



WHITE PAPER

MATERIEL MANAGEMENT OUTSOURCING AND PRIVATIZATION

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Office of the Chief Counsel

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DEPARTMENT OF THE ARMY
HEADQUARTERS, U.S. ARMY MATERIEL COMMAND
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REPLY TO
ATTENTION OF

AMCCC (27)

12 May 1997

MEMORANDUM FOR SEE DISTRIBUTION

SUBJECT: Materiel Management Outsourcing and Privatization Initiatives

1. Enclosed for your review and use is a White Paper on materiel management outsourcing and privatization initiatives. This Paper is the product of a joint effort among U.S. attorneys from the U.S. Army Materiel Command, the Office of the Army General Counsel, the Office of the Judge Advocate General, and the U.S. Aviation and Troop Command.
2. The White-Paper develops a hypothetical materiel management privatization-proposal and addresses the legal issues that arise from this proposal. The purpose of the Paper is to provide attorneys with a common Army-wide framework for identifying and evaluating these issues as they arise. As such, the paper is intended to serve as a tool for attorneys for providing advice to managers. We emphasize, however, that this White Paper is devoted solely to legal issues, and is not intended to provide a comprehensive approach to the evaluation of materiel management privatization proposals. Equally important to this greater effort are non-legal considerations relating to management objectives for pursuing a particular initiative, and the policy environment in which these decisions are made. These latter issues of readiness, economics, management objectives, and impact on industry and current federal employees cannot be overlooked.
3. If you have any questions pertaining to the material covered in the White Paper, please contact Ms. Elizabeth F. Buchanan, Office of the Command Counsel, U.S. Army Materiel Command, at DSN 767-7572. She will either answer the question or refer it to the attorney preparing that section of the White Paper. Comments and suggestions for improving this Paper are also welcome.
4. AMC -- America's Arsenal for the Brave.

A handwritten signature in cursive script that reads "Edward J. Xorte".

EDWARD J. XORTE
Command Counsel

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All MSC Chief Counsels

MATERIEL MANAGEMENT OUTSOURCING AND PRIVATIZATION

I. INTRODUCTION

This White Paper is designed to take a hypothetical materiel management privatization proposal and address the legal issues that arise from the proposal. The purpose of the White Paper is to assist Army attorneys through development of a common Army-wide framework for examining these issues. Critical to this effort is communication between attorneys in the field, the U.S. Army Materiel Command (AMC) Command Counsel, and Department of the Army (DA) legal counsel (both from the Office of The Judge Advocate General (OTJAG) and the Office of General Counsel (OGC)). Effective communication throughout the Army legal community is key to improved service to our clients.

Materiel management privatization initiatives fall into an area of the law in which there is little case precedent. There have been major developments in the past year, with regard to regulatory guidance and development of business models.¹ This Paper is designed to be a tool for attorneys to use in providing legal advice to managers. Options have been identified that entail various degrees of risk. As we apply the various alternatives, our purpose is to provide our clients with the best legal advice. We are committed to supporting our clients in accomplishing the mission. As our clients address matters involving outsourcing and privatization, their foremost consideration will be military readiness and economics. We must offer an explanation of the legal requirements for various options, all of which must be considered not **only** in light of executive objectives, but also in light of legislation and Congressional direction.

No paper can provide a “one size fits **all**” solution to every issue arising from materiel management privatization proposals. The development of common or permissible interpretations of **statutes** and regulations provides only one part of the analysis required in the resolution of legal issues. Equally critical is the **application** of specific facts to these interpretations. In consequence, proposals must be evaluated on a case by case basis with particular attention paid to the matching of particular facts with agreed upon interpretations. Alternatives must be selected in good faith, and in compliance with reasonable interpretations of law.

II. HYPOTHETICAL

The Government is interested in contracting for complete life cycle support for Weapon System X. The data for that weapons system partially belongs to the Government and partially belongs to one or more contractors. The support which the Government is considering contracting includes the non inherently governmental portions **of**: stock control; requirements determination; acquisition of parts and services; engineering support; configuration management;

¹ For example, OMB Circular A-76 Revised Supplemental Handbook was issued March 1996. Draft DOD **Instruction** 4100.33 and Draft Army Regulation 5-20 seek to implement this Handbook in the context of the unique statutes governing DOD actions.

storage, distribution and disposal of inventory; supply support; and depot level maintenance. The Government would like to combine these functions in a single contract going to either one contractor or a team of contractors to obtain the benefits of “one stop shopping,” ease of incorporating system improvements and efficiency. These functions are largely being performed by a total of more than 45 DOD civilian employees in several different locations and organizations. At least one of the principal functions has been the subject of a Base Closure and Realignment (**BRAC**) recommendation and is scheduled to move to a specified Army location.

III. SUMMARY OF LEGAL CONCERNS

- A. OMB Circular A-76 and the related DOD statutes governing contracting out
- B. Base Realignment and Closure
- C. Depot Maintenance - Core Logistics, the 60-40 Rule and Private-Public Competition
- D. Competition
- E. Small Business
- F. Fiscal Considerations
- G. Antitrust
- H. Summary of Legal Issues and Recommendations

IV. DISCUSSION

A. **OMB CIRCULAR A-74 AND THE RELATED DOD STATUTES GOVERNING CONTRACTING OUT**

1. Introduction

OMB Circular A-762 requires that federal agencies perform **cost comparisons** when converting work to or **from** m-house, contract or interservice support agreement, unless an exception applies.³ **In addition to the OMB Circular A-76, there are a number of statutes** which either reference OMB Circular A-76 or reference some aspect of a **cost comparison.**⁴

² **Bolding** will be used throughout this White Paper to focus attention on the major points.

³ OMB Circular A-76, Revised Supplemental Handbook, Part I, Chapter 3, **para** A.1.

⁴ The principal statutes are:

10 USC 2461 - requires notice to Congress and a detailed cost comparison before converting any commercial or industrial function of the DOD which on October 1, 1980 was being performed by 45 or more DOD civilian employees to contract performance. There are some statutory exceptions, such as war or national emergency, and purchases of goods and services of the blind and other severely handicapped.

A fundamental issue in the analysis of OMB Circular A-76 and the related DOD statutes is whether those DOD statutes impose responsibilities in excess of those imposed by OMB Circular A-76, or merely require the DOD to comply with OMB Circular A-76. A related issue is to what extent certain materiel management proposals may fall outside the scope of both OMB Circular A-76 and the related DOD statutes. Those issues are discussed below.

2. Actions not considered to be within the scope of either the Circular or the statutes

Some actions have not been treated as “conversions” of work to or from in-house, contract or interservice support agreement for purposes of either the OMB Circular A-76 or the related DOD statutes. For example, OMB has determined that functions which are privatized or reengineered to the extent of being fundamentally different **from** current functions **are** not being “converted” for purposes of OMB Circular A-76. By way of example, OMB concurred that the **Office** of Personnel Management was not required to perform a cost comparison when it divested its security investigation function to a private company through an Employee Stock Ownership Program (**ESOP**). OMB also concurred that DLA was not required to perform a cost comparison when it divested itself of the “acquire, store, and ship” business and moved to direct vendor deliveries in the Prime Vendor Program.⁵

10 USC 2462 - requires the **Secretary of Defense** to purchase goods and services (other than those which must be performed by military or government personnel) from the private sector if the private sector can provide the goods and services **for a lower cost** (including any cost differential required by law, Executive order, or regulation) than the cost at which the **Department** can provide the same goods or services. This statute also requires the Secretary of Defense to ensure that all costs considered are realistic and fair.

10 USC 2464 - requires the Secretary of Defense to identify **logistic capability** that must be maintained to ensure a ready and controlled source of **technical** competence and **resources**, and prohibits contracting for that activity under OMB Circular A-76 or any successor regulation or policy unless **the** Secretary of Defense waives the requirement with a determination that government performance is no longer required for national defense reasons. Prior notice to Congress is required before a waiver is effective.

10 USC 2467 - requires the Secretary of Defense to include **retirement costs** in any cost **comparison** conducted by the DOD under OMB Circular A-76. Also requires **regular consultation with affected employees and their labor organizations**.

10 USC 2469 - requires the Secretary of Defense to use merit based selection procedures to move a depot level workload over \$3 million to another DOD depot level activity and to use **aprivate-public competition** to move a depot level workload over \$3 million to performance by contractor. **OMB Circular A-76** (or any successor regulation or policy) does not apply to a performance change covered by this statute.

Section 8015 of the FY 97 DOD Appropriations Act (P.L. 104-208) prohibits use of appropriated funds to convert any function currently performed by more than 10 DOD civilian employees **until a most efficient and effective organizational analysis** has been completed, and **certification** of such is made to the defense committees of Congress. There are exceptions for purchases of goods and services from the blind or other severely handicapped or **from** a business under 5 1% Native American ownership.

Federal Workforce Restructuring Act (P.L. 103-226), section 5g, requires the President to ensure that **service contracts are not increased as a result of streamlining or buyouts without cost comparison**.

⁵ **The Prime Vendor Program** is a Defense Logistics Agency (DLA) initiative in which military customers obtained goods directly **from** a commercial vendor. Instead of filling customers requisitions by issuing stock from a DLA depot, DLA electronically transmits requisitions to the Prime Vendor. The Prime Vendor then fills the requisition by sending the goods directly to the military customer. The Prime Vendor program initially applied to commercial items only. DLA has begun experimenting with the Virtual Prime Vendor (VPV) program to apply

There is very little guidance on what facts are required to be established to qualify as privatization or business process reengineering. More directly, it is unclear whether the hypothetical materiel management privatization proposal would qualify as privatization or substantial reengineering for purposes of not having to perform a cost comparison.

In the absence of any case law or policy, the best place to start is the definition for privatization provided in the OMB Circular A-76 Revised Handbook. That definition states that privatization is:

“the process of changing a public entity or enterprise to private control and ownership. It does not include determinations as to whether a support service should be obtained through public or private resources, when the **Government** retains full responsibility and control over the delivery of those services.”

Applying that definition would indicate that two **critical factors** distinguishing privatization (to which cost comparison does not apply) from **outsourcing**⁷ (to which cost comparison does apply) are **control** and **ownership of assets**. **Thus**, to the extent the Government gets out of the “acquire, store, and ship” business, gives up ownership of spare parts and tool sets, and contracts for results rather than specifies functions, the Government is closer to a privatization or business process reengineering that would warrant a decision not to perform a cost comparison. Divesting a business whether through an ESOP or other arrangement would meet the definition of privatization, as opposed to outsourcing, because the Government is giving up both control of the function and the assets.

Other factors that may distinguish privatization **from** outsourcing are whether there is a commercial market for **the** function which meets Government requirements, whether the function is a core **function** to the Government organization, and whether the function as reengineered could be performed by current Government employees without substantial retraining or investment.

If there is a **commercial market** for the function which meets Government requirements, then it is an easier decision for the Government to give up its in-house capability and rely on the commercial sector to provide the goods and services. There will also be less need to control the function because competitive pressures in the market will provide some degree of control.

Prime Vendor materiel management concepts to weapon system applications. The VPV is required to fill requisitions, forecast future requirements, and maintain a surge capability to meet mobilization demands.

⁶ OMB Circular A-76 Revised Handbook, Appendix 1.

⁷ Outsourcing was defined by the Defense Science Board in its August 1966 report as the “transfer of a support function previously performed in-house to an outside service provider.”

⁸ A core function is a commercial activity operated by a cadre of highly skilled employees, in a specialized technical or scientific development area, to ensure that a minimum capability is maintained. Draft AR 5-20, Definitions. A core function is different **from** core logistics. (See Section III C for definition of core logistics).

If the function, however, is a **core function** to the Government organization, then the government will probably require more control over the function. Core **functions** require significant policy (management) decisions to be made concerning the nature of the organization, its mission and the necessary or important functions that will be deemed essential. A core function is less likely to be privatized. Even if not core, a commercial type activity involving the application of substantial core expertise, such as with an evolving weapons system, might intermingle the Government and commercial roles to such an extent that there is no “clean” privatization.

Finally, if the function as reengineered is available in the commercial market **but could not be performed by Government employees without substantial retraining or investment**, **this** is a factor that lends itself to a finding that the reengineered requirement is so fundamentally different from current functions that a cost comparison would not be helpful. To take an extreme example, if the Government is moving from a storage and transportation function characterized by written paper entries and an inability to locate any items in transit to a storage and transportation function in which computerized data processors read bar codes and automatically enter in the location of items through an Internet connected computer system easily read by everyone in the supply system. The Government could reasonably conclude that the skill differential (between paper entries and maintaining a automated system) and the investment required (to upgrade facilities) may not be warranted if automated services were routinely available in the commercial sector. This is a case in which functions are not being “converted.” On a very macro level, the function may be storage - but the methodology and process improvements are so different that it can be said that these are not the same functions.

Both DOD and DA have agreed that certain functions which are reengineered or privatized are not “converted” for purposes of cost comparisons. Draft DOD Instruction 4 100.33, para B. 14, states “[This Instruction “D]oes not apply to workload reductions resulting from business process reengineering where commercial activities are not directly converted to or from contractor performance, such as use of direct vendor deliveries in lieu of storage and distribution.” Draft Army Regulation 5-20, **para 1-6j**, states:

“Legislative/Administrative **Exclusions...j**. Privatization of a commercial nature, when the Army transfers ownership, control, and responsibility for performance of the activity, is not a commercial activity conversion to contractor performance. For example, privatization of a wastewater treatment plant or an electrical distribution system may be accomplished by transferring ownership of facilities, with or without land, along with the operation and maintenance responsibility for the plant or system, to a commercial utility company. The transfer to a non-federal entity ends Army involvement in the activity and provision of the service. The Army no longer determines requirements or provides quality assurance for the service, and does not have control of provision of the service or operation and maintenance of the facility. These **privatizations** are not subject to the cost competition requirements of DA Pam 5-20.”

When the facts of a particular proposal demonstrate that a function is being divested, privatized, or reengineered to the extent that the function is fundamentally different, not **only** the OMB Circular A-76, but the related DOD statutes referencing cost comparison, most efficient and cost effective organization analysis and OMB Circular A-76 are not applicable.

It is possible that a materiel privatization proposal may be able to demonstrate divestiture, privatization, or reengineering to the extent of being fundamentally different such that a cost comparison would not be necessary, depending upon the specific nature of the proposal. Each proposal must be analyzed on a case by case basis.⁹ Because there is no clear guidance in this area, practitioners should exercise caution. The early assistance of counsel in the development of proposals will increase the certainty with which managers can define the legal process requirements for implementation. The decision that a proposal possibly affecting more than 45 current government employees is not within the scope of OMB Circular A-76 and the related DOD statutes should be coordinated with the Major Command because of the possibility of litigation and Congressional **interest**.¹⁰

3. Exemptions and waivers to the cost comparison process

a. Introduction

Even if a proposal cannot reach the extent of demonstrating divestiture, privatization or fundamental reengineering to warrant a determination that the function considered for contract is not the same function as is currently performed, there are a number of **exemptions and waivers** to the cost comparison requirements in OMB Circular A-76. The **exemptions and waivers with the** greatest relevance to the materiel management privatization proposal are:

(1 j A new requirement or a severable expansion to an existing requirement (which should be put on contract rather than be performed in house);¹¹

(2) Waivers are granted to an activity at an installation ¹²scheduled for closure or in cases where functions are designated for termination on specified dates;

(3) Functions with 10 or fewer full time equivalent (FTE) civilian employees;¹³

⁹ The facts of a particular case should be examined for other possible statutory exceptions to OMB Circular A-76, such as the exception for functions funded with research and development funds (10 USC 114 note [section 802 of P.L. 96-107]) or cooperative agreements for prototype efforts related to weapon systems (section 804 of the FY97 DOD Authorization Act).

¹⁰ The number 45 was chosen because of the possible impact of 10 USC 246 1.

¹¹ OMB Circular A-76 Revised Handbook, Part 1, Chapter 1, **para** D.2 and D.3.

¹² OMB Circular A-76 Revised Handbook, Part 1, Chapter 1, **para** E.6.

¹³ OMB Circular A-76 Revised Handbook, Part 1, Chapter 1, **para** D.5.

(4) An activity performed by more than 10 FTE civilian employees if fair and reasonable prices can be obtained through **competitive** award and all directly affected permanent employees will be placed in comparable positions;

(5) Case by case waivers in which the designated agency official determines that the conversion will result in significant financial or service improvement without reduction in the level or quality of future competition or ¹⁵the in-house offer has no reasonable expectation of winning a cost comparison competition. These waivers are subject to administrative appeal; and

(6) Depot **maintenance**.¹⁶

When evaluating OMB Circular A-76 exemptions and waivers to the cost comparison process, it is critical to determine the impact of various DOD and federal statutes that impose or reference various cost comparison requirements. Those statutes were summarized at footnote 4.

b. Two Possible Positions

There are at least two positions which can be taken on the issue of the interface between OMB Circular A-76 and the statutes that impose or reference cost comparison requirements.

The first, and more commonly held position within the Army and perhaps within DOD, is that the various DOD and federal statutes must be read to impose cost comparison and most efficient and cost-effective analysis requirements in addition to or different from those imposed by OMB Circular A-76. For example, Draft DODI 4100.33 permits direct conversions (without cost comparison) for conversions of functions involving 11 through 45 FTE personnel **only** when the “DOD component shall submit a certificate to Congress that certifies that the Government calculation for the cost of performance is based on an estimate of the most efficient and cost-effective organization.”

Similarly, Draft DODI 4 100.33 permits use of streamlined cost comparison procedures for organizations of more than 10 FTE under the same certification requirements. These requirements clearly represent an effort to comply with the requirements of section 80 15 of the FY 97 DOD Appropriations Act. In the same vein, Draft AR 5-20 permits a waiver to cost comparison process only when there is documentation that the various legal restrictions to converting DOD functions to contract (such as section 80 15 of the FY 97 DOD Appropriations Act and 10 USC 2461, 2462, and 2465) do not apply. This first position is discussed in more detail in **section e.** below.

¹⁴ OMB Circular A-76 Revised Handbook, Part 1, Chapter 1, **para D.6.**

¹⁵ OMB Circular A-76, Revised Handbook, Part 1, Chapter 1, **para E.**

¹⁶ 10 USC 2464, 2466, and 2469.

The second possible position is that the various DOD and federal statutes referencing cost comparison, most efficient and cost effective organization analysis and OMB Circular A-76 can be read to require the DOD to comply with OMB Circular A-76 as a whole, including the waiver and exemption provisions as well as the cost comparison methodology provisions. There is less Army and DOD support for this position, although Draft AR 5-20, para 4-20, authorizes direct conversion of functions being contracted under preferential procurement programs, functions designated for termination on a specified date, and patient care without apparent statutory authority other than OMB Circular A-76 exemptions.¹⁷ This position will be discussed in more detail in section f. below.

c. Statutory History

As a matter of normal statutory analysis, the first step in deciding what Congress intended with enactment of ambiguous statutory language is to review the statutory history. A review of the DOD statutes indicates that they were passed at different times for different reasons, and not as part of a coherent legislative plan.

The principal DOD statute affecting cost comparisons, 10 USC 246 1, **was** originally enacted as part of the FY 79 DOD Authorization Act as a compromise between Senate language that stated that OMB Circular A-76 was binding upon the Department of Defense and House language that required notice to Congress before any Government function was studied for conversion to contractor performance plus “the amount of the bid accepted and the cost of performance by Government personnel, together with all other costs and expenditures the government could incur by such **conversion.**”¹⁸ This provision was later codified in 1988 when a number of free standing legislative provisions from various DOD Authorization Acts were codified into permanent legislation as part of a Congressional effort to streamline legislation.¹⁹ This statutory history does indicate a Congressional intent to require DOD to comply with OMB Circular A-76, as well as a desire to have notice of certain contracting out efforts.

The DOD statute permitting local base commanders at installations closing under the Base Realignment and Closure Act (**BRAC**) to contract for services such as firefighting and guard services without cost comparison was enacted because “[S]uch studies are unproductive given the **skeletal** nature of the base workforce and such procedures will expedite base transfer to civilian use.”²⁰

The DOD statute requiring private-public competitions prior to moving a depot maintenance workload of \$3 million or more **from** a depot level activity to the private sector was

¹⁷ Two of the statutes, 10 USC 2461 and section 8015 of the FY 97 DOD Appropriations Act, do provide for exemptions for some ‘preferential procurement programs’.

¹⁸ Section 806, P.L. 96- 107. History found in U.S. Code Congressional and Administrative News, 96th Session, Vol. 2, page 1836.

¹⁹ P.L. 100-370; U.S. Code Congressional and Administrative News, page 1077.

²⁰ House Report 103-200, July 30, 1993.

originally enacted in 1992 and significantly amended in 1993 to address concerns that **workload** was being moved from depot maintenance **activities** being realigned or closed under **BRAC** without a fair consideration of the alternatives

In summary, various reasons have been proposed for the enactment of these statutes. These reasons are not necessarily consistent. A driving concern on the part of Congress seems to be that the DOD have verifiable and valid reasons for deciding to convert functions currently performed by federal employees to contractor performance.

d. Case Precedent

There is very little case law which analyzes the impact of the statutes - that is, do the statutes incorporate OMB Circular A-76 and its cost comparison process or do they add additional or different requirements over and above OMB Circular A-76? The principal case which does discuss the relationship between the DOD statutes (10 USC 2461 and 2462) and the Circular found that by enacting 10 USC 2461 [and related sections of Chapter 146 of title 10], Congress was directing the DOD to contract out in the context of Circular A-76; and more specifically, to contract out when a cost comparison demonstrated that the Government **would** save money by contracting out.²² This case, taken literally, supports the proposition that compliance with OMB Circular A-76 constitutes compliance with the various statutes that require various portions of the OMB Circular A-76 process. It should be noted that this case is a complete departure **from** prior Circuit cases in that the Sixth Circuit established a right of displaced federal employees to challenge a “wrongful privatization” action under the Administrative Procedure Act. No Circuit Court other than the Sixth Circuit has reached this position.

e. Prevailing DOD View

The current prevailing DOD position is that the DOD unique statutes require cost comparison or MEO certification requirements in addition to or different from those required by OMB Circular A-76. OMB Circular A-76 contains a series of exemptions and waivers that might apply to a particular materiel management proposal.²³ Under the prevailing DOD position, even if OMB Circular A-76 contains an exemption or waiver which might apply, we must certify and submit a Most **Efficient Organization (MEO) analysis or cost comparison to Congress unless there are exceptions to the statutory requirements that would permit another result. Each of the statutes contains similar but different exceptions. For example, 10 USC 2461 only applies to functions being performed by DOD civilian employees on October 1, 1980.**

²¹ Conference Report No. 103-357, November 10, 1993, pages 656-657.

²² Diebold v. United States of America, 947 F.2d 787 (6th Cir. 1994), cert. denied, 513 U.S. 1153 (2003). “The fact that a contractor’s failure to comply with its [A-76] directives is evidence of compliance or lack thereof with the statutory directives in 41 USC 401 et seq. and 10 USC 2462.”

²³ Examples of potential exemptions and waivers include the exemptions and waivers described in section a. above. The application of those potential exemptions and waivers is more fully described in section f. below

There are also exceptions for functions to be performed by the blind and severely handicapped. Section 8015 of the FY 97 DOD Appropriations Act only applies to functions being performed by DOD employees on the date of enactment of the Act, and has similar but different exceptions (including not only functions to be performed by the blind and severely handicapped but also functions to be performed by companies under 51% Native American ownership.)

The statutory requirement to submit a cost comparison or MEO analysis does not necessarily mean that the whole OMB Circular A-74 process must be followed to arrive at the result. In other words, if the statutes do not incorporate OMB Circular A-76 as a whole (including all exemptions and waivers), then they do not necessarily include the whole set of processes that encompass a Circular type cost comparison either. Some provisions of the OMB Circular A-76 process may be mandated by law. For example, 10 USC 2462 requires that the DOD apply any cost differential required by law, Executive Order, or regulation. OMB Circular A-76 is a federal regulation, and we may be required to apply its 10% cost differential in the absence of other regulations.²⁴ Other aspects of a Circular type cost comparison are not mandated by law, and may be given a different definition by DOD than provided in OMB Circular A-76. For example, we may **define** the term “cost comparison” in 10 USC 2461 to refer to a streamlined cost analysis in cases in which the Circular itself would provide an exemption or waiver, rather than an OMB Circular A-76 cost comparison.

Using this approach, we may find that an exemption or waiver from the Circular applies, thereby precluding a Circular requirement to perform a cost comparison. We may then comply with the DOD statutes through a streamlined cost analysis which analyzes the Government and contractor cost of performing the function. Any cost analysis would have to meet a “straight face” test regarding the reliability of the information. It would also have to address the “best case” Government cost. This information, plus any required impact study, would be provided to Congress.

Another possible source of relief from the cost comparison requirement can be found in the statutory language. Two of the principal DOD statutes are triggered by specific dates at which the activity or function must have been performed by Government employees. 10 USC 2461 is triggered when the Government considers converting to contractor performance “commercial or industrial type function of the Department of Defense that is being performed by more than 45 civilian employees as of October 1, 1980.” Section 8015 of the FY 97 DOD Appropriations Act is triggered when the Government considers converting to contractor performance an activity or function being performed by Government employees “on or after the date of enactment of this Act.” It is possible that the activity or function under consideration for outsourcing was not being performed by Government employees on the triggering dates for one or both of these statutes. In analyzing the dates on which activities or functions were being performed, a

²⁴ OMB Circular A-76, Revised Supplemental Handbook, requires that there be a minimum cost differential of the lesser of **10%** of the personnel costs or **\$ 10 million** over the performance period before performance of a function is changed to contractor or in-house performance. This minimum cost differential recognizes the costs of conversion.

fundamental question is the definition of activity or function. Is activity or function general or specific? More specifically, when 10 USC 2461 statute provides that cost comparisons are only required for functions or activities being performed by more than 45 civilian employees **as of October 1, 1980**, does this statute apply to functions or activities in the broader sense of **materiel management functions for any weapon system** or does it apply to materiel management functions of the **particular weapon system**?

A DOD commercial activity is defined in Draft DODI 4100.33, Appendix A, as “[A]n activity that provides a product or service obtained (or obtainable) from a commercial source.. .A DOD commercial activity may be an organization or part of another organization. It must be a type of work that is separable **from** other functions or activities so that it is suitable for performance by contract.” Draft AR 5-20, Appendix A, defines “functional activities” as “those installation activities responsible for producing a product or service.” Neither of these definitions are especially helpful in determining **whether** the statutes apply to functions or activities in the broader sense of materiel management functions or to materiel management functions of a particular weapon system.

The better position would be that functions and activities apply in the broader sense of materiel management functions, especially if the essential nature of the function does not differ depending upon the exact nature of the weapon system. **However, if a weapon system were not fielded until after October 1, 1980, and the functions were at least somewhat different because of the technology of the weapon system, it is possible to take the position the function would not fall under the restrictions of 10 USC 2461**, and its Congressional notice requirement. In any event, if the DOD statutes governing the cost comparison process are held to be in addition to OMB Circular A-76 requirements, then a certificate to Congress that the Government calculation for the cost of in-house performance is based on an estimate of the most efficient and cost effective organization would be required to comply with section 8015 of the FY 97 DOD Appropriations Act.³

In no case should any portion of a materiel management privatization proposal which concerns depot maintenance follow OMB Circular A-76 requirements. If a privatization proposal concerns a depot maintenance workload currently being performed in the DOD depots with a value of \$3 million or more, there must be a competition following 10 USC 2469. DOD is currently developing guidance for these competitions, which should be available shortly for use.²⁶

f. A Minority View

If we take the position that the DOD statutes require us to comply with OMB Circular A-76 and impose no additional requirements, then OMB Circular A-76

²⁵ Draft DODI 4100.33.

²⁶ See Vol. 67, Federal Contracts Report. at page 183.

exemptions and waivers as applied to the hypothetical materiel management privatization proposal would be analyzed as follows:

(1) **New Requirements or Severable Expansion:** The OMB Circular A-76 exemption for new requirements or severable expansions would not apply in this case because the materiel management functions are currently being performed by Government employees unless the functions were reengineered to the extent that they could be said to be a fundamentally different and new requirement. (See the discussion in section 2 above).

(2) **Installation closing under BRAC:** OMB Circular A-76 Revised Handbook exempts an activity at an installation scheduled for closure or functions designated for termination on specified dates from the cost comparison process.²⁷ Some attorneys have argued that any function impacted by a BRAC decision may be contracted without cost comparison because BRAC decisions result in the realignment and closure of installations and functions. We believe that this position is not supported by either the OMB Circular A-76 exemption or the statute exempting DOD from cost comparison requirements for guard, firefighting and other base support functions at an installation closing under BRAC within 180 days.²⁸

The installation closure or “BRAC” exemption in OMB Circular A-76 applies to functions at closing installations or functions designated for termination. It makes sense to waive cost comparison in these cases because there is no long term Government workforce to make an in-house bid. People leave as the function begins the closure process, and it becomes increasingly more difficult to hire for a temporary position.

In the hypothetical materiel management privatization proposal, a function is moving to a specified DOD location as a result of BRAC. The people performing the function at the losing site will either receive transfer of function rights (and move with the function), or there will be a determination that the mission is being performed at the gaining location (which can absorb the function with or without some increase in personnel). In either case, there is a permanent Government workforce with the ability to compete. The BRAC statute permitting DOD to contract for base operations type functions at installations within 180 days of closure is very limited.²⁹ It would not apply to the materiel management privatization proposal under consideration in this paper because that function is not a base operations type function, the contract will not be with the local government, and the function is moving, not closing.

(3) **Functions performed by 10 or fewer FTE.** If the materiel management proposal involves less than 10 or fewer FTE, it may be converted to contract without cost comparison.

(4) **Activity performed by more than 10 FTE employees when all of those employees are placed in comparable positions and fair and reasonable prices will be**

²⁷ OMB Circular A-76 Revised Handbook, Part 1, Chapter 1, para E.6.

²⁸ 10 USC 2687 note, section 2905(b)(8) of the 1990 Defense Base Closure and Realignment Act.

²⁹ 10 USC 2687 note, Section 2905(b)(8) of the 1990 Defense Base Closure and Realignment Act.

obtained through competitive award. The hypothetical materiel management proposal does not state whether all current Government employees can be placed in comparable positions. Assuming that all Government employees can be placed in comparable positions, there will be a competitive award with fair and reasonable prices, and that the statutes are read to include all OMB Circular A-76 exceptions, we should be able to privatize materiel management functions in our hypothetical without performing a cost comparison. If all current Government employees cannot be placed in comparable positions or if the award will be on a sole source basis, then this exception would not apply.

(5) Case by case waivers in which the designated agency official determines that **the** conversion will result in significant financial or service improvement or the in-house offer has no reasonable expectation of winning a competition: The hypothetical materiel management proposal is also unclear whether conversion of the materiel management functions would result in significant financial or service improvements. Assuming that the proposal could demonstrate that acceptance of such a proposal would result in significant financial or service improvements, a **waiver** should be possible. The case by case waiver is found in the March 1996 OMB Circular A-76 Revised Supplemental Handbook. There is very little guidance on what facts are required to establish significant financial or service improvements for purposes of **a** waiver of cost comparison requirements. In the absence of any guidance, possible support for a waiver might exist when the Government either commits that it will convert the function **only** if it obtains contractor proposals which clearly demonstrate significant cost or quality improvements that can not reasonably be met with a Government **workforce** and likely capital improvements or prepares a Business Case Analysis that adequately demonstrates the cost or quality improvements.

(6) Depot Maintenance - See the discussion above. Separate statutes require a depot maintenance competition before moving a depot level maintenance workload with a value of \$3 million or more currently performed by DOD depots into the private sector.

The position that the DOD unique statutes require nothing more than compliance with OMB Circular A-76, and can be waived or subject to exemption, is the most problematic position at this time because of the lack of case law. The risks include litigation, adverse Congressional reaction, and possibly a violation of the Antideficiency Act (because section 8015 of the FY 97 DOD Appropriations Act is enforced through funds control). It is the considered opinion of the undersigned attorneys that there is reasonable support for the position that when an OMB Circular A-76 exemption applies, the DOD unique statutes can be read not to require any additional requirements because the cost comparison requirement was never triggered. Those attorneys are uncomfortable with the concept that the statutes can be waived with a administrative agency waiver, and would not advise that course of conduct. When an **administrative** agency waiver is issued, the undersigned attorneys would recommend submission to Congress of an adequate cost comparison addressing “best case” Government cost and any required impact studies.

4 . I n S u m m a r y

A manager trying to determine what level of process is required to contract out for functions currently being performed by government employees has a number of options which involve different costs, benefits and risks to implementation. **An analytic approach to these options would provide the following options:**

1. Determine whether OMB Circular A-76 contains any exemptions or waivers that apply to the proposal. If it does, then consider whether the DOD related statutes would require any additional reporting. If no additional reporting is required, then document the existence of the exemption or waiver, and continue with implementation of the proposal.

2. If OMB Circular A-76 contains an applicable exemption or waiver, but the related DOD statutes would require reporting of an MEO or cost comparison, then the manager must decide whether he would prefer doing a full OMB Circular A-76 cost comparison (a decision which involves more cost and delays at the beginning of the process but which may reduce later litigation over the applicability of the Circular) or would prefer doing an adequate cost analysis considering the Government's "best case" costs but not necessarily a full OMB Circular A-76 cost comparison. This latter option bears some risk of litigation over the applicability of OMB Circular A-76, but saves the costs and delays inherent in the full cost comparison. There will be costs in performing the adequate cost analysis. The principal risk is that the decision not to perform a cost comparison could be overturned either by the courts or through adverse political reaction, and the manager required to perform a cost comparison after investing the effort into implementing this approach.

3. If the OMB Circular A-76 would not apply to the materiel management proposal because the proposal can fall into privatization category, document these facts and continue with implementation. This option bears a somewhat greater risk of litigation over the applicability of OMB Circular A-76, but saves some costs and delays inherent in the cost comparison. The principal risk is that the decision not to perform a cost comparison could be overturned either by the courts or through adverse political reaction, and the manager required to perform a cost comparison after investing the effort into implementing this approach. There must be a good cost analysis to justify the decision.

4. If the materiel management proposal falls within the apparent scope of the related DOD statutes, but an exemption from OMB Circular A-76 would apply, then the attorney should consider presenting the manager with two final choices. First, the manager could choose to seek a Congressionally legislated pilot project to permit the materiel management privatization proposal to move forward. This option minimizes any legal challenges but may be politically impracticable to persuade Congress to permit a test. As a second option, the manager may conclude that the DOD statutes require compliance with the Circular, and establish no additional requirements if supported by the local attorney's interpretation of the Diebold case and the statutory history, and after consultation with the MACOM legal office. When an exemption

exists, there is no further notice required.³⁰ This option bears a somewhat greater risk of litigation over the applicability of OMB Circular A-76, but saves some costs and delays inherent in the cost comparison. There are also risks of an adverse Congressional reaction and the potential for an Antideficiency Act violation should a court determine that section 80 15 of the FY 97 DOD Appropriations Act established additional requirements. A manager could be required to commence a cost comparison should the decision not to perform a cost comparison be overturned. There must be a good cost analysis to justify the decision.

B. BASE REALIGNMENT AND CLOSURE

In accordance with Defense Base Closure and Realignment Act of 1990,³¹ all BRAC recommendations become effective and have the full force and effect of law after completion of Congressional consideration. The Secretary of the Army is legally bound to implement the BRAC Commission's recommendations. The Secretary of the Army must initiate their implementation within 2 years from the date the President transmitted his closure and realignment recommendations to Congress and complete their implementation within 6 years of the date when the President transmitted his recommendations to Congress.

Generally, given the nature of the BRAC statutory process, the DOD is required to execute in accordance with the BRAC language, barring any subsequent special legislation to the contrary. Once execution has been completed, then DOD can change the organization mandated by the BRAC language.

There have been many instances of BRAC recommendations from the '91, '93 and '95 BRAC rounds where the specific language of the recommendation was perhaps not the most efficient way to realign a particular mission/function, may have been more costly to implement than another alternative, or because of post-BRAC changed circumstances did not make management "sense" to execute. All of these instances have received the highest scrutiny and challenges from both Congress and the White House. Nevertheless, implementation of that particular BRAC recommendation has ultimately been found to be required by law.

In cases where the BRAC Commission's language is clear, the Secretary must implement the recommendation as stated. In cases where the recommendation language is ambiguous, the Secretary's interpretation is entitled to considerable weight and deference. If challenged, the³² courts will generally review the Secretary's interpretation using a "reasonableness" standard. When a BRAC recommendation specifically states where a particular mission is to be relocated, it is referred to as a "directed move" and it must comply with unless special legislation is enacted directing otherwise. There is no internal agency process to accomplish a desired change to a BRAC recommendation once the BRAC recommendation has become law. This situation is

³⁰ This approach is a reasonable interpretation of law when applied to exemptions from the Circular. It is not recommended when an agency case by case waiver is envisioned.

³¹ Public Law 101-510, Section 2904(a).

³² ChevronUSA, Inc. v. Natural Resources Defense Council, Inc., 467 U.S. 837 (1984).

different **from** a BRAC recommendation that does not specifically reference a particular site, thus allowing for flexibility as to where the mission/function can be relocated or performed, and is referred to as a “**discretionary move.**” A discretionary move allows the agency to send the **mission/function** and positions associated with that mission to a site of its choice based on sound management considerations or may even, depending on the language of the specific BRAC recommendation, provide for its performance in the private sector.

In analyzing the instant case, the BRAC recommendation requires the workload to move to a specific location. There is no indication that special legislation has since been enacted to provide otherwise. **Therefore, the BRAC recommendation must be implemented.**

The fact that we must implement the BRAC recommendation does not mean that the Secretary is precluded from taking otherwise legally appropriate actions with respect to how those missions/functions are performed. The Secretary is invested with broad authority to take those actions necessary to “conduct all affairs of the Department of the Army.³³ This broad authority must be construed in harmony with the BRAC law. There is nothing in the BRAC law that conflicts with the Secretary’s exercise of his authority to disestablish, reorganize, reduce in force, or contract out activities or take other actions designed to achieve greater operational efficiency and better meet **Army** requirements.

A decision by the Secretary in this case to entertain a materiel management privatization initiative would be consistent with the BRAC Commission’s general intent and purpose to “reduce our nation’s” defense infrastructure in a deliberative way that will improve long-term ³⁴ military readiness and ensure that taxpayer dollars are spent in the most efficient way possible. Indeed, the Commission’s 1995 Report urges DOD to consider privatization as an effective means to “reduce operating costs, eliminate excess infrastructure, and allow uniformed personnel to focus on skills and activities directly related to their military missions” @age 3-3).

It is unreasonable to construe the BRAC law as somehow freezing military missions/functions as they existed at the time of the BRAC Commission’s recommendation and suspending the Secretary’s otherwise lawful authorities to manage and organize Army operations pending relocation. A more reasonable interpretation of the BRAC law permits the Secretary to exercise his authorities to determine how best to relocate in accordance with the Commission’s recommendation. In exercising his authorities, the Secretary must take care to ensure that, based on the facts and circumstances of each case, his actions are consistent with the Commission’s intent and purpose and are not taken for the purpose of avoiding the Commission’s recommendation.

In summary, the BRAC law requires that the materiel management function move to the designated location, but the Secretary retains the authority to appropriately determine how those missions/functions will be performed subject, of course, to other relevant statutes

³³ 10USC 3012.

³⁴ BRAC Commission’s 1995 Report to the President, Executive Summary.

and regulations. Consequently, the law would not preclude the Secretary from contracting out a portion of the materiel management function due to move as long as the missions/functions that the Army retains in-house relocate to the designated location in accordance with the Commission's recommendation. As a practical matter, both a BRAC move and contracting out of a materiel management function are lengthy processes. In effect, this guidance permits the ongoing analysis and – if required – cost comparison of privatization proposals to take place concurrently with the **BRAC** move. In some cases, the actual contract may not be awarded until after completion of the **BRAC** move. Where that is so, commanders should continue to comply with BRAC directive language while conducting their contracting out assessments.

The Secretary's decision is not to be viewed in a vacuum but as part of a dynamic process. This process requires him to consider all possible actions (such as divesting, reorganizing, reducing in force or contracting out activities that comprise the mission/function subject to the BRAC recommendation) that will result in his decision as to how to fully implement the **BRAC** recommendation before any of the mission/function is moved to the gaining site - while at the same time achieve greater operational efficiency and better meet **Army** requirements. He must have a vision of the ultimate organization. Failure to develop this vision could result in moving federal employees to a gaining site and then immediately commencing a cost comparison which could adversely impact those employees.

C. DEPOT MAINTENANCE - CORE LOGISTICS, THE **60/40** RULE AND PRIVATE-PUBLIC COMPETITION

1. Core Logistics and the 60/40 Rule

Organic depots exist to support the readiness and sustainability requirements of the armed forces. DOD maintenance depots are, by design, capable of increasing output to high levels in a short period of time to accomplish contingency workload in support of current military strategy. In order to support this role, there is an irreducible minimum of depot maintenance capability that must be accomplished by organic depots. These skills, competencies and facilities are what comprise “core” logistics (“CORE” in DOD shorthand). **Currently, two provisions of Title 10 contain prohibitions on contracting out depot level maintenance in order to ensure CORE capabilities.** Each also provides for waiver of the prohibitions in certain circumstances. The two statutes complement each other in outlining the concept and to an extent, the substance of CORE.

The first enacted provision, 10 USC 2464, requires that the Department of Defense retain a maintenance capability for mission essential materiel in DOD operated depots. This is core logistics capability. This is defined as including personnel, equipment and facilities to ensure a ready and controlled source of technical competence and resources necessary to ensure effective and timely response in emergency situations. To ensure this capability, it prohibits contracting out under A-76 or any successor regulation or policy, of two types of activities:

(1) Logistics activities identified by the Secretary of Defense as necessary to maintain core logistics capability; and

(2) Depot level maintenance of mission essential materiel performed at locations listed in Section 123 1 of Public Law 99-145. Section 123 1(b) of Public Law 99-145, the 1986 DOD Appropriations Act, lists all DOD installations at which depot level maintenance is performed, including all Army depots, Rock Island and Watervliet Arsenals, and Crane, McAlester and Hawthorne Army Ammunition Plants.

This statute provides that the **Secretary of Defense may waive this** prohibition and provide for consideration of an activity for conversion to contractor performance under A-76 upon a determination that Government performance is no longer required for national defense reasons. Regulations issued by the Secretary shall specify criteria for making this determination. The waiver may not take effect until the House and Senate Appropriations and Armed Services Committees are notified and a waiting period has expired. Procedures for a waiver are specified in DOD Directive 4100.33, September 8, 1985.

The second provision, 10 USC 2466, provides that not more than 40 per cent of the funds made available in a fiscal year to a military department for depot level maintenance and repair workload may be used to contract for the performance by non-Federal Government personnel of such workload for the military department. Any funds not used for a contract must be used for performance of depot level maintenance and repair by DOD employees. The Secretary of a military department may waive the applicability of this requirement for a fiscal year to a particular workload or to a particular depot-level activity if the Secretary determines that the waiver is necessary for reasons of national security and notifies Congress regarding the reasons for the waiver.

The two statutes define core logistics in different terms. 10 USC 2464 exempts depot level maintenance activities which have been designated by the Secretary of Defense or by Congress itself as necessary to maintain core logistics capability from OMB Circular A-76 cost comparison reviews. However, Congress did not mandate that any particular system maintenance be performed in any depot, or that an overall level of maintenance activity be performed in any particular depot as opposed to private industry. While Congress thus expressed the general policy and concept of “core logistics” as preservation of an organic depot maintenance capability, the decision as to exactly what, in terms of the types of skills and systems to be supported, constitutes “core logistics” is left to the Department of Defense, subject to the overall 60 per cent floor set forth in 10 USC 2466. The 60 per cent rule was adopted statutorily by Congress because of differing methods of determining CORE by each service and consequently different amounts of workload that were reserved as CORE for the organic base. The rule is applied to the overall total of funds available for depot maintenance in the military department. Because 10 USC 2466 restricts the use of appropriated funds, a violation of this statute also potentially violates 31 USC 1301, because funds would be used for a purpose other than the purpose for which they were appropriated.

Current DOD policy describes CORE in these terms:

“Depot maintenance CORE is the capability maintained within organic defense depots to meet readiness and sustainability requirements of the weapons systems that support the JCS scenarios. CORE exists to minimize operational risks and to guarantee required readiness for these weapons systems. CORE depot maintenance capabilities will comprise only the minimum facilities, equipment, and skilled personnel necessary to ensure a ready and controlled source of required technical competence. Depot maintenance for the designated weapons systems will be the primary workloads assigned to DOD depots to support CORE depot maintenance operations.”³⁵

An essential part of CORE is the capability to perform depot maintenance on designated weapon systems organically. The determination of CORE capability requirements and depot maintenance workloads necessary to sustain these capabilities are developed by each service using a methodology agreed upon by the services. CORE is calculated as a number of direct labor hours of workload, exercising particular skills in support of weapons systems.

Considering the hypothetical example, it is necessary to make several inquiries in regard to CORE logistics restrictions before considering contracting out: **First, is the workload itself considered CORE because of skills associated with the weapons systems, or because of the total number of labor hours needed to sustain the organic base as calculated under the DOD methodology? If it has been designated as CORE for either reason, we may need a waiver from the provisions of 10 USC 2464** to allow the workload to be converted to contractor performance. A complication is that the statute contemplates a waiver **only** to perform an A-76 cost comparison, since its ostensible purpose is to exempt organic depot maintenance from A-76 commercial activity reviews. It is possible that this could be read as conflicting with the later enacted provision of 10 USC 2469 that A-76 does not apply to competitions for maintenance workloads which depots are performing. In this case, we would give effect to the later enacted statute and perform a depot maintenance competition under 10 USC 2469.

Second, will conversion of the workload cause the overall level of workload for the Department as a whole to fall below the 60 per cent floor mandated for organic performance by 10 USC 2466? This concern is usually easier to deal with because the 60 per cent level is applied to all the funds available from appropriations to the military department to perform depot level maintenance. **If conversion of the workload would cause the overall level of workload for the Department as a whole to fall below the 60 percent floor mandated for organic**

³⁵ Memorandum, Office of the Deputy Under Secretary of Defense (Logistics), 15 November 1993, Subject: Policy for Maintaining Core Depot Maintenance Capability, established the definition of core. Memorandum, Office of the Deputy Under Secretary of Defense (Logistics), 1 February 1996, Subject: Agreements and Assignments (A&As) from the January 30, 1996 Defense Depot Maintenance Council (DDMC) Meeting, approved the current CORE calculation methodology.

performance, it could not be contracted out unless other workload were moved from the private sector to the organic sector to compensate.

2. Depot Maintenance Competition Requirements

Federal law, 10 USC 2469, contains a requirement that the Secretary of Defense shall ensure that the performance of a depot-level workload, which has a value of \$3 million or more and is being performed by a depot level activity of DOD, is not changed to performance by a contractor or by another depot-level activity of the Department of Defense unless the change is made using--

(a) Merit based selection procedures for competitions among all depot-level activities of the Department of Defense; or

(b) **Competitive procedures for competitions among private and public sector entities.**

The law provides that OMB Circular A-76 does not apply to a performance change under this statute.

A related section of the law, 10 USC 2470, mandates that any depot level activity of the DOD is eligible to compete for a Federal agency depot maintenance or repair workload for which competitive procedures are used to select the entity to perform the workload.

10 USC **2469** was originally enacted in Public Law 102-484 (the FY 93 DOD Authorization Act). The legislative history indicates that the Armed Services Committees were originally concerned with workloads being transferred from depots that were being closed under BRAC, and wanted to ensure that workloads were not simply shifted to the private sector without consideration of the organic depot maintenance base.

No reason is stated in committee reports for the exemption from OMB Circular A-76. 10 USC 2469 applies to workloads that could be performed by non-DOD employees consistent with 10 USC 2464 and the **60/40** rule, i.e. to above CORE workload. As noted earlier, depot maintenance is considered completely exempt from the requirements of A-76. This is based on the conjunction of 10 USC 2464, which exempts CORE maintenance from commercial activity reviews, and 10 USC 2469, which exempts **non-CORE** workloads from A-76 procedures.

DOD policy issued in November 1994 defines “merit-based selection procedures” for competitions among DOD depot activities as being approved depot maintenance interservicing procedures. Concerning the competitions among private and public sector entities, DOD policy is that activities will only compete for workloads that are considered within their CORE capabilities. If a DOD activity successfully competes for workload of another Federal Agency under 10 USC 2470, DOD policy is that **CORE** workloads of the DOD activity, in like amounts to that won competitively, will be considered for possible outsourcing.

On May 2, 1997, the Undersecretary of Defense (Acquisition and Technology) issued policy guidance governing public-private competitions under 10 USC 2469 which modifies this previous policy. This guidance provides that depot level maintenance and repair workloads not needed to sustain core capabilities will be available for public-private competition. It is recognized that competition can lower costs, irrespective of whether the workload is outsourced. It is also stated that DOD activities will be eligible to compete in accord with 10 USC 2470. While more detailed implementing regulation must be issued, significant points of the guidance are as follows:

Whether workloads are CORE or non-CORE will be determined by a biennial requantification of non-core workloads as an adjunct to the CORE redetermination process. Any workload newly determined “non-core” and therefore eligible will undergo a market analysis to determine if public and private sector sources exist. Any workload package over \$3 million found “competition-viable” as a result of market analysis will undergo a public-private competition. Existing non-core workloads will not be reviewed for possible public-private competition more frequently than every five years.

Source selection guidelines for the competitions are left to each military department, subject a number of specific rules. The contracting and source selection organizations are to be independent of competing public depots. “Issues” (protests) raised by the public activities are to be resolved internally. Past performance of public depots is to be considered and past performance reporting and data collection and reporting system for public depots will be established. While the principle of “maximal cost comparability” is to be observed, the guidance specifies that the cost elements specified in the OMB Circular A-76 Revised Supplemental Handbook will be considered in evaluations. At a minimum, guidelines will be consider Federal Income Taxes, Cost of Facilities Capital and non-recurring transition costs in evaluations.

Accounting procedures and cost estimating systems of public activities will be reviewed by DCAA. An appropriate authority of each military department will be designated to resolve inadequate disclosures and ensure acceptability to DCAA. DCAA will make periodic evaluations, and also assess accuracy and completeness of incurred costs on depot awards.

Considering the hypothetical, **if depot maintenance being transferred to the private sector was deemed to be above CORE**, both under 10 USC 2464 and the 60/40 rule, and it is at least \$3 million on a fiscal year basis, **then a competition is required involving organic sources and the private sector.**

As mentioned above, public-private depot maintenance competitions were held for specific DOD depot maintenance workloads from 1991 to 1994 under the authority of an Appropriations Act provision which continues to be reenacted annually by Congress. The current provision is Section 8041 of the FY97 DOD Appropriations Act, Public Law 104-208. It authorizes the Secretary of Defense to acquire the “modification, depot maintenance and repair of

aircraft, vehicles and vessels, as well as the production of components and other Defense-related articles” through competition between defense depot maintenance activities and private firms. The Senior Acquisition Executive (or delegate) must certify that successful bids include comparable estimates of all direct and indirect costs for both public and private bids. Similar provisions in previous Appropriations Acts were utilized to compete selected “above CORE” maintenance workloads in an attempt to drive down maintenance costs. Candidate workloads were selected by the services and approved at the DOD level. In May 1994, following the recommendation of the Defense Science Board Depot Maintenance Task Force report, the Deputy Secretary of Defense discontinued the competitions. The reason cited was the impossibility of achieving a level playing field between public and private bids. In particular, the inadequacy of the financial management systems of the services to determine the actual cost of specific workloads was cited. The authority of this provision is thus currently unavailable.

If the new DOD policy is issued, public-private competitions will be reinstated, but it appears that they will be conducted because mandated under the authority of 10 USC 2469, and not because DOD has chosen to exercise the discretionary authority under the DOD Appropriations Act provision. The draft policy and public-private competition guidance make no mention of certification that successful bids contain comparable estimates of all direct and indirect costs, which is a statutory requirement under Section 8041, FY97 DOD Appropriations Act.

D. COMPETITION

The Competition in Contracting Act of 1984 (CICA) generally requires that solicitations permit full and open competition, and contain restrictive provisions and conditions to requirements only to the extent necessary to satisfy the needs of the agency.³⁶ Since bundled, consolidated or “total package” procurements combine separate, multiple requirements into one contract, they have the potential for restricting competition by excluding firms that can only furnish a portion of the requirement. The GAO will review challenges to such bundled solicitations to determine whether the approach is reasonably required or necessary to satisfy the agency’s minimum needs.

The GAO will uphold the bundling of requirements only where agencies have provided a reasonable and legitimate basis for using such an approach, *i.e.* have justified the restrictions on full and open competition. The justification for the decision to bundle or use a total package approach must be based upon an investigation and evaluation of evidence which will support the decision and not on unsupported claims or statements made by the agency. In short, the GAO will carefully scrutinize the individual facts of each case to determine whether or not it involves unique enough circumstances which justify the decision to consolidate requirements and inhibit competition.

³⁶ 10 USC 2304(a)(1).

Mere administrative convenience to the agency will **not** justify using the total package approach. In the Better Service case, the GAO stated:

Further, the fact that bundling will be more administratively convenient is insufficient to support this inherently restrictive approach. When the concerns of administrative convenience are being weighed against ensuring full and open competition, the Competition in Contracting Act (CICA)..., and its implementing regulations require that the scales be tipped in favor of ensuring full and open competition. National Customer Engineering, footnote 3.³⁷

In Better Service, the GSA attempted to bundle for its federal supply schedule the purchase, rental, maintenance, repair and lease-to-purchase of photocopiers, supplies and accessories. The protester argued that the bundling of photocopier sales function with repair and maintenance functions unduly restricted competition by excluding firms which only performed one role. The approach was struck down because the GSA presented no evidence justifying it other than administrative convenience to the agency. Cost saving claims were not supported by the record.

In the GAO case of Pacific Supply, Inc., the Air Force attempted to bundle the procurement of a wide range of T56 aircraft engine spare parts, from turbine vane assemblies to a variety of screws, bolts, spacers, sleeves and brackets.³⁸ All of the parts had previously been procured by individual contracts on a sole source basis from the Original Equipment Manufacturer (OEM), Allison Gas and Turbine. The contractual vehicle was a requirements contract with a \$2.5 billion ceiling over a 5 year contract period with self deleting features to allow specific parts of the 294 part bundle to be broken out as additional suppliers became qualified manufacturers. While the GAO lauded the self deleting feature, it held since individual delivery orders need not be synopsized, there would be no additional advertising of the requirement over the life of the contract, thus inhibiting competition. It concluded that the only legitimate purpose being served was administrative convenience and, therefore, the decision to bundle such a broad range of parts over such a long contract term was not justified.

In what types of situations will the GAO or the BCA sustain the agency's decision to bundle or consolidate requirements? One of the main reasons consistently upheld is the need to acquire or maintain overall system integration or parts compatibility. In Southwestern Bell Telephone Company, the Air Force wanted to procure a complex telecommunications system providing, "the necessary combination of hardness, redundancy, mobility, connectivity, interoperability, restorability and security to obtain, to the maximum extent practicable, the survivability of national security and emergency preparedness

³⁷ Better Service B-26575 1.2, 96-1 CPD 90.

³⁸ Pacific Sky Supply, Inc., B-228049, 87-2 CPD 504.

telecommunications in all circumstances, including conditions of crisis or **emergency**.”³⁹ Accordingly, it wanted one contractor to provide the entire system in order that all parts of the telephone system would be compatible and to assure the proper coordination of maintenance, troubleshooting and repair of the entire interrelated system. The Air Force pointed out that it was operating under a “National Communications System” Executive Order which required the system to be in a constant state of readiness and that its previous experience with individual (unbundled) contracts were evidenced by difficulties and substantial delays which caused down time of the system.

In Resource Consultant, the Navy was able to consolidate several tasks associated with the modification of its Weapon System Trainer (WST) for the P-3 aircraft because the **contractor would be responsible for the development and implementation of an integrated system**.⁴⁰ The modification required redesign efforts for two main components (front and rear sections) of the WST which could not be broken out to different contractors because the two components were so intricately interrelated. Likewise, in Magnavox Electronics Systems Co., the Air Force was allowed to bundle the procurement of a missile and its guidance system because of the need for complete system integration?⁴¹

Another line of cases generally allowing bundling or consolidation is in the area of building maintenance services where the GAO has permitted, when adequately justified, the consolidation of a building’s separate operation and maintenance services requirements into a single commercial facilities management (CFM) contract. For example, in the case of A&C Building and Industrial Maintenance Corp., the GAO permitted the consolidation of 15 services for management, operation, maintenance and engineering operations for a single building.⁴² Thereafter, in The Sequoia Group, Inc., the GAO permitted the consolidation of CFM services for five federal facilities in two Texas cities.⁴³

Then in Border Maintenance Services, Inc., the bundling of CFM services was permitted for five buildings in four Texas cities.⁴⁴ In the A&C Building, case the justifying reasons were: (1) bundling would **centralize administration and coordination** of the contract; (2) it would **unify responsibility** for deficiencies in performance and prevent “finger pointing” by separate contractors; (3) It would **improve operation** of the buildings; and (4) it would **eliminate the need for the agency, the GAO , to hire additional personnel** to manage and monitor the contract. In Sequoia, supra, the primary reason which justified the consolidation was the fact that the agency, the GSA, had recently **undergone serious staffing cuts** and was under a hiring freeze which limited its ability to monitor multiple contracts in two cities. In Border, supra, the unique facts which justified the total package were: (1) **loss of employees with a hiring freeze** and (2) **past history of problems**

³⁹ Southwestern Bell Telephone Company, B-23 1822, 88-2 CPD 300.

⁴⁰ Resource Consultant, Inc., B-255053,94-1 CPD 59.

⁴¹ Magnavox Electronics Systems Co., B-258037,94-2 CPD 227.

⁴² B-230839, 88-2 CPD 67.

⁴³ B-252016,93-1 CPD 405.

⁴⁴ B-260954, 95-1 CPD 287.

associated with individual contracts, e.g., finger pointing by individual contractors when performance difficulties arose. It should be noted that in all of these cases competition was not totally eliminated by the consolidation. Even after bundling, while some small contractors were effectively removed from the competition, numerous others were capable of performing the stated consolidated requirements.

In these bundling cases, many times an agency will cite cost cutting or concern about incurring additional costs as justification for bundling. The GAO has held that these costs must be clearly demonstrated. In the case of National Customer Engineering, it was stated that:

Restricting competition is presumed to raise, not lower, the cost that the government will pay, and the desire to reduce costs is generally neither a permissible nor logical basis to restrict competition. See 41 USC Sec. 253.⁴⁵

Accordingly, when agencies are concerned that separate contracts lead to additional costs, the GAO recommendation appears to be that the proper course of conduct is not to limit competition, but rather to structure the Request for Proposal evaluation criteria such that the additional costs are taken into account.*

If the agency desires to award a life cycle support contractor to an OEM on a sole source basis, all of the individual functions of the **total** package proposed contract should be analyzed in accordance with CICA to determine which of the functions can be justified for an award on a sole source basis. Thereafter, an analysis should be conducted to determine whether -- breaking the total package into its component parts -- non sole source functions can be reasonably bundled or consolidated with sole source functions using the legal principles set forth above.

Applying the above legal concepts to the hypothetical materiel management proposal, it is clear that the desire to have the benefits of “one stop shopping” alone will not justify the total package approach because administrative convenience is repeatedly struck down as a justification for bundling. This is especially the case since the desired approach will totally eliminate competition and not just inhibit it. That is, functions which most probably must be awarded sole source (configuration management, engineering support) are being consolidated with those that may be capable of performance by other contractors (stock control, storage, distribution and disposal of inventory, depot level maintenance). Since the cases interpreting CICA generally require the Government to use the least restrictive approach in defining its requirements, it may be that many of the functions will have to be unbundled from the total package unless logical, legitimate and supportable reasons can be advanced to conclude

⁴⁵ National Customer Engineering, B-25 1135, 93-1 CPD 225.

⁴⁶ Id.

otherwise. Traditional examples of logical, legitimate and supportable reasons include a documented need to maintain system integration or parts compatibility, development or implementation of an integrated system, or serious staffing problems plus a history of problems associated with past individual contracts.

Building on these examples, a legitimate case for bundling in the context of materiel management would seem to arise when the Government's minimum need is to achieve a true privatization or business process reengineering. In these initiatives, as discussed above, the Government divests itself of a particular function by shifting responsibility for the function -- including control and asset ownership -- to the private sector. Thus, in the case of a true privatization or business process reengineering, bundling could probably be justified as necessary to permit the government to satisfy its minimum needs. Any other result would force the Government to maintain management responsibility for the function, thereby precluding its ability to exit the subject business. Similarly, from the contractor's perspective, it is hard to conclude that a private party would be willing to accept contractual responsibility for full performance were its success dependent on the work of firms not subject to its control.

As a cautionary note, while the factors of control and asset ownership that underlie the concepts of privatization and reengineering are also relevant to bundling, this link cannot be pushed too far. In particular, attorneys should be careful to keep their analysis of "scope" for cost comparison purposes separate from their analysis of bundling under CICA. This is to say, it is possible for an attorney to conclude that a particular initiative is beyond the scope of OMB Circular A-76, but that the proposed bundling of functions is impermissible under CICA. In our hypothetical, for example, even if the Government's proposal was judged to fall outside the scope of all cost comparison requirements, a strong case under CICA would still have to be made to justify bundling distribution related activities with depot maintenance. In particular, the Government would have to make the case that the activities at issue were so interrelated that the award of multiple contracts would cause the Government to retain the role of systems integrator. Lacking such an explanation, GAO might require the Government to make multiple awards, as the burden of managing one or two additional contracts covering severable functions would not preclude the Government from exiting the logistics support business or from reengineering materiel management functions. Similarly, attorneys should be wary of proposals to bundle logistics support functions with procurement opportunities. Regardless of the magnitude of promised cost savings, such proposals are unlikely to withstand scrutiny under CICA.

E. SMALL BUSINESS

Outsourcing life cycle support for weapons systems will inevitably reduce contract opportunities for small businesses. This reduction will complicate the buying activity's task of meeting small business contracting targets set by the Department of the Army but will not, of itself, violate the Small Business Act or DOD specific legislation pertaining to small business contracting.

Neither the Small Business Act⁴⁷ nor the laws governing federal procurement-48 mandate the award of a specific number or types of contracts to small businesses. These laws, however, require contracting agencies to award a “fair proportion” of total government contracts to small businesses⁴⁹, and establish goals for contracting with small disadvantaged businesses (SDB).⁵⁰ Legislation specific to the Army, such as that establishing Test Programs for Modernization through Spares⁵¹, merely reaffirms the Government’s small business subcontracting policy set out in the Small Business Act.

The procurement regulations add no substantive requirements beyond what is stated in the statutes, except to **establish**⁵² a Government policy of contracting with small businesses to the maximum extent practicable. Other than to repeat statutory goals for **SDB** contracting, no specific dollar figures or percentage requirements are set out in the regulations. FAR policy on small business utilization, for example, requires only that small business concerns “be afforded an equitable opportunity to **compete**⁵³ for all contracts they can perform to the extent consistent with the Government’s interest.” Individual acquisitions or classes of acquisitions that have been set aside to meet the “fair proportion” **requirement**⁵⁴ can be replaced by small business contracting opportunities in other programs. **Likewise**, repetitive set-aside requirements can be avoided by a redefinition of the **Government’s** “requirement,” and good faith effort to provide alternate contracting opportunities.

Where small business contracting opportunities are lost with the government, they can be made up, in part, through subcontracts with the prime life cycle support contractors. For large companies, the extent of subcontracting opportunities will have already been addressed in the **firm’s** Comprehensive Small and Small Disadvantaged Business Subcontracting Plan which is incorporated by reference into its contracts.⁵⁶ Lack of good faith efforts to comply with subcontracting goals exposes the prime to the potential of liquidated damages.⁵⁷

⁴⁷ 15 USC 63 1, et seq.

⁴⁸ E.g., the Armed Services Procurement Act (10 USC 2302, et seq.)

⁴⁹ 15 USC 63 1,644.

⁵⁰ 10 USC 2323.

⁵¹ P.L. 104-201, section 312.

⁵² FAR 19.201.

⁵³ FAR 19.202-1. Similar language is found in the DFARS (Part 219) and the AFARS (Part1 9).

⁵⁴ FAR 19.502-1. The dollar value of any life support contract will almost always exceed the threshold for the total small business set-aside requirements of FAR 19.502-2; similarly, the partial set-aside requirements of FAR 19.502-3 will be inapplicable so long as the contracting officer determines that the requirement is not severable.

⁵⁵ DFARS 2 19.50 1.

⁵⁶ **FAR** policy requires agency consent to subcontracts when the subcontract work is complex, the dollar value is substantial, or the government’s interest is not adequately protected by competition and the type of prime contract or subcontract. FAR 44.102. Circumstances meeting these criteria will be present in many life cycle support type contracts.

⁵⁷ 15 USC 637(d)(4)(F).

F. FISCAL CONSIDERATIONS

If the contractor and contracting authority propose funding life-cycle support through the use of operation and maintenance (O&M) dollars as opposed to Defense Business Operation Funds (DBOF) (now Army Working Capital Fund (AWCF)), several issues arise. The first issue is whether there is a purpose problem with the proposed use of funds. In the instant case, so long as the contracting authority intends to use O&M for logistics support, as opposed to procurement or an RDT&E type effort, there would appear to be no purpose problem. Second, as a matter of acquisition policy, the “completeness” of the contractor’s proposal comes into play. **Here, the issue is whether the subject weapon system will remain dependent upon DLA for support, or whether sustainment of the system will become the sole responsibility of the contractor.**

Related to this second question is an overarching issue concerning the survival of the AWCF system. Two considerations are particularly important. First, if sustainment of the weapon system, at least in part, is to remain a DLA responsibility, complications arise concerning the interface between the logistic support systems of DLA and the contractor. In consequence, attorneys faced with such an issue should verify coordination between personnel in the procurement and logistics communities.

Second, consideration should be given to the impact of a particular privatization initiative on systems that would remain part of the AWCF system. In this regard, AWCF charges for overhead are directly related to the number of systems that participate in the revolving fund. The defection of a sizable system could, on its own or by triggering the defection of other systems, raise substantially the overhead charge assessed against systems remaining in the AWCF. Similarly, the defection of a significant system from the AWCF could impede the AWCF’s effort to expand and modernize -- activities requiring an infusion of capital for support.

Again, in light of these policy concerns, attorneys faced with a proposal to fund life-cycle support with O&M dollars, should inform their MACOM, and ensure at their level that proper coordination is made with both the logistics and financial management and comptroller communities.

G. ANTITRUST

Antitrust issues potentially arise when a team of three to four large Fortune 500 type contractors propose complete (“end to end”) life cycle support for a major Army weapon system. Each contractor is an original equipment manufacturer (OEM) for at least one major component of the weapon system.

The federal antitrust laws are the chief source of competition conduct standards affecting contractor teaming efforts, to include joint venture enterprises. The principal statutory and regulatory sources of these conducts standards are: Section 1 of the Sherman Act (15 USC 1), Section 2 of the Sherman Act (15 USC 2), Section 7 of the Clayton Act (15 USC 1 8), and

Section 5 of the Federal Trade Commission Act (FTCA) (15 USC 4 1-58), and the enforcement guidelines of the Department of Justice (DoJ) and Federal Trade Commission (FTC).⁵⁸

Also applicable, but less well known, are a number of federal procurement statutes and regulations. These sources make clear that the antitrust statutes and related case law fully apply to the formation and operation of joint enterprises by government contractors. In this sense, public procurement policy recognizes the benefits that teaming arrangements potentially offer by allowing contractors to pool resources.⁵⁹ But at the same time, there is nothing in statute or regulation to suggest that government contractors are exempt from the antitrust laws. This is evidenced by Section 9.604 of the FAR which provides that “nothing in this subpart authorizes contractor team arrangements in violation of antitrust statutes.” And, it is further evidenced by FAR provisions requiring contractors to certify that they have not colluded with competitors in preparing bids on government contracts.⁶⁰ Moreover, while the antitrust laws are aimed at the conduct of private parties, government personnel are directed to assist the antitrust agencies in the enforcement of these laws.⁶¹

An important insight for Army attorneys to keep in mind is that the hypothetical described above raises antitrust issues in a context different from the more familiar situation of a merger or acquisition. Whereas the hypothesized teaming arrangement contemplates review under Section 1 of the Sherman Act, mergers are covered by Section 7 of the Clayton Act, which prohibits acquisitions if their effect “may be substantially to lessen competition, or [to] tend to create a monopoly ...” 15 U.S.C. § 18 (1982). Also worth noting, is the different procedures by which the antitrust agencies become involved in investigating a teaming arrangement versus reviewing a merger. With respect to the former, the antitrust agencies tend to rely on leads provided by other government agencies or private parties. By contrast, in the merger and acquisition context, it is the merging parties themselves who are required to provide the antitrust agencies with information on their planned transaction. The obligation to provide such information comes from the Hart-Scott-Rodino (HSR) Antitrust Improvements Act of 1976⁶² which requires the merging parties to notify the FTC and DoJ before completing certain large dollar transactions.⁶³ In practice, however, despite these

⁵⁸ This section draws from, William E. Kovacic, *Antitrust Analysis of Joint Ventures and Teaming Arrangements Involving Government Contractors*, 58 ANTITRUST L.J., 1059-1 115 (1990).

⁵⁹ See e.g., FAR Section 9.602.

⁶⁰ . See FAR Sections 3.103- 1 and 52.203-2.

⁶¹ See 10 U.S.C. 2305 (b)(9) requiring a bid or proposal evidencing a violation of the antitrust laws to be referred to the Attorney General for appropriate action; FAR 3.3--**Reports** of Suspected Antitrust Violations, stating that “[c]ontracting personnel are an important potential source of investigative leads for antitrust enforcement and should therefore be sensitive to indications of unlawful behavior by offerors and contractors

⁶² Section 7A of the Clayton Act, 15 U.S.C. §18A.

⁶³ The significance of the HSR is that it creates mandatory waiting periods during which the parties may not close a proposed transaction and conduct joint operations. In transactions, other than cash tender offers, the waiting period is thirty days (fifteen days for cash offers). Prior to the expiration of this initial waiting period, the antitrust agency “cleared” to review the transaction may request additional information from the parties pertaining to the transaction. Under the HSR Act, such “second requests” for information extend by twenty days the waiting period during which a proposed transaction cannot be closed. These extensions to the waiting period, however, do not begin to run until

procedures, challenges to defense industry mergers occur rarely. Thus, in the history of the Clayton Act *only* four such cases have actually been litigated in federal court.⁶⁴ In all four cases, the courts concluded that there were substantial risks of adverse effects on competition and entered injunctions prohibiting the proposed acquisitions. During the same period, hundreds of defense industry mergers were allowed to proceed without antitrust challenge.

Reviewing Teaming & Joint Venture Arrangements. As mentioned, the primary provision of the antitrust laws applicable to teaming and joint venture arrangements is Section 1 of the Sherman Act.⁶⁵ Importantly, however, Section 1 does not condemn categorically all such arrangements. Instead, Section 1 is used to attack bid-rigging or market allocation schemes characterized as joint ventures. But, at the same time, case law interpreting Section 1 also recognizes the need of co-venturers sometimes to impose restrictions on one another to facilitate a legitimate cooperative enterprise. Restrictions used for this purpose are unobjectionable as a matter of antitrust law.⁶⁶

For the purposes of this white paper, the main question raised by Section 1 is whether the proposed collective effort represents an efficiency-enhancing integration of economic functions or a disguised effort to restrict output without any redeeming efficiency consequences. As the Supreme Court opined in Broadcast Music Inc. v. Columbia Broadcasting System, Inc., the key issue is whether the questioned arrangement “facially appears to be one that would always or almost always tend to restrict competition and decrease output” or is meant to “increase economic efficiency and render markets more, rather than less, competitive.” 441 U.S. 1, 19-20 (1979). Proceeding from this analysis, the trend in antitrust cases is to regard *as per se* illegal unadorned agreements to fix prices, rig bids, or allocate contract awards. On the other hand, collective efforts presenting plausible efficiencies are treated under a “rule of reason” in which the legal conclusion reached varies with the degree of potential anticompetitive danger and the strength of the claimed efficiency explanations.

Applying these standards to our suggested hypothetical, the core issue becomes whether the contractors are able to justify their collective effort on efficiency grounds. Practically speaking, this means asking whether the product or service offered by the contractor team would be unavailable but for the proposed collective effort. Or, put differently, the question becomes whether the proposed joint venture represents an effort to forgo independent

the merging parties are in “substantial compliance” with the government agency’s request for additional information. Generally speaking, if the antitrust agency does not challenge a merger before the HSR waiting period expires, it is quite unlikely that the agency will choose to sue at a later date to reverse or alter the transaction.

⁶⁴ The four cases are: Grumman Corp. v. LTV Corp., 522 F. Supp. 86 (E.D.N.Y.), *aff’d*, 665 F.2d (2d Cir. 1981), FTC v. PPG Industries, Inc., 628 F. Supp. 881 (D.D.C), *aff’d in part*, 798 F.2d 1500 (DC. Cir. 1986), FTC v. Imo Industries Inc., 1992-2 Trade Cas. (CCH) § 69,943 at 68,555 (D.D.C. Nov. 22, 1989), FTC v. Alliant Techsystems Inc., 808 F. Supp. 9 (D.D.C. 1992).

⁶⁵ 15 U.S.C. § 1 (1982).

⁶⁶ . See e.g., NCAA v. Board of Regents, 468 U.S. 85 (1984); Northrop Corp. v. McDonnell Douglas Corp. 705 F.2d 1030, 1049-54 (9th Cir.), *cert denied*, 464 U.S. 849 (1983).

bidding, or the submission of a separate unsolicited proposal, in favor of a joint proposal through which the contractors will allocate work and profits.

If presented with a teaming arrangement, attorneys should also consider the effects of such arrangements on competition at sub-tier contracting levels. At issue is a concern that teaming arrangements serve in effect to create a vertically integrated company capable of satisfying some or all of the inputs for their products or services internally. While this is not *per se* undesirable, attorneys should look to ensure that any contract awarded to the team contain adequate safeguards to ensure that sub-systems, components and the like be purchased from the most efficient source. This means, where appropriate, going out of house to purchase an item from a subcontractor that is not part of the prime contract team. Similarly, attorneys should look out for situations where the creation of a teaming arrangement would make the team both a competitor with and supplier to another firm or team with respect to the prime contract.

Because of the sensitivity of these matters and the potential involvement of the antitrust agencies, Army attorneys should alert their MACOM upon learning of a teaming or joint venture arrangement that appears to raise issues similar to those discussed above. The MACOM will follow-up as appropriate and coordinate with DA.

H. SUMMARY OF LEGAL ISSUES AND RECOMMENDATIONS

1. There is insufficient detail in the hypothetical to address the fiscal issues of the proposal.

2. Small business aspects must be addressed in the acquisition plan.

3. **Whether the** materiel management services can be combined into one contract depends upon the ability of the government to demonstrate a need to maintain overall system integration, unify responsibility for deficiencies, and improve overall operations. Convenience is not a sufficient justification, in and of itself, for combining services into an omnibus contract. A sole source to the Original Equipment Manufacturer (OEM) would have to be justified on the basis of lack of technical information, need for configuration management or engineering services only available from the OEM, or other reasons. If a team of contractors sought to provide the materiel management services, antitrust issues would have to be addressed, and coordinated with the DoJ.

4. **The** fact that a part of the materiel management services have been directed to move under BRAC to a specific site does not preclude consideration of a materiel management privatization proposal as long as management and oversight of the function move as directed and the move does not violate the intent of the recommendation. Political risk increases as the size of the function due to move under BRAC is privatized because the gaining location, and its representatives, have been expecting an increase in local employment.

5. The depot maintenance piece of the proposal must be separately evaluated for core logistics and impact on the Department's ability to contract out no more than 40% of funds provided for depot maintenance. If the depot maintenance piece can be contracted after consideration of these factors, then a private public competition should be commenced for that piece only.

6. With regard to whether OMB Circular A-76 and the related DOD statutes apply to the proposal, there is very little case law or legislative history to provide much guidance. The manager has a series of alternatives depending upon the risks and costs that the manager chooses to accept. A brief summary of the alternatives and the risks associated with the alternatives, is as follows:

A. ~~Least Risk~~ Congressionally legislated pilot project to permit the materiel management privatization proposal to move forward. This option minimizes any legal challenges but may be politically impracticable to persuade Congress to permit a test.

B. **Medium Risk A:** Perform an OMB Circular A-76 cost comparison, giving Congress the statutory required notices and documents. This is the proper option to take unless an exemption or waiver applies. This option minimizes possible legal and political attacks for failure to follow the cost comparison requirements, but is expensive and time-consuming. It also may open the manager to the delays and risks of employee appeals under the administrative appeals process, and of contractor protests to the GAO and courts. The costs and risks are **frontloaded** in that the delays and costs occur during the cost comparison process. A well done cost comparison **will** probably not be overturned as a result of litigation.

C. **Medium Risk B:** This approach assumes that either an exemption or a waiver applies to the proposal. It also assumes that the DOD statutes require cost comparison and MEO requirements in excess of the Circular but that those requirements can be met with an adequate cost analysis, but not necessarily an OMB Circular A-76 cost comparison. The DOD Congressional committees will be given notice of the analysis and reasons for the decision. This option bears some risk of litigation over the applicability of OMB Circular A-76, but saves the costs and delays inherent in the cost comparison. There will be costs in performing the adequate cost analysis. The manager could be required to perform a cost comparison should the decision not to perform a cost comparison be overturned.

D. **Medium Risk C:** This approach assumes that a materiel management proposal meets the tests for privatization or business process reengineering. The manager will document those facts and move to implement. This option bears a somewhat greater risk of litigation over the applicability of OMB Circular A-76, but saves some costs and delays inherent in the cost comparison. The manager could be required to perform a cost comparison should the decision not to perform the cost comparison be overturned. There must be a good cost analysis to justify the decision.

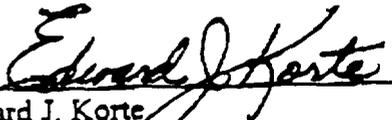
E. **High Risk**: This approach assumes that grounds for an OMB Circular A-76 exemption exist. Readers of the **Diebold** case and the statutory history of 10 USC 246 1 may conclude that the DOD statutes require compliance with the Circular, and establish no additional requirements. When an exemption exists, there is no further notice required. This option bears a much greater risk of litigation over the applicability of OMB Circular A-76. but saves some costs and delays inherent in the cost comparison. There are also risks of an adverse Congressional reaction and the potential for an Antideficiency Act violation should an outside court determine that section 8015 of the FY 97 DOD Appropriations Act established additional requirements. The manager could be required to perform a cost comparison should the decision not to perform a cost comparison be overturned. There must be a good cost analysis to justify the decision. This option should not be used when an agency case by case waiver is contemplated.

IV. CONCLUSION

Materiel management outsourcing and privatization proposals are complex. They must first be carefully evaluated by managers for impact on readiness and economics. Then legal issues can be addressed. This White Paper represents an effort to develop a consensus on legal issues in an area in which there is little case law and piecemeal statutory language. It is not a silver bullet. Time and the ongoing dialogue among agencies, the legislature, the unions and the courts will eventually result in greater definition of the requirements for these outsourcing and privatization proposals. Even when a manager has determined that a proposal fulfills readiness and economic needs, and can be legally accomplished, that manager should consider the impact of the reaction **from** Congress and its constituents. A wise counsel would recommend projects, especially in the beginning, with the greatest possibility of success and the least adverse impact on people in order to demonstrate the benefits of the program. The necessity of accomplishing solid cost and technical justification for management decisions cannot be overstated. These projects must make sense, and the benefits must be verifiable, or we risk losing all flexibility.

**MATERIEL MANAGEMENT OUTSOURCING AND PRIVATIZATION
WHITE PAPER**

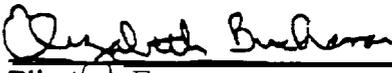
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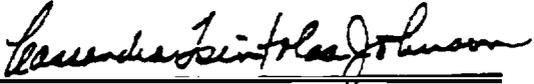

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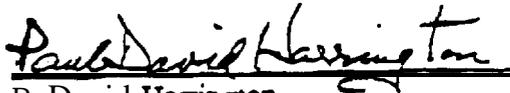

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APPENDIX I

Discussion of Comptroller General and Court Cases

Comptroller General Cases

Scope of Review

Generally, the GAO will decline to review an agency's decision whether to operate a commercial activity under contract by private enterprise or in-house using government facilities and personnel because those decisions are matters of executive branch policy. The GAO will, however, review A-76 decisions resulting **from** an agency's issuance of a competitive solicitation for the purpose of comparing the cost of private and government operations of the commercial activity to determine whether the comparison was faulty or misleading. *Crown Healthcare Laundry Services*, B-270827; B-270827.2, April 30, 1996, 96-1 CPD ¶207.

GAO reviews agency decisions to retain services in-house instead of contracting for them solely to ascertain whether the agency followed the announced "ground rules" for the cost comparison. GAO will recommend corrective action only where the record shows both that the agency did not follow the announced procedures and that this failure could have materially affected the outcome of the cost comparison. This applies GAO's standard rule requiring protesters to demonstrate that they were prejudiced by an agency's actions. *United Media Corporation*, B-259425.2, June 22, 1995, 95-1 CPD ¶289, at 3.

Agency's determination of the size of its government in nature staff is a management decision involving judgmental matters that are inappropriate for review by GAO. *PSC, Inc.*, B-236004, October 26, 1989, 89-2 CPD ¶380.

Interested party

GAO dismisses protest filed by union representing government employees challenging A-76 cost comparison because it is not an interested party. OMB Circular A-76 procedures provide for an appeals process for a "directly affected party" but do not authorize an appeal outside the contracting agency by a person not eligible to maintain an appeal under GAO's Bid Protest Regulations. *American Federation of Government Employees - Request for Reconsideration*, B-219590.3, May 6, 1986, 86-1 CPD ¶436; *Joseph B. Evans - Request for Reconsideration*, B-218047.2, March 11, 1985, 85-1 CPD ¶296 (dismissing protest filed by federal employee on same grounds).

Exhaustion & Timeliness

GAO will dismiss a protest challenging an A-76 cost comparison where the protester has failed to exhaust the administrative appeals procedures that agencies have established under FAR 7.307 for considering these types of challenges. *Professional Servs. Unified, Inc.*, B-257360.2,

July 21, 1994, 94-2 CPD ¶39 at 3; *Trans-Regional Manufacturing, Inc.*, B-245399, November 25, 1991, 91-2 CPD ¶492.

GAO will not review any objection to a cost comparison not specifically appealed to the agency. *Id.*, *Ameriko Maintenance Co. - Request for Reconsideration*, B-236764.2, November 7, 1989, 89-2 CPD ¶441 (protest challenging GSA's adjustments to in-house estimate made in response to initial administrative appeal dismissed where protester failed to exhaust administrative appeal challenging the adjustments taken. Arguably, this constitutes an exception to GAO's timeliness rule requiring a protest to be filed when an agency takes an action adverse to the protester's position.)

GAO rejects agency claim that a protest is untimely where the underlying appeal, although filed within the 15 day period under the agency's administrative appeals procedures, was not filed within the 10 days period under GAO's bid protest rules. It appears an administrative appeal is not equivalent to an agency-level protest for timeliness purposes. *Base Services, Inc.*, B-235422, August 30, 1989, 89-2 CPD 192.

Cost comparisons

a. *Procedural issues*

GAO will not entertain a protest challenging an agency's decision to perform services in-house where a competitive solicitation for cost comparison purposes has not been issued. *Services Alliance Sys.*, B-243306, March 18, 1991, 91-1 CPD ¶297; *Information Ventures, Inc.*, B-241441, January 29, 1991, 91-1 CPD ¶83 (dismissing challenge to agency's decision to continue performing majority of journal indexing work in-house where no competitive solicitation has been issued.)

An agency's decision to perform services in-house need not be based on the results of an A-76 cost comparison. The lack of such a study does not provide a valid basis upon which to object to an agency's action. *Techniarts Engineering*, B-243045, March 5, 1991, 91-1 CPD ¶250.; See also *Techniarts Engineering v. U.S.*, 51 F.3d 301 (D.C. Cir. 1995) (specific statute authorized maximum utilization of in-house assets); *Maron Inventories, Inc. - Reconsideration*, B-237651.4, July 20, 1990, 90-2 CPD ¶54 (internal FAA policy guidance established freeze on contracting out necessitating cancellation of solicitation and use of in-house capabilities.)

In an A-76 cost comparison, bidders and the government should compete on the basis of the same scope of work. An agency should adjust its in-house cost estimate if it was not based on the scope of work specified in the solicitation. *United Media Corporation*, B-259425.2, June 22, 1995, 95-1 CPD ¶289 at 5; See also *Crown*, 96-1 CPD ¶207.

Air Force's refusal to disclose historical cost data in A-76 procurement upheld where: (1) RFP contained comprehensive statement of work; (2) RFP included agency's best estimates of volume of work to be done in each major work category; (3) agency reasonably was concerned

that requested historical cost data would allow experienced offeror to estimate approximate amount of government's own price; and (4) historical data have not otherwise been made available. *Saxon Corp.*, B-236194; B-236194.2, November 15, 1989, 89-2 CPD ¶462.

An agency may properly ignore "government in nature" positions in a cost comparison, even though they constitute part of the planned in-house organization because the costs are essentially a "wash" as the positions will be needed whether or not the function is contracted out. *PSC, Inc.*, B-236004, October 26, 1989, 89-2 CPD ¶380; *Bay Tankers, Inc.*, B-227965.3, November 23, 1987, 87-2 CPD ¶500 (agency is free to make management decisions on appropriate staffing levels to accomplish a statement of work if they are not made in manner tantamount to fraud or bad faith and subsequent cost comparison is performed in accordance with established procedures.)

b. *Substantive issues.*

GAO rejects claim of flawed cost comparison and determines that offeror not prejudiced by Air Force's decision to add contract administration/quality costs (\$20 1,934) to Crown's bid under A-76 cost comparison solicitation for laundry services because the in-house cost proposal remained less expensive (\$424,740) absent the additional costs and essentially included similar costs. *Crown*, 96-1 CPD ¶207 at 7.

GAO rejects challenge to Air Force deduction of common costs (maintenance contracts for (GFE)) from in-house bid under A-76 cost comparison for audio-visual services where agency will retain responsibility for these costs whether services performed by contractor or in-house and agrees with Air Force that costs associated with converting contract photographers should be treated as a conversion differential cost because they expand an in-house activity and are not "one time" conversion costs. *United Media Corporation*, B-259425.2, June 22, 1995, 95-1 CPD ¶289 at 7. **This** case is noteworthy because GAO performed the calculations required by the A-76 handbook instead of relying on the accuracy of software used by the Air Force.

GAO has determined that a mock reduction-in-force (FUF) procedure is a proper method of calculating associated one-time conversion costs, such as severance pay, relocation costs, retraining costs and costs of supplementary personnel to process the RIF, and recognizes that such estimates involve complex and somewhat subjective judgments. *Intelcom Support Services, Inc.*, B-234488.2, August 7, 1989, 89-2 CPD ¶109 at 4.

The use of a small disadvantaged business set-aside to conduct an A-76 cost comparison is not improper provided the usual criteria for setting aside the procurement are met. *Government Contracting Resources*, B-2439 15, August 15, 1991, 91-2 CPD ¶153, footnote 1; *Logistical Support, Inc.*, B-234621, May 24, 1989, 89-1 CPD ¶500.

Developing agency's in-house estimates based on actual average usage figures are more accurate and more appropriate than commercial estimating guides suggested by protester. *Alltech, Inc.*, B-237980, March 27, 1990, 90-1 CPD ¶335 (Corps of Engineer's reliance on

average dollar costs to haul dredged materiel from two previous contracts in developing in-house estimate upheld where that method was specifically endorsed and reviewed by USAAA.); *EPD Enterprises, B-236303*, October 30, 1989, 89-2 ¶393 (upholding Marine Corps' prorated allocation of operation, depreciation and maintenance expenses associated with use of bulldozer based on historical work and shop repair orders and vehicle fuel reports).

GAO dismissed protest allegation that Army's in-house estimate failed to include additional employee benefit costs of converting temporary employees into permanent status dismissed as untimely raised. *PSC Inc., B-236004*, October 26, 1989, 89-2 CPD 380 at fn. 3.

Service Contract Act

The fact that federal employees are not subject to the SCA and the applicable wage determinations does not constitute a legally impermissible competitive advantage for the government. There is no requirement in the A-76 cost comparison "ground rules" to include a factor equalizing such inherent relative advantages and disadvantages of governmental and commercial entities. *Inter-Con Security Sys., Inc., B-257360.3*, November 15, 1994, 94-2 CPD ¶187, fn. 7; *Ameriko Maintenance Co., B-243728*, August 23, 1991, 91-2 CPD ¶191; *Paige's Sec. Servs., B-235254*, August 9, 1989, 89-2 CPD ¶118 (no requirement to neutralize advantage from use of military personnel).

Performance bonds

GAO denies protest claiming that performance bonds in A-76 cost comparison creates an unfair advantage for the government because it does not need to include bonding costs in its in-house cost estimate. Although government and offerors must compete on the same statement of work, they may be subject to different legal requirements in obtaining or performing the contract that may cause the commercial firm to suffer a cost disadvantage. The fact that the government may have a cost advantage due to its self-insurance capability does not make the cost comparison defective. Nothing limits the government's right to require bonds in cost comparison situations to the same extent as authorized in other procurements. *J&J Maintenance, Inc., B-239035*, July 16, 1990, 90-2 CPD ¶1735; *Phillips Cartner & Co., Inc., B-235666 B-235667; B-235668*, September 6, 1989, 89-2 CPD ¶217 (denying challenge to indemnity and insurance provisions).

Liquidated damages

Inclusion of liquidated damages provision for nonperformance in A-76 solicitation issued by VA for laundry services upheld where amount deducted represents as nearly as possible the cost of the services not provided. There is no requirement that an A-76 cost comparison include a factor to equalize the competitive position of the government and commercial offerors with regard to potential deductions for defective performance. *Crown Management Servs. Inc., B-233365.3*, September 20, 1989, 89-2 CPD ¶249; *Bay Tankers, Inc., B-227965.3*, November 23, 1987, 87-2 CPD ¶500.

Exercise of options

GAO rejects claim that an agency is obligated to perform a cost comparison and determine that it would be more economically advantageous to resolicit for a requirement rather than exercising an option in an existing contract awarded pursuant to A-76 procedures. *Satellite Services - Reconsideration*, B-252009.2, March 24, 1993, 93-1 CPD ¶264.

Cancellation of solicitation

Agency's decision to cancel a solicitation, rather than award a contract under A-76 cost comparison procedures, held reasonable because of (1) uncertainty regarding budgetary constraints; (2) significant alterations of the government furnished equipment list and (3) likely workload reductions caused by reorganization. Source *AV, Inc.*, B-241 155, January 25, 1991, 91-1 CPD ¶75.

Protest sustained where GSA's decision to cancel solicitation and perform services in-house because of: (1) the magnitude of the contract, (2) performance problems with the existing contractor and (3) cost - held unreasonable where internal agency memorandum indicated that the contracts would have been awarded if there had been adequate competition (i.e., more than 1 offer). *Griffin Services, Inc.*, B-237268.2, June 14, 1990, 90-1 CPD ¶558.

FOIA

An agency may refuse to disclose historical cost data in A-76 procurement where the agency is reasonably concerned that the requested historical cost data would allow experienced offeror to estimate approximate amount of government's own price. *Saxon Corp.*, B-236194; B-236194.2, November 15, 1989, 89-2 CPD ¶462.

Ambiguous specifications

GAO rejects claim of ambiguous specifications in an A-76 cost comparison solicitation for grounds maintenance services ruling that the Air Force provided all information in its possession; that the information provided adequately described the work requirements and that an agency is not required to obtain historical information for inclusion in an IFB. *ANV Enterprises*, B-270013, February 5, 1996, 96-1 CPD ¶40.

OMB Circular A-76 requires agencies to prepare in-house cost estimates on the basis of most efficient and cost effective in-house operation (MEO) needed to accomplish the requirements. While sufficient information must be provided to bidders to allow intelligent competition, agencies are not required to disclose the basis of their cost estimates or provide bidders with historical data concerning staffing levels, if the solicitation provides sufficient information descriptive of the agency's requirement. *Ameriko Maintenance Co.*, B-243728, August 23, 1991, 91-2 CPD ¶191 at 3; *Paige's Sec. Servs.*, B-235254, August 9, 1989, 89-2 CPD ¶118; *Pacific Architects & Eng'rs*, B-212257, July 6, 1984, 84-2 CPD ¶20.

Court Cases

Judicial review

Court of Appeals concludes the Army's decision to contract-out food services is not matter committed to agency's discretion and is subject to judicial review where underlying statutes (10 U.S.C. §2462), OMB Circular A-76 and regulation governing DOD Commercial Activities Program, 32 C.F.R. 169, contain measurable, objective standards limiting an Army's discretion in determining most economical way to procure commercial services. Court distinguished decisions issued by the Third and Eleventh Circuits, cited below, because they dealt with earlier, less-stringent version of Circular A-76 and improperly focused on the broad discretion typically exercised by the agency involved (i.e., the Army) rather than analyzing the statute involved and determining whether it provided standards by which to govern the agency's actions. *Diebold v. U.S.*, 947 F.2d 787,789, 808 (6th Cir. 1991); *Diebold v. U.S.*, 961 F.2d 97, (6th Cir. 1991) (denying petition for rehearing en banc.); *CC Distributors, Inc., v. United States*, 883 F.2d 146 (D.C. Cir. 1989) (Concluding regulation governing DOD Commercial Activities Program, 32 C.F.R. 169, provides judicially manageable guidelines to review Air Force's determination that a particular activity is governmental function.)

Court of Appeals concludes Administrative Procedure Act does not afford union and government employees a judicial forum to contest cost-analysis studies and evaluations that formed basis of Army's decision to contract out stevedoring operations because (1) such managerial decisions are committed to agency discretion by law and the statutes and regulations implicated (5 U.S.C. §301 et. seq.; OMB Cir. A-76; DOD Directive 4100.15) lack discernible guidelines against which a court may analyze an agency's decision; (2) the decision involves military and managerial choices inherently unsuitable for consideration by the judiciary (separation of powers considerations); and (3) the contracting out decision presents issues of a factual, rather than of a legal, nature requiring exercise of specialized knowledge and expertise. *Local 2855, AFGE (AFL-CIO) v. U.S.*, 602 F.2d 574 (3rd Cir. 1979); *AFGE v. Brown*, 680 F.2d 722,726 (11th Cir.1982), cert. denied, 459 U.S. 1104, 103 S.Ct. 728 (1983) (same result based on analysis of §806(a) of DOD Authorization Act of 1980, prohibiting circumvention of personnel ceilings and requiring congressional notification of study and certification of in-house calculations.); *AFGE v. Hoffmann*, 427 F.Supp. 1048, 1079-82, 1085 (N.D. Ala. 1976) (same result; even if agency action were subject to review, the scope of that review under Administrative Procedure Act would be limited to determination whether there was a rational and defensible basis for agency's actions.)

District court concludes it has jurisdiction to review Navy decision to resolicit bids from private contractors for fire fighting services under commercial activity study because decision to issue a second IFB to correct ambiguous specifications was matter of interpreting federal statute and its implementing regulations, was not inherently military or connected with either national defense or foreign policy except tangentially and union bringing suit on behalf of government

employees was “fairly comparable” to a disappointed bidder situation. *International Association of Firefighters, Local F-100 v. U.S. Department of the Navy*, 536 F.Supp. 1254, 1260 (D.C. R.I. 1982)

Standing (contractors)

Court of Appeals reverses lower court and finds that contractors operating engineer supply stores have constitutional and prudential standing to challenge Air Force’s decision to convert those stores to government-operated functions without cost comparison based on the loss of an opportunity to compete for those contracts and §1223 of the National Defense Authorization Act of 1987 which seeks to protect contractors by eliminating biases in the contracting out process favoring in-house performance. *CC Distributors, Inc., v. United States*, 883 F.2d 146 (D.C. Cir. 1989).

Court of Appeals affirms lower court’s ruling that unions representing civil service mariners and employees of unsuccessful bidders under Navy procurement to contract out operation of government-owned oceanographic ships lack standing to challenge violations of the Service Contract Act because the injury, loss of present or future jobs, is neither traceable to the omission of a wage determination **from** the contract nor fairly redressable by the contract remedy, resolicitation, sought by the union. *National Maritime Union of America v. Commander, Military Sealift Command*, 824 F.2d 1228 (D.C. Cir. 1987); *National Maritime Union of America v. Commander, Military Sealift Command*, 632 F.Supp. 409 (D. D.C. 1986) (predecessor case.)

Court concludes union representing employees lacked prudential standing under OMB Circular A-76 to challenge NASA’s reassignment of work from union employees to in-house workforce without comparative cost analysis because the “immediacy of interest” of employers (i.e., union) was not identical to the employees’ interest which indicated that Congress intended employees, as directly-intended beneficiaries, to be relied upon to challenge agency disregard of the law, as opposed to unions as potential peripheral beneficiaries. *Motion Picture Laboratory Technicians v. NASA*, 587 F.Supp. 1467 (D.C. Ill. 1984).

Standing (unions/federal employees)

Court of Appeals reverses lower court and holds that employees and air traffic controllers association have prudential standing to challenge FAA’s decision and implementation of plan to privatize level 1 air traffic control towers under the Office of Federal Procurement Policy Act Amendments (OFPPAA) where the interests asserted by plaintiff, ensuring the FAA does not privatize inherently governmental functions, is an interest expressed in the statute’s legislative history. Case remanded to district court for determination whether the individual plaintiffs and union meet constitutional and associational standing requirements, respectively. *National Air Traffic Controllers Association v. Pena*, 1996 U.S. App. LEXIS 8258, (6th Cir. 1996); *Lodge 1858, AFGE v. Paine*, 436 F.2d 882 (D.C. Cir. 1970) (holding employees and union challenging

workforce reduction in non-A-76 case have standing to challenge NASA's employment of contract employees where number of contract employees is fixed by statute.)

On remand, district court denied defendant's motion to dismiss and determined that the individual plaintiffs met constitutional standing requirements because they alleged a concrete injury, the loss of their current jobs, which was impending given that the FAA had begun implementing its plan to privatize level I air traffic control towers. The court determined that the union satisfied the associational standing requirements because (1) its members had standing to sue in their own right; (2) the interests it sought to protect - protection of union members' jobs - were germane to the organization's purpose; and (3) neither the claim asserted nor the relief requested required the participation of the individual members in the lawsuit, that is, determination whether the FAA violated OMB Circular A-76 and request for declaratory and injunctive relief does not depend on the individual plaintiffs' circumstances. Parties ordered to brief exhaustion issue. *National Air Traffic Controllers Association v. Pena*, 944 F.Supp. 1337 (N.D. Ohio 1996).

Court of Appeals affirms lower court's ruling that unions lack prudential standing to sue the Army over decision to contract out logistics services previously provided by federal employees under OMB Circular A-76 or section 1223(b) of the National Defense Authorization Act (NDAA) of 1987 because interest asserted, preservation of jobs, inconsistent with or marginally related to the "zone of interests" to be protected by the relevant statutes. The statutes analyzed included: the Budget and Accounting Act of 1921 and the Office of Federal Procurement Policy Act Amendments of 1979, the authorities under which OMB Circular A-76 was promulgated, that sought to increase efficiency in government operations, contemplated the loss of federal jobs without affording discharged employees protection or a remedy and espoused a federal policy of relying on the private sector; and §1223(b) of the NDAA that sought to protect government contractors against built-in bias favoring in-house performance of services. The unions also lacked standing as disappointed bidders because they never bid on a contract. *National Federation of Federal Employees v. Cheney*, 883 F.2d 1038 (D.C. Cir. 1989); *AFGE v. Hoffmann*, 427 F.Supp. 1048, 1079-82 (N.D. Ala. 1976) (former employees lack prudential standing and constitutional standing to sue BMDO due to lack of causation between agency action and injury suffered where (1) employees' inability to perform work contracted out inconsistent with claim that employees could "bump and retreat into" jobs if retained in-house and (2) no showing that work would be performed in-house absent challenged contracts.)

Court concludes union representing civil service employees who performed fire fighting services was in effect an unsuccessful bidder defending low bid (i.e., in-house estimate) prepared and submitted by Navy employees and had prudential standing to challenge Navy's decision to resolicit bids under ASPR which reflected Congressional intent that commercial and industrial functions be performed at the lowest possible cost to the Government and which could benefit civil service employees currently performing the function. Ultimately, court determines Navy had rational and defensible basis to resolicit bids to correct ambiguity in original solicitation. *International Association of Firefighters, Local F-1 00 v. U.S. Department of the Navy*. 536 F.Supp. 1254, 1264 (D.C. R.I. 1982)

Court of Appeals affirms lower court's ruling that former government employees and unions representing said employees lack prudential standing to sue Air Force over decision to contract out food service operations under the Service Contract Act, which protects employees of private contractors, and the Veteran's Preference Act, which provides a preference for veterans only over other federal employees, because their interest in preserving their jobs was not in the zone of interests to be protected by these statutes. *American Federation of Government Employees, Local 1668 v. Dunn*, 561 F.2d 13 10 (9th Cir. 1977); *American Federation of Government Employees, AFL-CIO v. Stetson*, 640 F.2d 642 (5th Cir. 198 1); *Local 2855, AFGE (AFL-CIO) v. U.S.*, 602 F.2d 574,584 (3rd Cir. 1979) (nothing in civil service statute or regulations prohibits the abolishment of positions held by veterans or other civil servants and contracting out the work previously performed by them.)

Ripeness/Exhaustion

District court determines that case challenging FAA's privatization of Level 1 air traffic control towers is ripe where (1) many **FAA** level 1 employees have lost their jobs and for those still employed the loss of their jobs is "certainly impending"; (2) the factual record is **sufficiently** developed for adjudication since the plan has been approved and is being implemented and the only questions presented are legal; and (3) withholding judicial relief until every affected employee loses his or her job would cause hardship to plaintiffs whose careers are a stake. *National Air Traffic Controllers Association v. Pena*, 944 F.Supp. 1337 (N.D. Ohio 1996).

Court of Appeals **affirms** lower court ruling that Air Force employees' failure to exhaust administrative remedies, promulgated by Civil Service Commission to determine whether the so-called Pellerzi Standards governing whether a contract was a personal services contract had been violated, precluded them from obtaining judicial review on that issue where there has been no showing that resort to these procedures would be inadequate or futile. *American Federation of Government Employees, Local 1668 v. Dunn*, 561 F.2d 13 10 (9th Cir. 1977); *Local 2855, AFGE (AFL-CIO) v. U.S.*, 602 F.2d 574,584 (3rd Cir. 1979)

Cost comparison

Court of Appeals concludes U.S. Information Agency could decide to produce television broadcasts in-house, rather than through the use of a commercial source, without comparing costs of each alternative as required by the Economy Act or OMB Circular A-76 because specific requirements of **TV Marti** Act called for "maximum utilization" of agency resources and controlled over those of the Economy Act, a statute having general applicability. *Techniarts Engineering v. U.S.*, 51 F.3d 301 (D.C. Cir. 1995).

Without addressing if union representing civil servants has standing, court of appeals finds decision by Chief of Naval Operation to reverse administrative appeals official and award A-76 solicitation for maintenance and repair work to contractor reasonable interpretation of Navy's A-76 regulations despite regulatory provision indicating appeal decisions were final and not subject to review because CNO retained ultimate authority, under regulations, over commercial activities program and contracting out decisions. *LAMAW, Naval Air Lodge 1630 v. Secretary of Navy*, 915 F.2d 727 (D.C. Cir. 1990)

Without addressing if unions representing civil servants and contract employees have standing, court of appeals finds Navy's refusal to grant second administrative appeal to challenge its decision to re-award a contract to operate government-owned ships to another bidder after incorporating Service Contract Act reasonable where (1) the Navy's cost estimate and the gap between the Navy's estimate and the bidder's proposals had not materially changed from *prior* solicitation and (2) the unions seeking the appeal had both the incentive and opportunity to appeal the original award but had failed to do so. Court also finds Navy's decision to extend right of first refusal for employment openings to permanent, but not temporary, employees reasonable given the agency's fear that doing so would deprive displaced permanent employees. *National Maritime Union of America v. Commander, Military Sealift Command*, 824 F.2d 1228 (D.C. Cir. 1987). *National Maritime Union of America v. Commander, Military Sealift Command*, 632 F.Supp. 409 (D.C.D.C. 1986) (predecessor case.); *Marine Transport Lines v. Lehman*, 623 F.Supp. 330 (D.C.D.C. 1985) (predecessor companion case; upholding agency decision to rescind tentative award to incorporate Service Contract Act provisions.)

FOIA

Court upholds Army's decision to temporarily withhold, under the civil discovery privilege of exemption 5 , historical cost data that will support in-house estimate until after bid opening and contract award where disclosure would enable an informed bidder to make a closer approximation of the government's bid which may chill competition and place the Army at a competitive disadvantage in bidding to continue doing the work in-house and may discourage commercial firms from taking the initiative to come forward with more innovative techniques for cutting costs. *Morrison-Knudsen Co. v. Department of the Army*, 595 F.Supp. 352 (D.C.D.C. 1984)

Property interest

Court rules former government employees lack property interest in employment lost through A-76 process so long as seniority and veterans' preference rights implicated as a result of reduction in force are observed. *AGFE v. Hoffmann*, 427 F.Supp. 1048, 1086 (N.D. Ala. 1976).

Labor Relations

Supreme Court rejects FLRA's interpretation of Civil Service Reform Act that IRS is required to negotiate with union during collective bargaining negotiations over proposed provision that would subject agency's "contracting out" decisions to grievance and arbitration procedures by adopting those procedures as the OMB Circular A-76 "internal appeals procedure." Court determines that FLRA's interpretation ignores the plain language of the management rights provision (Section 7 106(a)) - "nothing in this [Act] shall affect the authority of agency management officials in accordance with applicable laws ... to make [contracting out] determinations" - which supersedes the agency's obligation to bargain in good faith over grievance procedures under §7 12 1 of the Act. Court refuses to address whether circular is "applicable law" under management rights provision or "law, rule, or regulation" under the definition of grievance. *Department of the Treasury, Internal Revenue Service v. Federal Labor Relations Board*, 494 U.S. 922, 108 L.Ed.2d 914, 110 S.Ct. 1623 (1990). *Department of the Treasury, Internal Revenue Service v. Federal Labor Relations Board*, 862 F.2d 880 (D.C. Cir. 1988) (predecessor case)

Court of Appeals reverses the FLRA's conclusion, on remand from the Supreme Court, that OMB Circular A-76 is an "applicable law" subject to negotiation and holds that the circular qualifies as a government-wide rule or regulation under §7 117(a) and that the FLRA cannot require an agency to bargain over grievance procedures directed at implementation of the regulation where there is no preexisting legal right upon which the grievance can be based and the regulation precludes bargaining over its implementation or prohibits grievances concerning alleged violations. *U.S. Department of Treasury v. Federal Labor Relations Board*, 996 F.2d 1246, 1252 (D.C. Cir. 1993); *AFGE Local 134.5 and Department of the Army, Fort Carson*, 48 FLRA 168 (1993) (Authority adopts Court of Appeals conclusion that A-76 is a government-wide regulation and that proposals subjecting disputes over compliance with the circular under negotiated grievance procedure are nonnegotiable.)

Court of Appeals denies enforcement of FLRA order requiring Department of Health and Human Services to negotiate with union over provision requiring agency to comply with OMB Circular A-76 in making contracting-out decisions. Court concludes circular is not "applicable law" under management rights provision because it was an internal management directive of the Executive branch, it created no enforceable rights in third parties and provided no "law" for court to apply in adjudicating disagreements over its application. Court also concludes that the agency is not required to negotiate over union's proposal because it conflicts with the circular which qualifies as a government-wide rule or regulation, that is, official declarations of policy of an agency which are binding on officials and agencies to which they apply, by subjecting an agency's contracting out decisions to a grievance process external to the circular's appeals procedure. *U.S. Department of Health and Human Services v. Federal Labor Relations Authority*, 844 F.2d 1087 (4th Cir. 1988); *Defense Language Institute v. Federal Labor Relations Authority*, 767 F.2d 1398 (9th Cir. 1985) (union proposal requiring agency to correct all in-house cost estimate data in A-76 cost comparison improperly affected authority reserved to management to make contracting out decisions and was nonnegotiable.)