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OUTSOURCING INCOMPETENCE: AN ESSAY IN HONOR OF PAUL VERKUIL

Arthur J. Jacobson∗

I first encountered Paul Verkuil in the late 1970s, when I started teaching administrative law. I came across an article in the University of Chicago Law Review.1 It was a study of procedures for informal adjudication by administrative agencies. Its author was a professor teaching law at North Carolina. I remember it vividly. (About how many articles you read over thirty years ago can that be said?) It was everything I wanted my own work to be: passionate about the subject yet dispassionate about the results, simple yet unobvious, beautiful yet true. I remember wondering, “Who is this guy? He’s amazing!” He was Paul.

The next time I encountered him was close to twenty years later, when he became dean at the Benjamin N. Cardozo School of Law. Administrative law, it turned out, did not last. Paul did. It was only after he stepped down from the deanship to become a beloved colleague that I learned where that article came from. I was organizing a symposium on the legal theory of Baruch Spinoza. Paul told me that his grandfather, Leendert, was a devoted reader of Spinoza. He said that he had not so much studied Spinoza as he had inherited him from Leendert. He even wrote a moving recollection of that inheritance for my symposium.2 It was then that I understood who “this guy” really was. That passionate dispassion, unobvious simplicity, and beautiful truth of the article I had read in the late 1970s was the voice of Spinoza, refined and personified in Paul’s grandfather, and transmitted by him to Paul. What I was reading then in that article about procedures for informal adjudication was Spinoza, specifically Spinoza doing administrative law.

∗ Max Freund Professor of Litigation & Advocacy, Benjamin N. Cardozo School of Law, Yeshiva University. I would like to thank my assistant, Captain Erik Wilson of the United States Marine Corps, without whom this Essay could not have been written. I would also like to thank Professor Eric Jensen for his discussions with Captain Wilson.

Nowhere are Paul’s Spinozist virtues more prominently on display than in his recent monograph, *Outsourcing Sovereignty*. In it, Paul unfurls a tight and elegant argument against the pathologies of the privatization movement in the federal government. He dates the privatization movement to the Iran-Contra affair, which first came to light in 1986. The significance of Iran-Contra, Paul suggests, is that certain members of the Reagan Administration decided to privatize foreign policy once Congress refused to finance the contras’ guerilla campaign against the Nicaraguan government. But perhaps the origins of the privatization movement can be traced back even further than Iran-Contra, to the deregulation that began during the Carter Administration—a steady contraction of the reach of government that began with deregulation and continued with privatization.

Whatever the source of privatization, its consequences, Paul argues, have been clear. Government has overreached in outsourcing government functions. It has outsourced not only government functions that are amenable to outsourcing, but also those that are not: the “inherent” government functions. Roughly speaking, those are the functions that require the exercise of judgment by public officials acting as agents of the sovereign. The sovereign, Paul argues, is “We the People,” made sovereign by the Constitution of the United States. Functions amenable to outsourcing, in contrast, are those that do not require the exercise of sovereign judgment; they are functions that may be well-defined by contract and closely monitored by “Officers of the United States.” The key to the distinction between government functions that are inherent and those that are not, in Paul’s vision, is accountability: the accountability of an agent to his principal, of “Officers of the United States” to “We the People.” Government is thus accountable only when its officers exercise the judgment entrusted to them over inherent government functions, and having exercised that judgment, only when they ensure its implementation either through a bureaucracy subject to their command and control or through adequately defined and monitored contracts with private sources. Government has failed to be accountable over the past generation in both possible ways—impermissibly farming out the exercise of judgment, while failing to implement such judgments as have been properly made.

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4 One could go back even further. Robert Timberg argues that the die for Iran-Contra was cast towards the end of the Vietnam War, when the men who were to become the authors of Iran-Contra were officers serving in Vietnam. ROBERT TIMBERG, THE NIGHTINGALE’S SONG 14 (2006). The lesson they learned from Vietnam, Timberg documents, was the betrayal of a military effort by a feckless political class. *Id.* at 15. They were not going to let that happen again.
The unaccountability of government, in turn, has its own pernicious consequence concerning the competency of government. Officials who fail to exercise judgment over inherent government functions—or who neglect to inscribe that judgment either in adequately staffed and motivated bureaucracies or in suitably defined and monitored contracts—invite incompetence of many kinds, all of which have marked the era of privatization and all of which Paul documents. If officials will not do their jobs—if they will not exercise judgment over inherent government functions, or will not staff and motivate a bureaucracy, or will not define and monitor contracts with private sources—then either the job will not get done or it will get done badly. That is the lesson of Paul’s study.

I want to take that lesson one step further. I want to place the incompetence that is the product of privatization in a larger context. I want to argue that the incompetence produced by privatization is inseparable from a broader crisis of state competence. I want to say why there is a broader crisis, and why that crisis is unavoidable under present conditions.

The poster boy for Paul’s argument about privatization must surely be Blackwater, one of the private security firms that, at the height of the Iraq war, provided “battlefield personnel for escorting convoys, protecting civilian leadership (e.g., Paul Bremer), and even interrogating prisoners.”

Paul’s account of Blackwater focuses on the pathologies of privatization:

In addition to conducting interrogations, assignments such as securing convoys or protecting Paul Bremer or even the Secretary of State often involve indirect or even direct combat confrontations. Indeed, sometimes contractors cause military actions even if they are not assigned to carry them out. The four Blackwater employees who were dismembered and mutilated in Fallujah, where they ended up while guarding a convoy, is a grim reminder of how the military must react to contractor actions. The Marines had to secure that city after that gruesome event, which was not in their plans beforehand.

Paul’s conclusion about the Fallujah incident is ineluctable. The Department of Defense, it appears, outsourced to Blackwater a task that it regarded as amenable to outsourcing, rather than as an inherent government function. Were the Department of Defense to offer a justification of this decision, they would argue that providing security to a supply convoy is akin to an ordinary civilian security operation—like night watchmen at a construction site or armed guards accompanying an armored car—and is thus distinguishable from combat, which, as most today would probably agree, is an inherent government function. But

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5 VERKUIL, supra note 3, at 27.
6 Id. at 28 (footnotes omitted).
the reality of a theater in combat does not permit so fine a distinction to be drawn. The Blackwater employees had necessarily to engage in combat, and their defeat drew the Marines into a combat operation they had neither desired nor planned. Contracting with Blackwater to provide security for convoys thus wound up diverting the United States military from operations they had in fact planned, and calling into question the competence of a military that could so unwittingly be the cause of its own distraction.

Paul’s Blackwater story is bad enough. The real story is worse. I asked Erik Wilson, a captain in the United States Marine Corps and a first-year law student at Cardozo, to look into the Fallujah incident a little more closely. Here is what he found.

The U.S. Army did not hire Blackwater directly. The prime contract, part of the Logistics Civilian Augmentation Program (LOGCAP), was between the Army and Halliburton. It was a contract to supply Camp Ridgeway, an Army base near Fallujah. (See Figure 1.)

Figure 1. Subcontracts for Supplying Camp Ridgeway

Halliburton then subcontracted the supply contract to KBR, and KBR subcontracted it to ESS. It was ESS that hired Blackwater to provide security for the convoys to Camp Ridgeway. Four subcontracts connect, or separate, Blackwater from the ultimate recipient of its
services. That looks like an awfully long chain of subcontracts. But things were not so simple.

Let’s start with the top of the chain. It was actually KBR’s predecessor, Brown & Root, and not Halliburton, that had the first LOGCAP contract with the Army. This was back in the 1990s, at the beginning of the LOGCAP program. In 2002, Halliburton created KBR (merging two of its subsidiaries, Brown & Root and M.W. Kellogg), and replaced the former Brown & Root as the prime contractor. Halliburton was thus the prime contractor at the beginning of the Iraq war in 2003. The LOGCAP contract Halliburton signed at that point, known as LOGCAP III, was the second renegotiation of the initial LOGCAP contract between the Army and Brown & Root. Halliburton’s role under LOGCAP III was only to guarantee KBR’s services, and the Army and other federal auditing agencies dealt directly with KBR, not with Halliburton. Halliburton was involved in LOGCAP III only because it owned KBR. Thus, after Halliburton divested itself of KBR in 2007, KBR once again became the prime contractor in the LOGCAP IV contract, which is just now coming into effect.

Now let us consider the bottom of the chain. ESS did not hire Blackwater directly. It hired Blackwater through a proxy company, Regency Hotel and Hospital Company of Kuwait. What happened was this: Regency and Blackwater had submitted a joint proposal to replace ESS’s existing private security contractor, Control Risks Group. Once Regency/Blackwater won the contract, they renegotiated it to make Regency ESS’s subcontractor and, in turn, make Blackwater Regency’s subcontractor. Apparently Blackwater wanted this arrangement so it could get exclusive credit for the successful security operations.

The presence of Regency in the chain is important because a dispute erupted between Blackwater and Regency about the armoring of the vehicles to be used in protecting the convoys. According to Captain Wilson, Blackwater used its subcontractor status to “blackmail” Regency, saying that Regency now had to provide weapons, armor, and

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7 Dana Hedgpeth, KBR Prepared to Sever Last Ties to Halliburton with Stock Swap, WASH. POST, Mar. 29, 2007, at D01.
8 Each LOGCAP contract has a maximum ten-year lifespan before it requires renegotiation.
10 See Hedgpeth, supra note 7.
other supplies, and that Blackwater would not supply them. The apparent aim of this strategy was to get Regency either to pay for Blackwater’s supplies or default on their contract, which Blackwater would try to take over at an increased profit once Regency was no longer in the way. Captain Wilson believes that Blackwater probably could not have gotten the security contract on its own and that it teamed with Regency for credibility, then tried to cut Regency out.

Partially as a result of this dispute between Regency and Blackwater over equipment funding, the Blackwater team was extremely underequipped and underprepared for the March 31, 2004, mission in which four Blackwater employees died.

I want to pause here in telling the story to make a comment. Outsourcing government tasks to a firm in the private economy subjects those tasks to the push and pull of the economy. I do not have the illusion, and neither does Paul, that elements of the bureaucracy are without their own motivations and distortions, but when you sign up with the private economy, you agree to participate in the private economy’s motivations and distortions. Let’s be blunt. There was a dispute between Regency and Blackwater over who would pay to armor the security for the convoys. That dispute led to the under-equipment and under-preparation of the security team on which the four Blackwater employees died. Their deaths led the military to launch an invasion of Fallujah. So here it is: A contract dispute led to a major development in a major war of the United States—and that is Paul’s point.

Of course, similar disputes can and do produce similarly horrible results in the language of the bureaucracy, instead of the language of the market. There is no doubt that the bureaucracy has its own version of contract disputes and its own version of letting hell to pay. One cannot say, “oh, had the market not been involved, things would have turned out just fine: The four men on the supply mission would not have been killed and the United States would not have had to invade Fallujah.” That is not Paul’s argument, nor is it mine. Nevertheless, the motive driving the decision-makers in the Blackwater incident was profit, rather than some other motive that we might attribute to the bureaucracy. While profit is OK as a motive for screwing up in Fallujah, that is not the question. The question is whether profit should be the guiding principal in directing our actions on a matter of state—on a matter of national interest. If it were not economically efficient for the United States to survive, would Richard Posner support it?

Now here is where the story gets particularly bad. Captain Wilson found that the LOGCAP contract between Halliburton and the Army—

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12 See id.
LOGCAP III—provided that security for the convoys would be the responsibility of the Army. The subcontract between Halliburton and KBR contained the same provision. The LOGCAP III contract explicitly prohibited the use of weapons by any agents of the prime contractor or any of its subcontractors, and also had several clauses referencing two orders from United States Central Command (USCENTCOM) and two orders from the Coalition Provisional Authority (CPA) that similarly restricted the use of weapons by civilian contractors.  \(^{13}\)

In spite of these provisions and orders, ESS hired Blackwater to run security for them; KBR was aware of that fact, and it is unknown if Halliburton or the Army were aware. Captain Wilson is of the opinion that if Halliburton or the Army were not aware, then it would have been due to deliberate ignorance.  \(^{14}\) But it was not just ESS that was illegally hiring private security contractors; KBR itself hired at least three private security firms, and even privately armed some of its own employees.  \(^{15}\) Blackwater agreed to provide ESS with a thirty-four man security team that would establish a command center, have risk management expertise, and provide security personnel to protect installations and convoys. In violation of this contract, the Blackwater team whose fate we are discussing was short of manpower and equipment—communications equipment, ammunition, weapons, body armor and armored vehicles. The convoy had not been risk-assessed, as was required by the contract between Blackwater and ESS. This lack of risk-assessment resulted in Blackwater guiding the convoy through Fallujah, rather than the safer roads around it. Blackwater also breached the contract by failing to provide six personnel to ride along with the convoy, sending only four instead. They also failed to provide rear gunners for the security vehicles and were short on automatic weapons to protect the vehicles.

The actual convoy ended up in the middle of Fallujah because of the lack of equipment and planning. The convoy’s destination was Camp Ridgeway. It was supposed to arrive on March 30, 2004. Because of the lack of planning, the convoy got lost and arrived at

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\(^{15}\) KBR Complaint, supra note 13, at 6-8. The Department of Justice is currently suing KBR for its failure and the failure of its subcontractors to abide by LOGCAP provisions that forbade the use of private security forces. Id.
Camp Fallujah, a Marine Corps Base. Once at Camp Fallujah, the Blackwater contractors located some KBR employees (since there were no ESS employees there), who told them how to get to Camp Ridgeway and warned them against going through Fallujah proper. The convoy departed Camp Fallujah, but was promptly sent back by a U.S. Marine Corps checkpoint, for reasons unknown. They spent the night at Camp Fallujah and departed for Camp Ridgeway in the morning. The convoy deliberately circumvented the Marine Corps checkpoint, instead going through an Iraqi Civil Defense Corps (ICDC) checkpoint. The trucks were ambushed and the Blackwater operators were killed. There are conflicting reports as to whether the ICDC soldiers actually escorted the convoy into Fallujah and facilitated the ambush.16

The deaths of the Blackwater contractors created a national and international outcry. There was an immediate call to invade and pacify the city of Fallujah. The Marines, who controlled the ground forces around Fallujah under the ultimate supervision of the Army, requested that Fallujah not be invaded, saying that invasion would be counterproductive to the progress the Marines were making there. Local residents of Fallujah had voluntarily returned the bodies of the Blackwater contractors, and the Marines were confident they would have the perpetrators in custody within forty-eight hours. Marine Corps Generals Mattis and Conway warned that attacking Fallujah at that time and in the manner suggested would cause the exact explosion in insurgency that in fact occurred after the invasion of Fallujah. Their supervisor, Army General Ricardo Sanchez, nonetheless recommended the siege of Fallujah to the Secretary of Defense, who ordered the invasion to take place almost immediately.17

I tell this story at length to alert all of us, myself included, to the perils of remitting important matters of state either to the bureaucracy or to contract. Both failed in Fallujah. How could the Army not know that Blackwater was running security for the convoys going to Camp Ridgeway? There is an answer to that question and it is not a happy one. Captain Wilson found that there was a severe lack of Army oversight of the LOGCAP contract.18 The LOGCAP contract is an Army contract, so supervision began with the Army. But responsibility for supervision continued up through the ranks of the Department of Defense, ultimately implicating at least half a dozen agencies within the Department, with overlapping responsibilities for ensuring the proper

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16 PRIVATE MILITARY CONTRACTORS, supra note 11.
execution of contract provisions and appropriate documentation of contractor expenses. One would think that having all these agencies on the job would guarantee accountability. But each of the agencies was seriously understaffed. Today, for example, the Department of Defense has approximately 600 auditor vacancies. There has been a direct correlation between the increase in contractor use and the decrease in federal regulators of their contracts. Even while the battle for Fallujah raged on due to the deaths of the Blackwater employees, the Department of Defense cut its contractor auditing staff by fifty percent. The senior supervisor for Army contracting at the time, a civilian federal employee named Charles M. Smith, had a staff of only two full-time contracting personnel and a part-time lawyer to oversee $5 billion worth of contracts.

So, did Fallujah teach us anything? Sadly not. The Army still does not track how many contractors are used to execute the LOGCAP contract, or how the subcontracts are specifically structured. Given this persistent failure of supervision, it is unsurprising that the Army either did not know that KBR and ESS were hiring security contractors, or simply failed to stop them. But the lack of supervision was actually much broader in scope.

A Department of Defense Inspector General (DOD-IG) report from 2008 found that the Army’s failure to supervise contracts like LOGCAP resulted in $7.8 billion worth of improperly documented payments. Of all the Army’s payments between 2001 and 2006, 73% failed to meet the Army’s own documentation standards. For commercial contractors like KBR, 99.5% of the payments lacked sufficient documentation. The 2008 DOD-IG report is especially useful because it includes two years of peacetime payments as well, indicating that the Army’s accountability problems pre-date the war. And if the Army cannot properly supervise its contracts in peacetime, there is essentially no hope in wartime.

These problems of supervision are the result of a failure to set clear regulatory guidelines, employ and train personnel, and hold violators accountable. Thus, only half of the Army’s contracting specialists—and only 2% of those on active duty—are adequately trained.

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20 See, e.g., id.
21 Safeguarding Taxpayer Dollars, supra note 9, at 2.
22 See, e.g., INTERNAL CONTROLS, supra note 18.
23 Id.
24 Id. at 4.
25 Id.
Accountability controls over contractor payments have never been finalized, there is still no formal training on LOGCAP contracts, and most of the personnel dealing with LOGCAP contractors have no LOGCAP experience at all.\(^\text{26}\) In theory, if the Army had had enough personnel to keep track of activities under the LOGCAP contract, it would have been possible to hold Blackwater and other subcontractors, running all the way up the chain to Halliburton, accountable for violating USCENTCOM and CPA orders and for breach of the LOGCAP contract. The Department of Justice is currently suing KBR for fraudulently passing along Blackwater’s security costs to the Army without separately identifying them as security costs.\(^\text{27}\) The same evidence supporting this civil claim would also establish a violation of the Major Fraud Act of 1988 (MFA),\(^\text{28}\) which makes it a felony for contractors or subcontractors to defraud the United States for amounts equal to or in excess of $1 million dollars (Blackwater’s original contract with Regency was for over $11 million\(^\text{29}\)). The Department of Justice has the power to prosecute civilian contractors and subcontractors providing support to the Department of Defense for felonies committed in foreign countries under the Military Extraterritorial Jurisdiction Act of 2000 (MEJA).\(^\text{30}\) KBR, a qualifying subcontractor, could therefore have been prosecuted under federal law for the MFA violation as if the crime had been committed in the United States.

However, lawsuits and criminal prosecutions offer only limited utility to theatre commanders: They are after-the-fact, take a long time, and have uncertain results. Moreover, prosecution under MEJA comes with its own distinct set of problems: The Department of Justice does not have a MEJA division, and MEJA cases are referred back to local United States Attorneys’ Offices, which are already heavily backlogged. Of far greater utility are three summary powers the Army possesses that can remove offending contractors from the conflict area while deflecting the time- and resource-intensive process of litigation to federal court in the United States. One method would have been simply to prohibit access to Army bases by problematic contractors. This would quickly and effectively sever their ability to execute their contracts, and, most likely, their ability to stay in Iraq. According to Captain Wilson, Army commanders favor this method because it efficiently avoids the burden of litigation under conditions of armed

\(^{26}\) See, e.g., id.; DEFENSE LOGISTICAL SUPPORT CONTRACTS, supra note 19, at 11-15.
\(^{27}\) KBR Complaint, supra note 13.
\(^{30}\) 18 U.S.C. § 3261.
conflict and limited resources. The Army also had the power to exclude contractors from Iraq altogether. Finally, the Army could have canceled, or threatened to cancel, any portion of the LOGCAP contract “tainted” by Blackwater.

Of course, the Army declined to use any of its summary powers. Why was that? Even if no relevant Army personnel knew about Blackwater’s operations prior to the ambush, they certainly knew about the operations afterwards. But still, the Army took no decisive action to end Blackwater’s services or the use of private security contractors in violation of weapons regulations and the terms of the LOGCAP contract. Why not? The simplest answer is that the Army deemed these services necessary to the larger war effort—that it was simply unable or unwilling to fill the void that would have been left if Blackwater and other private security contractors like it were suddenly gone. Likewise, according to this rationale, if the Army had known about the violations of USCENTCOM and CPA orders, and of the LOGCAP contract up and down the chain of subcontractors, it still would have taken no action for the very same reason.

Consider the record. Every moment in this sorry tale is marked by one species or another of incompetence. It is, to be sure, incompetence owing to privatization. But the incompetence is of broader reach than that. It is incompetence of governance altogether, where the incompetence owing to privatization is a symptom, not a cause.

We end where we began, in the company of Baruch Spinoza. Spinoza first proposed that sovereign is he who takes responsibility for the welfare of the subjects. He proposed this as a matter of fact, of stern realism in contrast with what he regarded as the idealism of Hobbes’s rather more chaste and withdrawn sovereign, who claims only to guarantee the peace. Spinoza is the prophet of the welfare state, the state that lives or dies by the welfare of its subjects. In such a state, every function imaginable is, at root, an inherent government function. There is no necessary distinction between public and private—or rather, the distinction between public and private is constantly being negotiated and redrawn. What is private is private only for reasons of state and not for its own reasons. We do not, in fact, have Hobbes’s state, a state that is responsible for keeping the peace and nothing else. Spinoza was right. Our state is Spinoza’s state. It is a state that is subject to limitless demands. Whether Franklin Roosevelt’s New Deal, Harry Truman’s Fair Deal, Lyndon Johnson’s Great Society, or George Bush’s Compassionate Conservatism—these are minor variations on a theme. The theme is that the state can never say no. If there is a problem in the world, the state is responsible for fixing it. The state is always being

pressed to the limits of its competence, and all too often beyond. At the same time, because the boundary between public and private is in constant negotiation, corruption and conflict of interest are baked into the core. That is not the fault of those who rule us; it is their fate, and ours, which we must, as Spinoza told us, accept with grace.

Years ago, I studied one way that the sovereign outsources judgment that has been enormously successful in many countries for close to two hundred years. At its most elementary, this outsourcing takes the specific form of fiduciary obligation, in which one person, a fiduciary, exercises a judgment that legally binds another person, the beneficiary of the judgment. Because the fiduciary’s judgment is a judgment that legally binds the beneficiary, it is necessarily a sovereign judgment, for it is only the judgment of the sovereign that can create or change another’s legally binding obligation. The fiduciary is necessarily the delegate of sovereign judgment.

The legal system instantiates this initial delegation of sovereignty in a series of constructions based upon, and elaborating on, the fiduciary obligation. The constructions range from agency and trust, to joint venture and partnership, to the corporation and the limited liability company. Limited liability is the consummate expression of the delegation of sovereign judgment inasmuch as it replicates in the private sphere a partial sovereign immunity, which simultaneously shields both the managers of an enterprise and its investors from liability to outside parties.

Fiduciary obligation and the myriad of associational structures built on it thus present a series of successful, and ancient, ways of outsourcing sovereignty. Of course, each of these ways comes with its own set of problems and frustrations. Each needs constant monitoring and adjustment. But on the whole, these structures do the job the sovereign has assigned them to do: self-legislation in contract and the exercise of judgment on behalf of another in discharge of fiduciary obligation. So the state can, in fact, outsource a certain kind of

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32 What marks the sovereign as sovereign and distinguishes it from every other social institution is precisely the power to create and change legal obligation. Of course, the sovereign, like any other social institution, can take on other tasks as well. Nothing limits it to changing and creating legal obligation. It can feed and it can clothe, it can educate, it can worship, build roads and pick up the trash. But none of these other tasks is unique to sovereignty. Only changing and creating legal obligation is.

33 On the delegation of sovereign judgment in general, see Arthur J. Jacobson, The Private Use of Public Authority: Sovereignty and Associations in the Common Law, 29 BUFF. L. REV. 599 (1980) (rejecting the nexus of contracts account of the corporation in favor of a delegation account). The question whether the institution of contract represents a delegation of sovereign judgment is controversial and difficult, and I shall not address it here. I took the position in the Buffalo Law Review article that it does not, because the essence of sovereign judgment is creating or changing legal obligations for another, which contract cannot accomplish. Id.
judgment, but only on a very strict condition: that the recipients of the power of judgment be subject to the discipline of the market. That is what permits the outsourcing of judgment to succeed. An outsourcing of judgment that simply puts a government function in private hands without subjecting it to a discipline of any sort—whether of politics or of the market or of bureaucratic coordination—cannot possibly succeed. The recipient of an undisciplined delegation of duty will use its powers at the expense of the public and for its own private good. That is what happened in Fallujah.