

LABOR RELATIONS AND CONTRACTING OUT REVERSING THE TIDE

"Americans want to 'get their money's worth' and want a Government that is more businesslike and better managed. The reinvention of Government begins by focusing on core mission competencies and service requirements. Managers must begin by asking some fundamental questions, like: why are we in this business, has industry changed so that our involvement or level of involvement is no longer required; is our approach cost effective and, finally, assuming the Government has a legitimate continuing role to play, what is the proper mix of in-house, contract and interservice support agreement resources . . . The OMB Circular A-76 Revised Supplement Handbook is designed to enhance Federal performance through competition and choice." Introduction, Notice of Transmittal Memorandum No. 15, to the OMB Circular No. A-76, "Performance of Commercial Activities, Revised Supplemental Handbook." April 1, 1996, 61 FR 14338.

I. WHY IS CONTRACTING OUT BECOMING SUCH A HOT ISSUE TODAY?

A. 1980s -- federal agencies' attempts to use Office of Management and Budget (OMB) Circular A-76 creates Congressional backlash - series of anti-A-76 protective statutes enacted (e.g., 10 USC 2461 and Public Law (PL) 99-661, Section 317).

B. 1990s.

1. Limited federal dollars--stagnant or declining agency budgets.

2. Bipartisan support for cutting down the federal government and making it leaner and more cost effective.

3. President's Reinventing Government Program.

a. March 3, 1993, President Clinton asked Vice President Gore to lead the National Performance Review (NPR), a campaign to reinvent government.

b. Phase I: Putting customers first; cutting red tape; empowering employees to get results; and cutting back to basics.

c. Phase II: Cutting Back to Basics - February 13, 1995, Privatization Resource Guide and Status Report (Draft).

"Basics means taking a hard look at what, the government does and determining what changes to make in federal programs and functions, if any;...moving the service delivery capability to the most effective provider....

In general, a refocusing and downsizing of federal activities will result." (Page 1).

"This is not a privatization exercise . . . This is a most cost effective alternative exercise. It would be irresponsible to do privatization for the sake of privatization. Privatization itself is not the goal. It's only a tool." Julia Stasch, GSA Deputy Administrator. (Page 9).

II. STATUTORY AND REGULATORY FRAMEWORK.

A. OMB Circular No. A-76, Performance of Commercial Activities, August 4, 1983.

B. OMB Circular No. A-76, Revised Supplemental Handbook (March 1996).

C. Office of Federal Procurement Policy Letter (OFPP Letter) 92-1, Inherently Governmental Functions (57 FR 45096, September 30, 1992). This sets the policy for Executive departments and agencies that certain functions are inherently governmental functions that must only be performed by Government officers and employees. The functions include those activities that require either the exercise of discretion in applying Government authority or the making of value judgments in making decisions for the Government. Governmental functions normally fall into two categories: (1) the act of governing, i.e., the discretionary exercise of Government authority; and (2) monetary transactions and entitlements.

D. Federal Acquisition Regulation Subpart 7.5, Inherently Governmental Functions, January 26, 1996, 61 FR 2628. This implements OFPP Letter 92-1. The premise is that it's a policy matter, not a legal determination, that a function is so intimately related to the public interest as to mandate performance by Government employees.

E. Federal Workforce Restructuring Act of 1994, PL 103-226, March 30, 1994. It requires the reduction of federal full-time equivalent positions (FTE) between 1994 and 1999 of approximately 272,900. Section 5(g) requires the President to take appropriate action to ensure that agencies not convert the work of employees included in the reduction target or the work of employees that accept a buyout to contract performance, unless a cost comparison demonstrates that there is a financial advantage to the Government.

III. RELATED STATUTES AND REFERENCES.

A. Conflict of Interest laws, 18 USC 201 et seq., generally prohibit any federal employee from engaging in official activities that could conflict with personal interests.

B. Procurement Integrity Act, 41 USC 423, governs the relationships between government officials and current or potential contractors.

C. Government Ethics Newsgram, Summer, 1995, Volume 12, No.2, U.S. Office of Government Ethics.

D. Chief Financial Officers Act of 1990, PL 101-576, November 15, 1990, provides new tools to improve the management of the Federal government by establishing Chief Financial Officers in 23 major Executive agencies as well as a new Deputy Director of Management and a Comptroller in the Office of Management and Budget, and establishing Federal accounting standards, integrate and modernize the Government's financial systems, and produce audited financial statements.

E. Government Performance and Results Act of 1993, PL 103-62, August 3, 1993, in response to the American public's "disdain for government and objections to

paying higher taxes," the Act improves the efficiency and effectiveness of Federal programs by establishing a system to set goals for program performance and to measure results in order to reduce waste, inefficiency and ineffectiveness in Federal programs.

F. Government Management Reform Act of 1994, PL 103-356, October 13, 1994, was enacted in response to both Congressional concern that the Federal Government be accountable for the spending of taxpayers' dollars and to the NPR's report, "From Red Tape to Results," that concludes that "those in positions of responsibility must have the information they need to make good decisions." It essentially expands the coverage of the 1990 Chief Financial Officers Act to provide for annual audited financial reports of all the activities, spending and revenues of 24 major Government departments and agencies reports; establishes pilot programs to create franchising operations that will consolidate administrative support services, improve competition and cut costs; and promotes electronic funds transfer for Federal wages, salaries, and retirement payments.

IV. HISTORICAL BACKGROUND.

A. In 1955, the Senate Select Committee on Small Business stated that government agencies should give high priority to eliminating competition with the private sector.

B. The Second Hoover Commission (1955) endorsed the policy of "Eliminating Government-operated services and functions that compete with private enterprise.

C. Bureau of the Budget Bulletin (BOB) 55-4 (1955) stated that the "public sector shall not carry on any commercial activity to provide a product or service for its own use, if such products and services can be obtained through ordinary business channels from private enterprise." Similar policy expressed in Budget Bulletins issued in 1957 and 1960.

D. Circular A-76 of 1966 issued for the first time which prescribed policy and implementing guidelines in BOB Bulletin 55-4 in a permanent directive.

E. The Circular underwent revisions in 1967 to clarify some provisions and to lessen the burden of work by agencies in implementation, and in 1976 to provide additional guidance on cost comparisons and prescribing standard cost factors for Federal employee retirement and insurance benefits.

F. Revised Circular A-76 issued in 1979 which included a Cost Comparison Handbook to ensure consistent and equitable cost comparisons and provisions for the protection of federal employees ("sunshine" access to reviews, appeals procedure, 10% cost differential favoring in-house performance, and requirement that contractor give right of first refusal to qualified Government employees).

G. Revised Circular A-76 issued in 1983.

V. HIGHLIGHTS OF CHANGES TO THE REVISED OMB CIRCULAR A-76 SUPPLEMENT.

A. **Cost comparison requirements.** Modifies and in some cases eliminates cost comparison requirements for recurring commercial activities and the establishment of new or expanded interservice support agreements.

B. **Listing of commercial activities.** Retains current listing of commercial activities attached to the August 1983 Circular A-76 and includes OFPP Policy Letter 92-1 guidance on what is "Inherently governmental functions." (See Supplement, Appendix 5).

C. **Reliance on the private sector.** Revision retains 1983 Supplement's requirements to contract new or expanded work, unless a cost comparison is conducted to support conversion to in-house or interservice support agreement performance. It also requires conversion to contract only when it's cost effective. It doesn't require conversion of in-house work to contract, as a matter of policy, without cost comparison.

D. **Exemptions from cost comparison.**

1. Circular itself exempts certain recurring commercial activities from cost comparison, including

mobilization requirements within the Department of Defense, the conduct of research and development and direct patient care activities in Government hospitals or other health facilities. The Revision clarifies this policy to permit exempt activities to be retained in-house or converted to or from in-house, contract or interservice support agreement performance, without cost comparison.

2. The list of exempted activities has been expanded to include national security activities, mission critical core activities and temporary emergency requirements. The determination of "core" functions is, fundamentally, a management decision.

E. Reduces reporting and other administrative burdens. Eliminates previously required study schedules and quarterly study status reporting as unnecessary and administratively burdensome. Agencies are still required to maintain an inventory of commercial activities with information on completed cost comparisons.

F. Waivers. Broadens an agency's authority to waive cost comparisons to convert to or from in-house, contract or interservice support agreement without cost comparison if it is found that (a) the conversion will result in a significant financial or service quality improvement and that the conversion will not serve to reduce significantly the level or quality of competition in the future award or performance of work or (b) there is a finding that the in-house or contract (in the case of a possible conversion from contract to in-house performance) offers have no reasonable expectation of winning a competition (for example, when an agency conducts a major independently conducted business analysis). Broadens the agency's authority to waive by delegating it down from the Secretary to the Assistant Secretary level. Within DOD this has been further delegated down to the Assistant Service Secretaries.

G. Provides for enhanced employee participation. Since the 1983 Supplement was silent on the subject, the revision clarifies employee participation opportunities and formalizes the requirement for agencies to consult with employees and their labor representatives for their full participation and involvement in the earliest

possible stages of the procurement process. Agencies are requested to afford employees and private sector interests an opportunity to comment on solicitations prior to the opening of bids. Revision also affords parties additional time to submit cost comparison appeals. **(See Chapter 1, Section G).**

1. Full participation in the development of performance standards, the Performance Work Statement (PWS), in-house management plan, Most Efficient Organization (MEO), and in-house and cost estimates, subject to the restrictions of the procurement process and conflict of interest statutes.

2. Upon issuance, a solicitation used in the conduct of the cost comparison will be made available to directly affected Federal employees or their representatives for comment. The employees or their representatives will be given sufficient time to review the document and submit comments before final receipt of offers from the private sector. Private sector offerors shall comment as provided by the Federal Acquisition Regulations.

3. Agencies shall make all relevant documents available for review as part of the administrative appeal process.

H. Performance standards. Though the 1983 Supplement did not permit conversion decisions to be based on the comparison of performance measures or standards, the revision does permit conversion to or from in-house, contract or interservice support agreement performance if the agency determines that performance meets or exceeds generally recognized performance and cost standards.

I. Eases transition requirements to facilitate employee placement. The revision authorizes the conversion of functions involving 11 or more FTEs to contract performance, without cost comparison, if fair and reasonable prices can be obtained from qualified commercial sources and all directly affected federal employees serving on permanent appointments are reassigned to other comparable federal positions for which they are qualified. This provision is limited to

competitive awards only. There is no requirement that restricts placement efforts within the federal employee's commuting area. **Note**, no commercial activity shall be modified, reorganized, divided or in any way changed for the purpose of circumventing the requirements of this provision.

J. The 10 FTE or Less Rule. The revision expands the 1983 supplement's rule that permits the conversion of a function to contract performance without cost comparison - even with adverse employee impacts - to the conversion of similarly sized activities to in-house or interservice support agreement performance, without cost comparison. The 10 FTE or Less Rule is a recognition that there is a break-even point where the cost of conducting the comparison is not likely to outweigh the expected benefits while cost comparisons at the 11-50 FTE levels do result in significant most efficient organization (MEO) and competition savings.

K. MEO Implementation. Requires agencies to develop a transition plan for each competitive solicitation. This facilitates agencies planning for employee placements and a more orderly transition of work to or from in-house, contract or interservice support agreement.

L. Post MEO Performance Reviews. Revision requires agencies to conduct Post-MEO Performance reviews on not less than 20% of all functions are retained or converted to in-house performance as a result of a cost comparison. This will ensure that the MEO was properly estimated and implemented and the work is being performed in accordance with the terms, quality standards and costs specified in the Performance Work Statement (PWS).

M. The streamlined cost comparison alternative. In addition to the generic cost comparison methodology, a streamlined cost comparison process has been developed for activities involving 65 FTEs or less. **Note**, management cannot modify, reorganize, divide or in any way change a commercial activity involving 66 or more FTEs for the purpose of using the streamlined cost comparison procedure.

N. **Source Selection.** Criticism levied against the 1983 Supplement was that it was too cost determinative and it relied too heavily on the low bid offer. The Revision allows for "best value" and "past performance" type concepts to be used in A-76 cost comparison process using competitive negotiation or source selection.

O. **Appeals.** The Revision extends to time frame for appeals to be submitted from 15 working days to 20. The agency may extend the appeal period to a maximum of 30 working days if the cost study is particularly complex; expands scope of appeals to include formal information denials, instances of clear A-76 policy violations, and clarifies that streamlined and sector specific cost comparisons are subject to appeal. Not accepted for appeal basis was an agency's decision to reorganize, that appeals be decided by another agency and agency's decision to conduct or not conduct a cost comparison.

P. **Right of First Refusal - Personnel Considerations.** Expands the Right of First Refusal first established by the 1979 Supplement. (**See Chapter 1, Section H**).

1. Adversely affected Federal employees are employees identified for release from their competitive level by an agency in accordance with 5 CFR Part 351 as a direct result of a decision to convert to contract, ISSA performance or the agency's MEO.

2. The right of adversely affected federal employees for first refusal for jobs created as a result of the decision to convert to contract or ISSA performance and for which they are qualified has been expanded to extend the right to existing and to subsequent contractor employees in the original or follow-on contracts, as provided for in Executive Order 12933, "Non-Displacement of Qualified Workers Under Certain Contracts."

3. Agencies should exert maximum efforts to find available positions for federal employees adversely affected by conversion decisions including priority consideration for available positions within the agency, establishing a reemployment priority list and an effective placement program, and paying reasonable costs

for training and relocation that contribute directly to placement.

VI. FEATURES OF THE A-76 PROCESS.

A. Exceptions to the OMB Circular A-76 cost comparison requirement to convert these activities to or from in-house, contract or ISSA.

1. National Defense of Intelligence Security.
2. Patient Care.
3. Core Capability.
4. Research and Development.
5. No satisfactory commercial source available.
6. Functions with 10 or fewer FTEs.
7. Meet or exceed generally recognized industry performance and cost standards.
8. Lower cost - as result of a cost comparison conducted with the Supplement procedures.
9. Temporary and emergency authorizations for in-house performance - when contractor defaults or is otherwise terminated, agencies should seek interim contract support, if feasible, otherwise, in-house or ISSA performance of a "contracted" activity may be authorized on a temporary and emergency basis.

B. Cost Comparison - Full Procedure (**Part I, Chapter 3**)

1. **Development of the Performance Work Statement (PWS) - (Section C)**. Defines what is being requested, the performance standards and measures, and time frames required. It provides the technical performance sections of the Request for Proposals (RFP), or Invitation for Bid (IFB), issued by the contracting officer.

2. **Development of the Quality Assurance Surveillance Plan (QASP) - (Section D)**. QASP describes

the methods of inspection to be used, the reports required and the resources to be employed with estimated work-hours.

3. Development of the Management Plan for the Most Efficient Organization (MEO) - (Section E).

Describes the Government's most efficient organization and is the basis of the Government's in-house estimates. It must reflect the scope of the PWS, should identify the organizational structures, staffing and operating procedures, equipment, transition and inspection plans necessary to ensure that the in-house activity is performed in an efficient and cost effective manner. Should include all initiatives and assumptions factored into developing the MEO.

4. Development of cost estimates and reviews by the agency's A-76 Independent Review Officer (IRO) - (Section I). Government's cost estimates are certified in writing as being in full compliance with the procedures and requirements of the Supplement. The PWS, Management Plan, QASP and all Government developed cost estimates with supporting documentation are forwarded to the agency IRO. (In Army's case, review is by U. S. Army Audit Agency).

5. Bids or proposals solicited from private industry - (Section H). All competitive methods of federal procurements provided for by the Federal Acquisition Regulation (FAR) are appropriate, including the sealed bid, two-step, source selection and other competitive qualification based or negotiated procurement techniques. A "best value" contract offer consideration is an acceptable criterion for selection.

6. Evaluation of bids and tentative decisions - (Section J). Evaluation of bids and tentative decision are made pending outcome of evaluation of bids for responsiveness, responsibility and resolution of possible administrative appeals of any appeals. For sealed bid procurements, the contracting officer opens the bids, including the Government's in-house cost estimate, and enters the price of the apparent low offeror on the Cost Comparison Form (CCF). The appeal process period begins when access to the completed CCF, and all supporting documentation, is provided to

affected parties for review, usually the day of the bid opening.

7. Public review and appeal period - (Sections J and K). Must be received within 20 calendar days after the date that all supporting documentation is made publicly available. The agency may extend to appeal period to a maximum of 30 days for a particularly complex cost comparison.

a. Basis will address specific questions regarding the agency's compliance with the requirements and procedures of the Circular, factual questions regarding agency justifications to waive a cost comparison (doesn't include right to appeal a decision not to issue a waiver, Chapter I, Section E4), or address specific questions regarding the costs entered by the Government on the applicable Cost Comparison Form. It will provide the rationale for questioning those items.

b. Identify specific instances of agency denials of information not otherwise protected by law or regulation. Demonstrate that the items appealed, individually or in the aggregate, would reverse the tentative decision.

c. An appeal can be submitted by an eligible appellant defined as federal employees (or their representatives) and existing Federal contractors affected by a tentative decision to waive a cost comparison; federal employees (or their representatives) and contractors that have submitted formal bids or offers who would be affected by a tentative decision to convert to or from in-house, contract or ISSA performance as a result of a cost comparison; or agencies that have submitted formal offers to compete for the right to provide services through ISSAs.

d. Agency A-76 Administrative Appeal procedures do not apply to questions concerning the selection of one contract offeror or another for competition with the in-house cost estimate; award to one contractor in preference to another; Government management decision involving the Governments certified in-house MEO, and the policies or procedures contained in the Circular and the Supplement.

e. The procedure does not authorize an appeal outside the agency or judicial review, nor does it authorize sequential appeals.

8. Decision to award contract or cancel solicitation - (Section K). The appeal procedure should provide for a final decision within 30 days of the appeal by the Appeal Authority.

9. Transition period - (Section E4d). Included in the Management Plan is the transition plan for the transition to or from current organizational structure to MEO, contract or ISSA performance, designed to minimize disruption, adverse impacts, capitalization and start-up requirements.

10. MEO or contract operational.

11. Post-MEO Performance Review - (Section L). When the MEO is selected as a result of the cost comparison, a formal review and inspection of the MEO should be conducted following the end of the first full year of performance. Post-MEO Performance Reviews will be conducted on not less than 20% of the functions performed by the Government as a result of a cost comparison. An annual list of Post-MEO Performance Review certifications will be made available to the public upon request. This list will identify the total number of cost comparisons completed since the issuance of the Revised Supplemental Handbook and the number of Post-MEO Performance Reviews completed.

C. Agency specific A-76 procedures can implement above general provisions and may include additional steps for undertaking A-76 cost comparison process.

D. Minimum threshold of defined costs that must be exceeded prior to the conversion to or from in house, contract or ISSA performance is established to ensure that the Government will not undertake a conversion for marginal estimated savings. The minimal cost differential is the lesser of 10% of the in-house personnel-related costs or \$10 million over the performance period. Factors such as decreased productivity, and other costs of disruption that cannot

be easily quantified at the time of the cost comparison are included in this differential. (**Part II, Chapter 2, Section 8**).

F. Streamlined Cost Comparisons for Activities with 65 FTE or Less. (**Part II, Chapter 5**).

1. Employees' participation and notification provisions are same as for full cost comparisons.

2. Upon notification of adversely affected Federal employees and publication of the tentative decision in the Commerce Business Daily to either contract, enter into an ISSA, or to retain the activity in-house, the A-76 Administrative Appeal process applicable to full cost comparisons will be initiated.

3. The Right-of-First-Refusal will be offered to employees adversely affected by the award.

VII. EXAMPLES OF RECENT CONTRACTING OUT/PRIVATIZATION INITIATIVES AT FEDERAL AGENCIES.

A. OPM training and investigations.

B. IRS.

C. DOE.

D. DOT-FAA.

E. DOD.

F. HUD.

G. GSA.

VIII. CURRENT CHALLENGES TO FEDERAL AGENCY CONTRACTING OUT/PRIVATIZATION INITIATIVES.

IX. THE FUTURE OF OMB CIRCULAR A-76 ACTIONS.

A. Chief Financial Officers view.

B. OMB view.

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