entry	Required Skill Level	Exposure to Danger
Equipment Support	High	High	Low
People Support	Medium	Medium	Low
Protection/ Guarding	Low	Medium	High

Source: Heidenkamp, 2012.

Equipment Support

The barriers to entry and the required skill levels are particularly high in the market for equipment support. New companies in this strongly regulated market face high initial capital investment for the development of proprietary technology and know-how, and compete with already established companies, usually the original equipment manufacturers, which benefit from their technical knowledge, experience curve cost advantages,[2] economies of scale and customer loyalty. Contractors providing equipment support have a relatively low exposure to danger as they are usually deployed within military rear echelons.

As an illustration of equipment support to operations, consider General Dynamics and the Defence Support Group (DSG), which operate in this market among other companies like BAE Systems, Thales and Finmeccanica. In March 2011, General Dynamics was awarded a £2 million contract by the MoD to support the newly opened Equipment Sustainability System (ESS), run by the DSG at Camp Bastion in Afghanistan.[3] ESS delivers an in-theatre equipment regeneration capability that would otherwise only be achievable by sending the equipment back to the UK, thereby saving costs and turnaround time of vital front-line equipment. DSG, whose team grew incrementally from the initial twenty-nine in October 2009 to over 100 members in May 2011, has been awarded main contractor status to operate ESS until 2013.[4]

People Support

The market for people support has lower barriers to entry, simply because the needs of troops have much in common with civilians in general and therefore many businesses already have relevant expertise. Although the up-front capital investments for the building of facilities and the establishment of supply routes are still high, the in-service costs are comparatively low.[5] The labour costs are constrained by the strong job demand in the market, especially from locals and 'third-country nationals',[6] and the comparatively lower skill levels required by the contracted tasks.[7] Like the market for equipment support, people-support operations have a relatively low exposure to danger, since contractors are usually deployed within military rear echelons.

As one example, under its contract awarded by the Foreign Office and through the MoD's Afghanistan Soft Multi Activity Contract (MAC),[8] the global engineering, construction and service company KBR, which also holds the MoD's CONLOG contract,[9] provides life support and healthcare services as well as facilities management, infrastructure support and hardened accommodation in Afghanistan. KBR delivers a comprehensive suite of services such as medical support (including nursing and medical supplies), sustenance, laundry and environmental services. It also supports British troops with essential services including running water bottling plants and catering, as well as constructing shelters and other buildings.[10]

Consider also Purple Foodservice Solutions, a company composed of DBC Foodservice, Vestey Foods UK and Supreme Foodservice Solutions. Since October 2006, the company has been the prime contractor for the MoD's Worldwide Food Supply and Operational Rations Contract, and also operates the overseas depot locations in Afghanistan. The contract runs until September 2013 and had an initial value for the company of £150 million in the first year.[11]

Other companies providing construction services as part of their people-support business include the US companies RECON International, which built the dining hall in Camp Bastion for £3.1 million between December 2010 and March 2011,[12] and Turner Facilities Management, the Prime Contract Infrastructure Support Provider in Southern Iraq (ISP) for the MoD since 2004.[13] The Prime Contract Infrastructure Support Provider in Afghanistan was awarded by the MoD to KBR in November 2006,[14] and at the end of 2011 KBR was successful in winning the rebid of the ISP contract.[15]

Protection and Guarding

The market for protection and guarding, by its nature, features a very high exposure to danger. On the other hand, the barriers to entry are relatively low, as indicated by the large number of new and often small firms competing in this market segment.[16]

In theory, contractors should be adequately trained and equipped to persist in a highly demanding threat environment, but in practice contractors may lack such expensive professionalism.[17] The low barriers to entry in the market for protection/guarding therefore generate a highly competitive business environment.

One of the very active companies in this market is G4S, the largest security company in the UK. In March 2010, the company was awarded a three-year contract by the Foreign Office for the provision of security services in Afghanistan. The contract is worth £23 million per year and covers the static protection of personnel and assets at a number of UK government sites in Afghanistan, including the British Embassy in Kabul, and the mobile protection of UK government employees as they move around Afghanistan.[18]

It should be mentioned that trained guards may have extensive military experience and so have the potential for offensive capabilities and services. Also, in reality the boundary between protection/guarding and 'offensive' action involving initiative in the use of lethal force can be hard to distinguish.

A Multi-Layered Market Structure

The specific characteristics of these CSO sub-markets point to the fact that the overall market does not only feature one layer of market dynamics. Rather, its multi-layered structure makes the CSO market a complicated place for the policy-maker, military practitioner and industrialist.

The sub-markets pose specific challenges to the public and private CSO stakeholders that require sub-market-specific solutions, but at the same time need to be approached in a comprehensive and coherent CSO policy framework. However, the required degree of coherence may be quite difficult to achieve as the sub-markets may develop in different directions, with different centres of gravity and at different speeds.

The characteristics of the public and private CSO market actors significantly affect their capability to address these challenges. They shape their activities and positioning in this environment, especially regarding the transactional processes among them. The next chapter assesses the nature of public and private CSO market actors, and the specific perspectives each actor has of the market, and provides a conceptual framework for the transactional processes among them.

Notes and References

1. Trevor Taylor, 'Review article: Private security companies in Iraq and beyond', *International Affairs* (Vol. 87, No. 2, March 2011), p. 446.

2. The experience curve effect states that the more often a task is performed, the lower the cost of doing it. The task can be the production of any goods or service. Each time cumulative volume doubles, value added costs (including administration, marketing, distribution and manufacturing) fall by a constant and predictable percentage.

3. 'General Dynamics UK plays key role in Camp Bastion Equipment Sustainability System', 7 March 2011, <http://www.generaldynamics.uk.com/news/camp%20bastion%20equipment%20sustainability%20system>, accessed 19 April 2012.

4. 'DSG: Supporting Camp Bastion', 5 April 2011, <http://www.defencemanagement.com/feature_story.asp?id=16148>, accessed 19 April 2012.

5. Author interviews with senior industrial experts.

6. Figures of the US Government Accountability Office show that, as of 31 March 2010, Iraqi/Afghan nationals (138,507) and third-country nationals (76,988) accounted for 82 per cent of all US Defense, State and USAID contractors in Iraq and Afghanistan (total: 262,631, US nationals: 45,927). See Government Accountability Office, 'Iraq and Afghanistan: Defense, State, and USAID Face Continued Challenges in Tracking Contracts, Assistance Instruments, and Associated Personnel', 11-1, October 2010, pp. 44–45.

7. Of course, some tasks in the people support sub-market require a high level of qualification as in the equipment support sub-market but the required skill level of the majority of the workforce in this sector is comparatively low.

8. KBR, 'Afghanistan Soft Multi Activity Contract (MAC)', <http://www.kbr.com/Projects/Afghanistan-Soft-Multi-Activity-Contract/Afghanistan-Soft-Multi-Activity-Contract.pdf>, accessed 19 April 2012.

9. The CONLOG contract, now renamed the Operational Support Capability Contract, is an enabling contract to secure a wide range of logistical support services for operations and exercises when the military requires them.

10. In Iraq and Afghanistan KBR also provided temporary deployable accommodation (TDA) and logistical support for 7,000 British troops with purpose-built tented facilities. This contract included the deployment, construction, operation and maintenance of twenty camps. See KBR, 'Temporary Deployable Accommodation (TDA): UK/Iraq/Afghanistan', <http://www.kbr.com/Projects/Temporary-Deployable-Accommodation/Temporary-Deployable-Accommodation.pdf>, accessed 19 April 2012.

11. See <http://www.purplefoodservicesolutions.com/faqs.htm>, accessed 19 April 2012.

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13. Turner Facilities Management Defence, 'Case Study: Front Line Support', <http://www.turnerestatesolutions.co.uk/media/13608/front%20line%20support%20-%20iraq.pdf>, accessed 19 April 2012.

14. KBR, 'Afghanistan Infrastructure Service Provider (ISP)', <http://www.kbr.com/Projects/Afghanistan-Infrastructure-Service-Provider/Afghanistan-Infrastructure-Service-Provider.pdf>, accessed 19 April 2012.

15. Seeking Alpha, 'KBR's CEO Discusses Q4 2011 Results: Earnings Call Transcript', 23 February 2012, <http://seekingalpha.com/article/387651-kbr-s-ceo-discusses-q4-2011-results-earnings-call-transcript>, accessed 19 April 2012.

16. For a list of companies in this sub-market see, for example, the list of the 307 International Code of Conduct for Private Security Service Providers (ICoC) Signatory Companies at <http://www.icoc-psp.org/uploads/Signatory_Companies_-_February_2012_-_Composite_List_SHORT_VERSION.pdf>, accessed 12 April 2012. The list of members of the British Association of Private Security Companies (BAPSC) is available at <http://www.bapsc.org.uk/?membership=list-of-members>, accessed 19 April 2012.

17. T X Hammes, 'Private Contractors in Conflict Zones', *Joint Forces Quarterly* (Issue 60, 1st Quarter 2011), pp. 29–30.

18. G4S, 'G4S awarded British Government contracts', 25 March 2010, <http://www.g4s.com/en/Media%20Centre/News/2010/03/25/G4S%20awarded%20British%20Government%20contracts/>, accessed 19 April 2012.

III. CSO Market Actors

The Demand Side: Public CSO Market Actors

It would be misleading to assume a single, one-dimensional 'public consumer' in these sub-markets. Instead, the markets feature multiple public CSO market actors, which differ, sometimes significantly, with regard to the nature of the benefit they receive from CSO; their capability to monetise the value of CSO (monetisation refers here to the process of converting some benefit received in non-monetary form – such as security – into monetary terms); and their focus area of concern in the CSO market.

These differences among them are relevant because the individual public actors do not operate as independent consumers, though the British political system and societal norms tie them together. As a consequence, there is a constant pressure in the public sector to balance the specific demands of its market actors.

The British Armed Forces and the Ministry of Defence

The British military – from the private on the ground to the generals in Permanent Joint Headquarters (PJHQ) – and the Ministry of Defence are the most obvious consumers of CSO. Their benefit derives primarily from the resources saved by outsourcing tasks to the private sector. Savings can be realised through lower human resource costs, less expenditure on research and development, and cheaper through-life support costs.

The real gains would appear to be made in peacetime, when the MoD does not have to pay for a large number of support personnel who would have nothing to do except train and simply be available if needed. In addition, contractors provide essential functional skills for today's operational environment, which the military appears to be unable to generate, at least in the short term.

Whereas financial savings can be measured at least in principle, operational enhancements gained through outsourcing – such as more available combat troops due to the release of human resources from non-combat functions and the provision of required niche capabilities by contractors – are much more difficult to evaluate. The complex nature of today's asymmetric conflicts makes it especially difficult to measure military performance overall, and to evaluate the value added of CSO in particular.

The main area of concern in the CSO market for the British armed forces and the MoD remains the in-theatre availability and sustainability of high-quality products and services provided by contractors, especially in the fields of equipment and people support.[1] Therefore, the main tasks for contract sponsors[2] are the formulation of coherent operational requirements for contractors, the conclusion of flexible and effective contracts, the development of adequate management structures at home and in theatre, and the building of appropriate relationships at the military-contractor interface.

The Policy-Makers Outside the MoD

Parliament and policy-makers in government departments other than the MoD (the Cabinet, Foreign Office, Department for International Development and Treasury) are another set of public consumers of CSO. Their consumption of services is twofold.

The primary benefit from CSO for these public actors is a greater freedom of action in British foreign and fiscal policy. Outsourcing non-core military tasks allows the government to match society's demand for a light military footprint in operations abroad, while also enabling politicians in the government and parliament to communicate a more cost-effective utilisation of scarce public financial resources – a 'political imperative' in an age of austerity and pressing domestic challenges, as stressed by former Secretary of State for Defence Liam Fox in his speech at Chatham House on 19 May 2011, in which he argued that 'tackling the crisis in public finances is not just an issue of economics but an issue of national security too … central to sustaining in the long term Britain's reach, military power and influence.'

In addition, the Foreign Office and DfID make direct use of contractors for their overseas operations. Between 2005 and 2010 the Foreign Office paid £72.2 million for the services of private security companies in Afghanistan.[4] These figures highlight the fact that the market for CSO is not confined to the military sector, not least due to the limited capability of the armed forces to provide protection for deployed Foreign Office and DfID staff.[5]

The monetisation of the CSO benefit for these public customers is far more complex than for the military and MoD. Budgetary savings from outsourcing, although contested by diverging evaluations of the contract's quality and debatable calculations of transactional costs – the costs of managing contracts, including arranging bids, monitoring outcomes and taking legal action for contract failures[6] – may be measured in monetary terms. However, gains in the political freedom of action – for example, to credibly threaten the use of force and/or actually deploy military forces if needed – are hard to monetise and do not necessarily translate into increased public support for policy-makers.

These public consumers are concerned with safeguarding political primacy in this core area of statehood; maintaining their capability to act in line with foreign, security and defence policy; and the reduction of public expenditure. Accordingly, they try to pursue a balanced approach towards CSO, demanding effective oversight and accountability mechanisms, in order not to appear driven in their strategic decision-making processes by private actors and also to prevent fraud and corruption in the CSO market. Of course, as regulation in this sector is a highly complex issue, and as policy-makers follow their own political and personal agendas in daily politics – being driven by their constituents' demand for economic growth and a healthy job market – there has been little regulation of this sector so far in practice.

British Society
Finally, although not a direct user of CSO services, there are also benefits to society. As the end-recipient of the British national defence effort, an increase in national defence capabilities through the use of contractors resembles a direct added value for the British public. In addition, the lighter military footprint in operations abroad corresponds with the restrained public attitude towards the use of military force overseas. The use of CSOs may therefore be regarded as a successful alignment of government policy with public preferences. Moreover, increasing use of contractors may provide cost savings, the benefits of which can be passed onto society through a healthier national budget and the use of resources elsewhere in public expenditure.

The monetisation of these benefits is difficult: defence outputs are of elusive value to wider British society.[7] There is certainly some added value, but its actual degree will differ among societal actors depending on the relevance they attribute to the defence sector and their general perception of the relationship between the state and its citizens. Furthermore, as the majority of the public – apart from some experts in academia and the media – does not have a professional interest in CSO, the government acts as a gatekeeper to the CSO market. Thus the area of concern for wider British society appears to be limited to an effective oversight, control and accountability mechanism for defence spending, rather than deployed contractors as such.

However, as can be seen from the case of Sandline International[8] – a UK-based company that provided weapons to Sierra Leone in violation of a UN arms embargo in 1997 with partial support from the British government and thereby caused an intense public debate – this passive attitude of the public towards contractors may shift if they are not used in line with public preferences.

The Supply Side: Private CSO Market Actors
The nature of the supply side in the CSO market is profoundly different. Corporate strategies and decisions taken by companies in the market usually do not combine to a coherent, aggregated 'CSO industry' approach. The

differences among private CSO market actors – market power, experience, technological and production advantages, finance and so on – determine each company's individual position, revenue and sustainability in the market for CSO.[9]

However, there are three trends that affect the supply side as a whole: first, the broadening of business models; second, the increasing complexity of ownership structures; and third, the increasing multinational alignment of corporate structures. These trends determine the relationship between the demand and the supply side and shape the companies' strategic direction. They determine what kind of products and services are offered, to which customers they get sold, who makes key corporate decisions and the level of control exercised by the demand side.

Broadening Business Models

The blurring of the traditional boundaries between security and defence has prompted companies to explore non-traditional business areas, especially in civilian markets. Whereas companies in the market for people support and protection/guarding have been quite successful in offering their services to a broader customer base, big original equipment manufacturers (OEMs) – although eager to extend their business model – sometimes struggle to offer services in the civilian market due to their specific corporate structures and way to market. For any company, the commercial viability of each business field – defence, security and civilian – in relation to corporate risk assessments is a precondition for future exploration.

Breadth in a company's business model, going beyond the military operational field, potentially increases a company's revenue base and may improve its capability to survive in a difficult defence market environment. However, especially for companies with dominant non-defence branches, there is an incentive to leave the market for defence (including CSO) if revenues become too small or financial risks too big. Of course, in practice a company's civilian and military branches are not generally self-sufficient. They are often connected by financial, technological and human resources aspects and can be regarded as cross-subsidising. Furthermore, the continued engagement in the defence sector may function as a foundation for contracts in the civilian sector and vice versa. This setup highlights the integration of the CSO market into the wider commercial market for security and defence products.

To illustrate, consider companies like BAE Systems, KBR, Serco, Thales Group and Finmeccanica, which all offer CSO elements and, according to Defence Analytical Services and Advice, were among the major MoD defence contractors in 2009/10.[10] On the one hand there are companies like Serco and KBR, for which defence is already a relatively small contributor to a broad base of revenues. Serco's defence branch accounted for only 21 per cent of the company's overall revenue in 2010. KBR, which holds the US Army's LOGCAP III/IV[11] contracts and the UK's MoD CONLOG contract,[12] generated 37 per cent of its overall revenue in the year 2010 from its infrastructure, government and defence business segment, which includes significant activities for civilian federal agencies in the US.[13]

BAE Systems, Finmeccanica and Thales, on the other hand, mainly conduct their business in the defence sector. As a 'pure' defence company, BAE Systems only has minor activities in the civilian sector. Finmeccanica's defence-sector related business activities accounted for around 59 per cent of the company's annual revenue in the year 2010.[14] Although Thales has significant civilian business activities in the aerospace and transport sector (constituting 42 per cent of its overall revenue in the year 2011), it still generated 57 per cent of its revenue in 2010 from its defence activities.[15] Nevertheless, the wider service business is increasingly important to these traditional defence OEMs. They have extensively developed their service branches, as can be seen from BAE Systems, which generated 49 per cent of its revenue in the first half of 2011 from service activities.[16]

Increasing Complexity of Ownership Structure

The interests of company ownership are another key aspect for the strategic direction of future development. Shareholders like the French state, which together with the state-owned Dassault company holds 52.89 per cent of Thales,[17] and the Italian Ministry of Economy and Finance, which retains 30.2 per cent of the shares in Finmeccanica,[18] have, apart from their natural economic interest, a strong incentive to ensure an effective national defence capability through a healthy defence industrial base.

National defence policy considerations may sometimes – or, one could argue, should regularly – outweigh shareholder-value considerations. This calculation does not apply in the same way to private shareholders, which are usually institutional, internationally orientated market actors, with a diverse shareholder structure of their own and a dominating focus on shareholder value. In this sense, the statement by former Secretary of State for Defence Dr Liam Fox in February 2011 that 'industry is ultimately answerable to shareholders for their profits while government is answerable to the taxpayers for the management of their money'[19] is correct, but also appears inadequate without mentioning government responsibility for the safety of its citizens.

As Table 2 shows, in December 2011 the seven largest shareholders of BAE Systems were institutional investors from the banking, private equity and insurance sector, which together hold 38 per cent of BAE Systems' issued ordinary share capital. Foreign shareholding in BAE Systems as of December 2011 was 37 per cent.

Table 2: Shareholder structure of BAE Systems.

Name of Shareholder (as of 31 December 2011)[20]	% of Issued Ordinary Share Capital
AXA S.A.	5.00
Barclays PLC	3.98
BlackRock, Inc.	5.16
Invesco Ltd.	12.00
Franklin Resources, Inc.	4.92
Legal & General Group PLC	3.99
Silchester International Investors LLP	3.01
Total	**38.06**
Foreign Shareholding (as of 27 December 2011)[21]	**37.07**

Source: Heidenkamp, 2012.

The globalisation of a company's way to the market internationalises the corporate decision-making process. For example, business deals envisaged by subsidiaries of non-domestic companies in the UK are regularly scrutinised by company headquarters outside the UK for financial and reputational risk. Such risk assessments take place in a global context and can be driven by various economic, political, societal, technological and legal factors beyond those in the UK.[22]

While in some cases the 'home' government may still own a significant percentage of a defence company, modern companies are, in essence, owned by individuals and organisations from all around the world, with these shareholders having either no particular identity or alternatively a number of varied national identities or affiliations.

These multi-layered, transnational ownership structures raise legitimate questions about the influence of governments and parliaments (as the monopolists of force in Western democracies) on the long-term strategic development of the defence industrial base at the national, regional and global level, as well as on the transparency and accountability of commercial decision-making procedures.

Increasing Multinational Alignment of Corporate Structures
When considering business models, environment, and the financial and human resource base of the CSO market, a global perspective is necessary. Large Western security and defence companies compete in an international context. Particularly for companies originating from Europe, the core position of 'home' markets has declined, while the importance of customers from North America, Asia, the Middle East and Latin America has increased.

For example, BAE Systems has identified Saudi Arabia and India – together with the United States, Australia and the United Kingdom – as 'home' markets where the group has established or seeks to establish a good position in the defence industrial base.[23] Similarly, Thales, which today generates close to 80 per cent of its revenues outside France,[24] calls Mexico, Brazil, India, China, Southeast Asia and the Middle East its target growth regions.[25]

Global investments are part of most large Western security and defence companies' business operations and expansionary plans. Coupled with their international ownership structure, this characterises them as truly multinational or even global corporations with highly globalised operations, ownership structures, workforces and customers.

As such, they also have a multinational human resource structure that presents them with the challenge of integrating different business cultures and linking them to the economic, political and wider societal setting in these countries. For example, of Finmeccanica's 71,071 employees worldwide, 43.2 per cent work outside of Italy, including 10,860 in the US.[26] Thales employs 1,820 of its 68,000 employees in South Korea; 630 in China; 480 in Singapore; 250 in India; 880 in Saudi Arabia; 390 in the United Arab Emirates; 320 in Brazil; and 120 in Mexico.[27]

Acknowledging this multinational reality, the UK government adopted the stance in the 2002 Defence Industrial Policy that any firm adding significant value in the UK would be treated as 'British'.[28] That meant that firms including Thales, Finmeccanica, Lockheed Martin and General Dynamics could be defined as UK national entities, allowing them easier access to the British market and integrating them into the British national defence effort.

Summing up, the supply-side actors in the CSO market have a strong interest in spreading the geographical reach of their commercial operations to offer more products and services to a broadened customer base, and to improve the foundation of their long-term revenue. But this commercial strategy is not without tensions. The complex ownership structures, opaque decision-making procedures and the relevance of CSO markets as part of a wider integrated security and defence business model, combine to generate a challenging environment for the public regulation and control of the private sector. Furthermore, there are the key strategic issues to consider of accountability of private market actors and the enduring sustainability of the CSO market. From a practical point of view, defence OEMs that present themselves as having several 'home' markets may have to address the question of which services they would offer to a 'home' country that wants help with launching a military operation, either at home or overseas.

Interactions Among CSO Stakeholders

The interaction among the forces of demand and supply in the CSO market takes place against a multi-layered market structure and a highly complex, interconnected web of public and private market actors. Any assessment of dynamics in the CSO market needs to take into account that these stakeholders view their professional environments through their interpretation of their surroundings and their own position.

Consequently, there is no consistent strategic CSO plan to follow for either public or private stakeholders, and neither will there be. Instead, multiple actor-specific perceptions in the market shape both the interactions between stakeholders and the future dynamics of the market. Accordingly, the CSO market, as with other commercial markets, seems to be characterised by emergent strategies that originate from the public and private market actors' efforts to constantly adapt to their professional world and to reposition themselves in the market.

Based on the assessment of market structure and the nature of public and private market actors, the next chapter examines the key drivers of future CSO market dynamics.

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IV. Key Drivers of Future CSO Market Dynamics

The future development of the CSO market is rooted in the socio-political, economic and operational context of defence, including, in particular, a political preference to outsource non-core elements of defence; societal constraints on the use of the military; a reduction and re-organisation of defence budgets; and a specific operational requirement profile.

Mediated by the stakeholders of societal explanations of defence – politicians, armed forces personnel, industrialists, employees in the defence industry, the media, academics, taxpayers and citizens – these four combine to generate five key drivers of CSO market dynamics; namely:

- The inherent dependence of the military effort on CSO
- The persistent need to advance CSO skills on the demand and supply side
- The increasing multinational integration and co-ordination of CSO policy
- The scope and character of future British operations overseas
- The future corporate focus on CSO services.

British Military Dependence on CSO
The British military effort is dependent on CSO because of the introduction of a 'core competency model' in the defence sector; the political and societal demand for a light military footprint on operations; and the operational need for specialist technological capabilities and niche skills, which the armed forces struggle to generate in the time and with the resources available.

The core competency model in the defence sector aims to outsource non-core military tasks to the private sector,[1] to allow the military to focus on its key skills and missions and re-invest the resources released into operational enhancements;[2] a point which is captured well by Joint Warfare Publication 4-05 (JWP 4-05), which states that 'The aim of CONDO is to free military personnel for employment where their military skills are most needed'.[3] This rationale also serves as the primary conceptual foundation of the markets for people support and protection/guarding, as formulated by the JSP 567 in its introduction on the use of CSO:[4]

> The use and importance of CSO have increased over time and CSO is an enduring element of today's operations. This reliance will increase in the future as the Defence Industrial Strategy has identified the need for the MOD and industry to think more innovatively about the allocation of roles and responsibilities, and to make best use of the MOD's and industry's comparative advantages in delivering and supporting military capability.

Although it has been argued that the transaction costs of outsourcing may offset some of the predicted efficiency savings,[5] the model is attractive to the policy-maker, the military planner and the industrialist for two main reasons.

First, it rationalises the gaps in the support force structure which emerged during the professionalisation and resultant reorganisation of the armed forces, when preference was given to combat capabilities. Second, if implemented successfully, it appears outsourcing non-essential tasks could generate a significant added capability along with other fiscal, industrial and political benefits.

Indeed, this outsourcing of parts of the military effort has corresponded with public opinion trends in the UK on the use of the military instrument. A recent YouGov survey showed that public support for overseas deployment of the armed forces appears to be relatively low:[6] only 10 per cent thought international crisis management should be a focus of UK foreign policy. Also, 33 per cent of those surveyed favoured an immediate withdrawal of British troops from Afghanistan, while a further 48 per cent supported a gradual withdrawal between 2011 and the end of 2014. Furthermore, 48 per cent would oppose military action against Iran to ensure it does not acquire nuclear weapons; only 32 percent would support such action if it were necessary.

Employing contractors – especially locals and third-country nationals – to conduct non-core military tasks allows policy-makers and military planners to meet the strategic and operational demand for effective and sustainable armed forces while responding to public concern, by maintaining a light military footprint on operations. Commenting on the relationship between US contractor fatalities and the public's casualty sensitivity, Steven Schooner and Collin Swan argue:[7]

> The military is populated by a 'blended workforce' that integrates soldiers with private-sector contractor employees ... in every conceivable aspect of the mission abroad. Not surprisingly, one result of this integration is that contractors are dying alongside – or in the place of – soldiers at unprecedented and (arguably) alarming rates. For the most part, this 'substitution' has taken place outside of the cognizance of the public and, potentially, Congress.

Of course, it should be noted that public reluctance towards the use of military force overseas may also have the opposite effect and significantly limit the growth potential of the CSO markets, as the report will assess in more detail below, should it translate into fewer and smaller operations in the future.

Finally, the dependence of the UK defence effort on CSO is driven by the specific operational requirements of twenty-first-century warfare. The introduction of new types of equipment onto the battlefield, especially at a time of rapid technological change, has increased the demand for contractors who can provide the required and rapidly evolving skills and capabilities to repair, maintain and even sometimes operate this new high-tech equipment.[8] The MoD is not alone in acknowledging that 'military personnel do not possess all the specialised skills required to maintain an increasing amount of technologically advanced equipment'.[9] The Netherlands, for example, has also used QinetiQ to operate and support a UAV system in Afghanistan.[10] Furthermore, sometimes the small amounts of kit procured through Urgent Operational Requirements (UOR) make it difficult to develop career lines in the armed forces for its support, inevitably creating a larger support role for the manufacturer.[11] Therefore, the market power of the suppliers is especially high in equipment support.

In essence, the UK will require CSO to support its military efforts in almost any future sustained operation, with a particular emphasis on equipment and people support. While the actual demand will vary according to the nature and duration of the operation, the following statement by former US Under Secretary of Defence for Acquisition, Technology and Logistics Ashton B Carter therefore also applies to the UK:[12]

> We're simply not going to go to war without contractors. We have to build that into what we call readiness, what we call training, what we call leadership, and what we call war planning.

Advancing CSO Skills on the Demand and Supply Side

The UK's CSO experience in Iraq and Afghanistan, although positive overall, suggests that both public and private market actors must continue to improve their CSO skills in order to redress shortfalls in the CSO market, primarily in public contracting, management and oversight capability, and the companies' ability to provide high quality services when they are required. Public and private CSO stakeholders alike have not yet fully understood and accepted the specific commercial and operational challenges inherent to the three CSO sub-markets.

Currently, there are only a limited number of experienced acquisition personnel with an in-depth knowledge of the commercial base and potential requirements of these sub-markets available within the government and armed forces to manage the funds and workload involved in such significant CSO demands.[13] This gap can only be closed by developing a CSO-specific career path for armed forces staff as part of an improved institutional contracting capability.

The UK Defence Academy's College of Management and Technology offers only two CSO management courses for MoD staff working in Contract

Sponsor, In-theatre Sponsor or Contract Management roles: three hours, approximately, of online training and a one-day classroom course.[14] Given their short duration, the stated aim of these two courses – 'to provide defence logisticians with a deeper understanding of the particular management issues and risks associated with contractor support on operations' – seems, at the very least, to be quite ambitious.

Moreover, attempts to develop proper CSO management and oversight capabilities in the UK have mainly focused on departmental structures and processes, while the capacity of the government workforce to manage and oversee contractors in theatre has only been addressed peripherally. Consequently, the organisational gap in pre-deployment, deployment and post-deployment management and oversight often results in ad-hoc solutions and significantly limits the value of contractors to the military effort in all three CSO sub-markets.[15]

Nor has the US yet found a practicable solution to this problem: the Department of Defense's increasing preference for outsourcing the management of operational contract support services has shown that the transfer of such a central government function leads to actual conflicts of interest.[16] Therefore, to avoid such problems, the UK and US governments must develop a strategic approach towards sizing, hiring, training and paying for a workforce that can effectively contract, manage and oversee contractors before they deploy and when they are in theatre.

For companies, it is important to take into account the implications of the operational environment for the delivery of the service when bidding for a service contract. Providing a service in a potentially hostile environment – with high commercial and personal risk, and constantly changing operational requirements that are neither easy to define nor to fulfil – is a uniquely challenging task and companies offering a similar service in a non-hostile environment cannot necessarily be successful under such conditions.[17]

It seems fair to assume that some companies had to learn this aspect of the CSO reality the hard way.[18] Using information compiled under the US Defense Base Act (DBA) by the Department of Labor, Steven Schooner and Collin Swan conclude:[19]

> [M]ore than 2,300 contractors have been killed in Iraq and Afghanistan ... between 2001 and the first quarter of 2011. Another 51,000 contractors have been injured; more than 19,000 at least somewhat seriously ... contractor deaths now represent over 27 percent of U.S. fatalities since the beginning of these wars.

CSO companies need skilled, well-trained and equipped, mentally and physically prepared, and reasonably paid employees to provide high-quality services.[20] They also need realistic risk assessments, grounded in an in-depth understanding of the highly complex operating environment and a balanced perception of commercial, reputational and personal risks.

It is true that the ability of both public and private stakeholders to operate effectively in the CSO market has improved significantly in recent years. As examples, consider the implementation of CSO policy at the strategic level through JSP 567, Defence Standard 05-129 and DEFCON 697,[21] as well as the adaption of the LOGCAP concept from the US in the form of the CONLOG contract. However, in order to ensure the availability and affordability of high-quality CSO services that reflect actual operational requirements in the future, the identified shortfalls need to be addressed in both a coherent and timely manner.

A key question in this regard is how to contract support services for scenarios that are not part of today's defence planning assumptions. The scale and duration of operations in Iraq and Afghanistan, for example, were not covered by defence planning assumptions, demonstrating clearly that future contracts need the flexibility to adapt to such changes in operational requirements while balancing affordability for the government and commercial viability for companies.

Although the CONLOG contract is not tied to defence planning assumptions, unlike its US counterpart, it may not be an adequate support instrument for all future UK operations. The US LOGCAP contract offers the delivery of a full capability within short notice, at least in theory, due to the greater predictability of requirements within the defence planning assumptions; whereas the CONLOG contract is first and foremost an enabling contract that provides better access to capabilities through its embedded planning cell at PJHQ. As such, it is an easy commercial building block but does not necessarily facilitate instantly the full spectrum of required capabilities for all future scenarios.[22] JSP 567 addresses this challenge as follows:[23]

> The degree of certainty and predictability of the requirement should influence sourcing options. Predictable requirements are more easily articulated within contracts … Where there is a need for significant operational flexibility with respect to the required output, location and volume of service or if the requirement is expected to ebb and surge significantly, then a contractor's fixed costs and capacity to respond should be considered. In Theatre there may be limited opportunity to renegotiate contract requirements and the timeline for resolution of commercial issues may both be incompatible with the tempo of operational decision making. The need to respond flexibly to changing operational requirements may be one factor which favours an SR solution.

Co-ordinating and Integrating Multinational CSO Policy

The UK is not alone in relying on contractor support for its military operations overseas. Although most Western states are as reluctant as the UK to outsource military capability, many also face more or less similar socio-political and economic constraints on the use of armed forces abroad, and so have turned to contractors to support their defence efforts.[24] Of course, the actual degree of reliance differs and specific national regulations apply, especially in the sub-market for protection/guarding.

Germany, for example, has contracted various services for equipment and people support as well as protection/guarding for its military operations abroad, particularly in Afghanistan.[25] Many of Britain's other allies and partners in Europe, like France, Italy and the Netherlands, use contractors for similar tasks.

These developments in the CSO market at the national level correspond to an increasing integration of outsourced services in multinational operations. In Afghanistan, NATO's Maintenance and Supply Agency (NAMSA) has consolidated a significant number of national people support contracts. Individual countries still hire contractors to meet their specific needs; however, NAMSA can now also handle the tendering process and oversee contracts, thereby saving costs for its member states.[26] In an interview in June 2010, the then deputy chief of Staff Support at SHAPE, Major General Leonardo di Marco, explained:[27]

> [W]e also see a rise in multinational logistics complimentary to national logistics ... In terms of contractor support to NATO operations, the NATO Maintenance and Supply Agency (NAMSA) provides service integration for current and future NATO operations ... NAMSA is negotiating the fuel for KFOR at the moment and has arranged real life support and other services at NATO airports and other air bases in Afghanistan ... My personnel [*sic*] view is that logistic support to NATO operations will definitely benefit from multinational arrangements and multinational support solutions. This will allow all logisticians to deliver best value for money and avoid duplication of efforts.

As a further example of outsourced services in multinational institutions, consider a recent European Defence Agency (EDA) tender for a contract to provide logistical support, specifically the provision of fresh food and catering, to the EU Battlegroup should it be deployed.[28] On this occasion, the EDA was acting on behalf of the ministries of defence of Austria, the Czech Republic, Ireland and Germany, offering a contract with a maximum value of €228 million and a duration of twelve months, subject to renewal for a further twelve months thereafter.

An important question for the UK is how different it can be in its approach to CSO, given its integration into a multinational framework on the strategic as well as the operational level.[29] It seems fair to assume that while there is enough scope for the UK to include specifically national elements in its CSO approach, it must also proactively adapt to the increasing multinational integration and co-ordination of CSO policy, not least to ensure the necessary interoperability with its allies and partners.

The US approach to CSO is also of special importance to the UK, given the close relationship between the two, both strategically and militarily. Reflecting its extensive experience with contractors in Iraq and Afghanistan, the US has initiated far-reaching reform in this area, which has become a high-profile issue for the US government, Congress and the Department of Defense, as well as for industrial and wider societal actors.[30] Against the background of an estimated $31 billion to $60 billion lost to contract waste and fraud in America's contingency operations, the Commission on Wartime Contracting in Iraq and Afghanistan states in its final report:[31]

> The need for reform is urgent … The United States will not be able to conduct large or sustained contingency operations without heavy contractor support. Avoiding a repetition of the waste, fraud, and abuse seen in Iraq and Afghanistan requires either a great increase in agencies' ability to perform core tasks and to manage contracts effectively, or a disciplined reconsideration of plans and commitments that would require intense use of contractors. Failure by Congress and the Executive Branch to heed a decade's lessons on contingency contracting from Iraq and Afghanistan will not avert new contingencies. It will only ensure that additional billions of dollars of waste will occur and that U.S. objectives and standing in the world will suffer. Worse still, lives will be lost because of waste and mismanagement. The nation's security demands nothing less than sweeping reform.

A core element of this reform agenda is the recognition at the highest political and military levels that the 'preparedness for contingency contracting is as much a national-security priority as procuring weapons systems'.[32]

Therefore, the report argues further, it is necessary to provide or reallocate adequate resources to contingency contracting, establishing a senior federal position responsible for overall strategic direction, mission alignments and inter-agency co-ordination for contingency operations to provide a whole-of-government approach; develop sufficiently staffed and deployable cadres for acquisition management and contractor oversight; include clear contracting guidance in planning, training, exercises, doctrine and policy documents; elevate and expand the authority of officials responsible for contingency contracting; improve contractor performance-data recording and use; and strengthen enforcement tools.

The UK should consider if these elements of reform – of course, adjusted to the specific UK and European context – could also improve its own approach to CSO.

The Impact of Future British Operations on CSO

The scope and character of future British operations overseas will heavily determine the long-term commercial and operational sustainability of the CSO market. With British operations in Iraq over and the beginning of the drawdown in Afghanistan – which may itself generate some CSO business, as the logistical task of re-deploying equipment and personnel to the UK will require contractor support – coupled with a widespread reluctance among the British public, political establishment and military command to engage in similar operations, MoD demand for CSO will probably decline for some time.

Although military operations will undoubtedly take place in the future, they are likely to resemble the relatively short, low-cost air campaign in Libya,[33] which has shown that the CSO business opportunities generated by these limited operations would be modest. Since there was no large land force deployed in Libya and NATO countries could provide extensive host-nation support, there was no demand for people support and protection/guarding services, and only very limited demand for in-theatre equipment support.

The key consideration for the British government and industry here is ensuring the sustainability and commercial viability of the CSO market. Faced with an undefined period marked by fewer business opportunities, companies may restructure their business models, exploring other sectors where possible, or simply exit the market through liquidation. With its military capabilities so dependent on CSO, the British government could find its options seriously limited should a situation arise that requires a large-scale operation at relatively short notice.

Moreover, the British experience of operations in Iraq has shown that a rapid increase in outsourced capabilities, although possible in general due to the inherent flexibility in the private sector, may come at the expense of the quality, accountability and sustainability of those services and, accordingly, the British operational capability to act. Planning for a potential industrial surge should therefore give special attention to long-lead items where only a few suppliers are available and to critical labour categories; it should recognise that companies do not usually have a 'standing army' of highly qualified employees that can readily be deployed at short notice.[34]

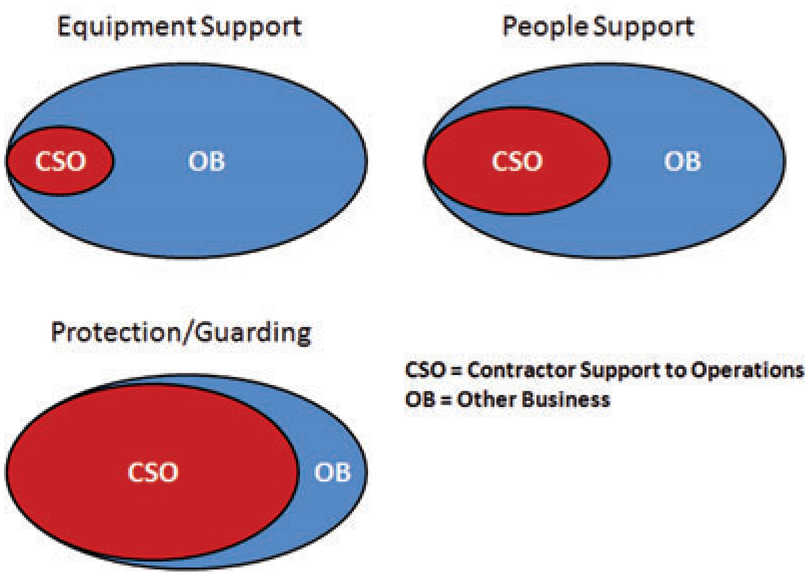
That said, a downturn in the CSO market could also begin a process of rationalisation on the supply side with benefits for both suppliers and customers, including price reductions, improved quality, increased consolidation of the supply side and, ultimately, greater long-term sustainability of the market. Therefore, the government needs to co-operate closely with industry to sustain critical CSO capabilities in both the private and public sector, which may also suffer as a result of reduced demand for CSO services. The government needs to acknowledge that sustaining an adequate defence industrial base includes paying attention to the service sector as a whole, and to the CSO sector in particular.

In summary, business opportunities in the CSO market may be fewer in the future but if a critical mass can be sustained and there is a rationalisation of the supply side, the overall quality, availability, sustainability and commercial viability of these services may improve considerably. Of course, such an improved, but probably smaller, supply base may also mean higher prices,[35] rendering CSO less affordable in absolute terms. In the meantime, the commercial risks for companies may increase, particularly for those whose business is reliant entirely upon this market.

The Future Corporate Focus on CSO Services

Finally, the future corporate focus on CSO services will shape the interaction between the demand and supply side in the market. However, it should be noted that the comparative importance of a company's CSO activity to its overall business, and accordingly the company's ability to sustain and extend core CSO skills, differs significantly between the CSO sub-markets (see Figure 3).

Figure 3: The relative importance of CSO to companies operating in each sub-market.



Source: Heidenkamp, 2012.

Companies in the equipment support sub-market primarily regard CSO as an integral part of through-life support for the customer, essential to the operational availability and sustainability of equipment, and therefore a core component of a product's portfolio. By providing such support and maintenance services for equipment in peacetime, when it is used by the armed forces for training, and post-conflict when it is in reserve, these companies are guaranteeing business viability in the future. Such activity should be sufficient to sustain core CSO capabilities in the equipment support market in the long term.

In the people support sub-market, companies usually provide CSO services as an extension of, or in addition to, those already offered in their primary, domestic markets. With military operations being reduced in scale and duration, these companies will face the challenge of re-integrating CSO activity into their core business where possible and realigning the remainder according to market realities. Given this, Andrew Pringle, the president of KBR's International Government Defence and Support Services (IGDSS), stated recently:[36]

> We are focused on growing IGDSS' business through diversification of our client base, including helping the U.K. Ministry of Defence meet its next round of challenges as the operational tempo slows ... We have also stayed in Iraq, where we support the oil and gas companies in the Rumaila oil fields, and see the U.K. government's transformation program across all departments as presenting real opportunities for us as more and more services are outsourced, and are also growing our government and defense services business in Australia.

As their market options are not limited to CSO, the commercial survival of people-support companies will likely not be at stake. In this sense, Trevor Taylor points out 'that the kind of people-support work being undertaken for the military by companies like KBR is also being replicated to some degree in sectors like mining exploration in difficult and remote areas. There is sufficient activity of that sort to allow those who secure contracts to keep their skills alive.'[37] Moreover, as many companies also provide services to the armed forces at home, their contracts may require them to sustain a certain level of CSO capability for overseas operations in case it is needed in the future.

Companies providing services in the protection/guarding sub-market potentially face the biggest challenges in the short to medium term, as their business model is strongly dependent on CSO business and most lack a strong foundation in the domestic market. Although some of the companies also provide protection/guarding services to domestic customers, transferring major parts of their CSO business will be very difficult given the less-threatening domestic environment and vastly smaller demand.

However, these companies should have considerable agility because they tend to employ only a few staff on long-term contracts and do not need to cover many capital investments over a long period. They should be able to downsize quickly and some may be able to keep their company's key skill sets alive, at least in an embryonic form. Alternatively, companies providing services where the use of force is a central consideration may well be tempted to seek non-Western customers to maintain turnover and profit levels.[38]

Depending on who these customers are and what specific type of protection/guarding service is required by them, there may be significant potential for conflict with UK national interests,[39] especially when the lines between defensive and offensive action blur on the ground. An expansion of the customer base in this sub-market should therefore be accompanied by more effective and transparent regulation, oversight, controls and standards.[40]

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39. Equipment support services may also be problematic in this regard, mainly because of their clear relevance for the sustainability of an operation and their potential to trigger technology transfers. People support services, although usually not at the forefront of public perception, may also come under scrutiny as they can be an essential component of operational logistics in support of an operation that is in opposition to UK national interests.

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from a national security perspective, whereas others are subject to specific business conduct constraints and procedures. See Ministry of Defence, *Equipment, Support, and Technology for UK Defence and Security: A Consultation Paper*, Cm 7989 (London: The Stationery Office, December 2010), pp. 30–34; Ministry of Defence, *Defence Industrial Strategy: Defence White Paper*, Cm 6697 (London: The Stationery Office, December 2005), pp. 46–47; Saferworld, 'Responsible Export Controls for UK Security and Conflict Prevention', March 2011, p. 3; William Dill and Darren Graham, 'A Pathway to a Private Security Market Infrastructure', *RUSI Newsbrief* (Vol. 31, No. 5, 2011).

V. Implications for Public and Private Market Actors

This report has assessed the fundamentals of the future CSO market dynamics in the UK – the structure, actors and key drivers. The report has identified a multi-layered interaction between the public and private CSO market actors that is driven by the inherent dependence of the UK on CSO when conducting military operations abroad; the lack of a coherent strategic approach to CSO on the demand side; the emergence of a multinational CSO policy, which responds to the rise in multinational logistics and complements national logistics considerations; the uncertain level of demand for CSO during future UK operations; and the commercial pressures for companies to sustain and advance their viability in the CSO market at acceptable financial and reputational risks.

The report has shown that there are several tensions between the drivers of the market that affect the availability, quality, sustainability, affordability and commercial viability of CSO services. Public and private CSO stakeholders must resolve or exploit these tensions if the UK is to ensure national security and its influence on the global stage in the long term. Therefore, both public and private CSO stakeholders will have to take decisive action.

The public sector has to grow organic capacities at the strategic and operational level to improve its CSO contracting, management and oversight capabilities and to sustain the availability of such solutions in the long term. In turn, this could, for example, help to promote greater market competition for equipment support services; improve single-source contracting where applicable; implement more effective controls in the market for protection/guarding; and create sustainable business frameworks, in which companies can provide the CSO services required by the customer while generating reasonable profits. These tasks are neither easy to fulfil nor can they be implemented without committing adequate financial, human and political resources.

The private sector has to secure the long-term sustainability and profitability of its CSO business models, which, particularly in the equipment and people support sub-markets, must be considered as part of wider service sectors. Ultimately, these companies have to deliver high-quality products and services which can be sustained in theatre at acceptable costs.

The private sector should accept that, due to its nature, the demand side will always be beset by severe tensions in its CSO decision-making and management procedures, and so it should proactively develop its CSO business model in close co-operation with its public counterpart. To this end, it is in the interests of industry to constantly pressure the public sector to set up the sustainable business framework described above and to insist on financially sensible and actually deliverable contracts. Companies should not just 'fly the flag' when government requires their support but should advocate their justified commercial interests.[1]

CSO could generate both significant added value to the UK's defence effort and the commercial success of contractor services if the stakeholders understand and accept the specific nature, capabilities, pressures and limitations of the public and private sectors. CSO is integral to sustaining the UK's defence effort and therefore it is important that public and private stakeholders work together to develop a more coherent approach to CSO that is able to better balance existing tensions in the market and more effectively handle commercial and operational risks.

The 'Total Support Force' (TSF) could be an adequate framework for such an approach. The TSF intends to provide 'for a fully integrated and sustainable military (Regular and Reserve), Civil Service, and contractor support force, which includes the use of contractors in the Sponsored Reserve role'.[2] However, there are 'significant hurdles to overcome in implementing the TSF concept: rejection of the change due to the lack of ownership of the benefits among those most affected; mounting opposition during the time lag to introduce the supporting tools for a TSF business case ... In particular, this requires a significant culture change in the ... management to transferring capability, functions and units that are the backbone of their professional life.'[3] It remains to be seen if policy-makers, the armed forces and industry can effectively work together to overcome these hurdles.[4]

More fundamentally, this report's evaluation of future CSO market dynamics has shown that the UK may well require a defence industrial policy which acknowledges the service sector as a core component of the defence industrial base and is capable of addressing the sector's specific challenges – not only on overseas operations, but also domestically. This policy would also have to clarify more precisely industry's role in the defence and security sector – a task that appears to be a cultural challenge first and foremost. In addition, it may be necessary to adjust communication around the importance of the defence industrial sector to the UK economy to redress popular perception: the government often refers to defence industry supporting 300,000 jobs in the UK,[5] but this figure does not take into account the service companies employees who support British military operations both at home and abroad.

Although the report has identified significant problems in the CSO market both on the demand and supply side, it is also important to stress that its overall track record, with all of its shortfalls, is not fundamentally bad. Given the substantial experience of CSO gained in recent operations, the continued advocacy of contractor services in defence by both the UK government and the British armed forces speaks volumes. Apart from the inherent dependence of the British military effort on CSO, it also reflects the high reliability and quality of services provided by most companies to the British armed forces abroad.

Furthermore, the 'power of the contract' should not be underestimated. Even if CSO may not always offer an absolutely solid and fully convincing business case in the future, companies with an established footprint in the market may tend to sustain their activities for more fundamental reasons. Especially in the equipment and people support sub-markets, companies regard their CSO activities as an extension of existing business that contributes to the companies' reputation as reliable partners for the government. Therefore, it would likely take a severe deterioration in the CSO business environment to fundamentally change this attitude.[6]

In the end, the dynamics of the CSO market illustrate the interdependence between public policies – industrial, defence industrial, security and defence – and economic and corporate performance, as well as the sustainability of the UK's defence effort and Britain's role in the world. Public and private actors have to respond to the complexity of their professional environments adequately and in time. It appears that the real test for CSO stakeholders and, more fundamentally, the sustainment of the UK's defence effort, is yet to come.

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