

**Statement by Gary Engebretson,
President of the Contract Services Association of America
Before
Commercial Activities Panel
Public Hearing
Washington, DC**

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This statement is being submitted on behalf of the 325 members of the Contract Services Association of America (CSA), as well as the multi-association Industry Logistics Coalition and the Coalition for Outsourcing and Privatization. We appreciate this opportunity to share our views on the ability of the Federal government to fully utilize competitive sourcing, outsourcing, and privatization options to achieve the necessary performance of commercial activities more efficiently, at “best value” and at lower total operating cost. Unfortunately, current statutes and Federal implementation policies unduly restrict the government’s actions related to competitive sourcing of commercial activities.

The Road to Acquisition Reform

During the height of the Cold War, the Department of Defense (DOD) had substantial budgets and its weapons systems were essentially defense-unique. Not much attention was even paid to civilian agencies. All that has changed in the last ten years. Tremendous advances have been made in the commercial sector in technology – no longer is the Government on the leading edge, but rather it is the private sector, with the Government lagging far behind. Recognizing this, Congress enacted a series of important acquisition reform initiatives. These all contributed to a more functional, effective acquisition process aimed at allowing the Government to purchase goods and services in the **commercial** marketplace, as well as strengthening the national industrial base. In the words of former Representative Bill Clinger, author of the 1996 Federal Acquisition Reform Act (commonly known as the Clinger-Cohen Act), acquisition reform achieved *“the goal of creating a more responsive system which provides more discretion to Government buyers and freedom for those who sell to them while maintaining the requisite degree of control and fairness.”*

Indeed, reforms like best value procurement and performance based contracting have changed both the practical and, just as importantly, the philosophical foundation of Federal contracting.

The Demand for Competition and a Fair Process

The issues of outsourcing and privatization are among the most prominent and important issues facing the Federal government. Indeed, much of what has been accomplished in the area of acquisition reform can and must **now** be applied to a more aggressive and comprehensive policy of competing commercial activities currently performed by government agencies. Moreover, how and where such competitions are conducted is a key acquisition reform issue.

We are not advocating that all Government services be contracted to the private sector. But as we continue to reinvent Government we must focus on competition. And that focus requires a balanced, responsible and unyielding commitment to exploring new ideas, challenging old prejudices and looking carefully at what services the Government must provide. It also requires a careful examination of **who**, inside or outside of Government, is in the best position to provide each service in the most efficient and effective way. This means, too, that the Government should adopt from the best of private enterprise those tools that foster the necessary incentives and rewards for high performance. And it must follow a fair process designed to protect the interests of the taxpayer and address the legitimate concerns of current Government workforce while, at the same time, ensuring that the Government operates in a maximally efficient manner. Above all, we must foster a process that is reliant on competition – and the private sector.

Competition is a key ingredient. Whether it is between the public and private sectors, or solely within the private sector, competition is the principal guarantor of quality and efficiency. Without competition, which provides necessary checks and balances, there is precious little incentive to provide goods and services of the highest quality and least cost. Competition lies at the heart of virtually every contemporary management – yet it remains sorely underutilized and faces formidable barriers within many areas of Government.

But competition is not just an endless quest for the lowest prices or costs. In its truest form, competition is a system of management in which there is an aggressive pursuit of all possibilities (in the case of Government, including a wide array of public/private partnerships) that can help the organization achieve its goals most efficiently and productively.

Therefore we must bring reason back to the discussion. If, as a nation, we are serious about enhancing efficiency and reducing the cost of Government, we cannot ignore the potential offered by increased competition for the provision of Government services. Nor can we afford to continue to tolerate the artificial barriers to that competition, barriers too often erected by parochial interests and so contrary to the real interests of the American taxpayer. As we renew our commitment to growing jobs in the private, rather than public sector, the enhancement of competition in Government becomes even more important.

The Need for Workforce Training

The role of retraining and job placement is a vital one – and it is an area in which the services industry is ready and willing to assist.

The ability of the acquisition workforce to implement and embrace changes hinges on the training and assistance that accompanies it. And it hinges on the degree to which that training is based on, and communicates, a real-world understanding of the competitive commercial marketplace. Because of the importance of outsourcing issues to the Government procurement process, industry recommends that procurement officials be provided with special training in the requirements of the A-76 process

Ironically, at the same time extensive cultural and process changes are being mandated through acquisition reform, the acquisition workforce is being reduced without a corresponding reduction in workload required by the “old system.” Moreover, fiscal support for education and training is coming under extreme budget pressure. We also may reach a crisis as talented acquisition individuals begin to retire; if not addressed, there is expected to be a gap within five years of trained and experienced high-level acquisition personnel. This must be addressed.

Outsourcing Myths and Realities

Several inaccurate assertions have repeatedly been made about the services industry. The first assertion is that service contractors achieve savings by paying their employees less. This is misleading and wrong. The service contract industry is governed by a host of wage laws, among them the Service Contract Act

Under the SCA, the Government provides wage rates for a variety of employees in addition to requiring money to be spent on fringe benefits. Violations of the Service Contract Act can result in fines and debarment. Indeed, the Contract Services Association of America (CSA) has a successful program with the Department of Labor to promote understanding of and compliance with the Service Contract Act.

A. It is disputed that outsourcing of Government functions actually saves money.

Study after study, from sources as diverse as the General Accounting Office (GAO), the Office of Management and Budget (OMB) and innumerable think tanks, have shown that competitively outsourcing the Government’s commercial activities saves money. For the taxpayer, this means an average savings of 30% regardless of who wins the competition. Broken down, this figure represents an average of 20% savings when an in-house team wins and an average of 40% savings when a private firm wins. At DOD alone, several studies have estimated that potential savings are in the neighborhood of \$30 billion dollars. Even reports that are critical as to the amount of savings achievable through outsourcing conclude that “competition for work, including competition between the public and private sector – regardless of who wins – can result in cost savings.”

B. Another inaccurate assertion is that contractors put Federal employees out of work, only to bring in their own people.

A study done by the National Commission of Employment Policy (NCEP), a branch of the Department of Labor, indicates that over half of the workers on outsourced Government functions went to work for the private sector firm, while twenty-four percent of the workers were transferred to other jobs and seven percent retired. The study concluded that less than seven percent of the workers needed to find new employment.

The question of jobs and job loss is one of the most misunderstood and misrepresented issues in the whole debate over competitive contracting. First and foremost, job loss is not a function of contracting but one of identifying the most efficient and productive means of implementing a

function or service, whether or not a contract is let. Since the Government's responsibility is to provide services in the most cost and quality conscious manner possible, making the system more cost and quality conscious must by definition involve some reductions in the workforce. Today, perhaps more than ever before, achieving maximum efficiency and productivity is imperative and must be the government's highest priority. But as noted above, the majority of employees easily find other employment.

C. And there is the term "Shadow Government."

It sounds provocative, but in fact it is inapplicable, alarmist and misleading. Oversight of Federal government contractors is, by its nature, an inherently governmental function. The power to create the scope of work, dictate the terms of the work and terminate the contract are functions performed by the Federal government, not the contractor. The contract itself embodies the responsibilities that the contractor must perform in order to keep the business; failure to do so may result in termination of the contract, and even civil or criminal penalties. The term "shadow Government" is nothing more than a "shadow argument."

The Problems Inherent in Public-Private Competitions

Industry has significant philosophical reservations regarding public-private competition. Indeed, we feel that it is not in the best interest of the taxpayer for the Federal government to compete directly with its citizens; this is partly reinforced by the lack of comparability between Government and industry cost accounting systems.

As OMB Director Mitch Daniels stated in an April 18 speech at a General Services Administration Federal Acquisition Conference, "*the general idea that the business of Government is not to provide services, but to see that services are provided seems self-evident to me.*"

While industry recognizes that public-private competitions will continue to be the rule, we are concerned that such competitions ultimately disadvantage all parties. For the private sector, the playing field is not, and likely never will be, entirely level. This is primarily due to the fact that, despite several recent laws, the Government does not have cost accounting systems in place to provide accurate or reliable financial data on workloads, does not have to pay taxes, and the methods by which it computes its overhead rates are not comparable with those of industry, nor does the Government "pay" for infrastructure (e.g. buildings and land). In addition, the Government does not face, either qualitatively or quantitatively, the same risks as a commercial contractor (e.g., on issues relating to termination for default, absorption of cost overruns or potential Civil False Claims penalties).

The factors listed above make it extremely difficult and, in some cases impossible, for industry to win a competition. For the Government, such competitions often result in decisions to retain work in-house because it does not appear that outsourcing represents the lowest cost to the taxpayer. However, in many such cases, the appearance is drastically different than the reality. The Government's "cost" is typically based on accounting systems that simply cannot capture the

real, total cost and almost always fail to provide an adequate framework for determining whether the Government's "cost" is, in fact, the most efficient organization for the taxpayer (including meaningful assessments of past performance, such as those rightfully applied to the private sector). Indeed, awarding a contract to the government is not even made on the basis of "best value" – a fundamental premise of acquisition reform – but rather low cost. If Government agencies are to continue to compete against private offerors to provide goods or services, it is vital that such competitions be conducted on the basis of truly comparable levels of performance, cost accounting practices, past performance and best value.

To reiterate, reliable cost and past performance information is crucial to the effective management of Government operations and to the conduct of competitions between public or private sector offerors. Unfortunately, this information has not been generally available and/or has often been found to be unreliable. The Chief Financial Officers Act of 1990 (CFO Act) included among the functions of chief financial officers "the development and reporting of cost information" and "the systematic measurement of performance." This includes performance by in-house, contract or ISSA resources. In July 1993, Congress passed the Government Performance Results Act (GPRA), which mandated performance measurements by Federal agencies. The Statement of Federal Financial Accounting Concepts No. 1, "Objectives of Federal Financial Reporting (1993)" stated that one of the objectives of Federal financial reporting is to provide useful information to assist in assessing the budget integrity, operating performance, stewardship, and control of the Federal government. In 1995, the Federal Accounting Standards Advisory Board (FASB) recommended standards for managerial cost accounting, which were approved by the Director of the Office of Management and Budget, the Secretary of the Treasury and the Comptroller General. These standards were issued as the Statement of Federal Accounting Standards No. 4, "Managerial Cost Accounting Standards for the Federal Government." *Despite these initiatives, the current process perpetuates an aspect of the public-private competition policy that has been severely discredited in recent years – the Department of Defense, and the other Federal agencies, still do not possess the cost systems or cost accounting procedures to accurately tally its costs for in-house activities.*

The need for comparable accounting data is implied in the *Federal Activities Inventory Reform Act* (FAIR Act) that is supported by industry. The statute requires an inventory of all commercial activities within the Federal government and allows contracting for the performance of those activities to pursue the "best value" for the taxpayer. It requires realistic and fair cost comparisons and establishes a definition for inherently governmental functions. The FAIR Act embraces several key principles: to achieve the best deal for the taxpayer; to be fair and equitable to all interested parties; and, to be instrumental in the government's overall reinvention effort. It is a rational and appropriate approach towards achieving the proper balance of utilizing public and private resources.

Much of what agencies can achieve through competitive sourcing is constrained by OMB Circular A-76, "Performance of Commercial Activities." This circular established Federal policy for the performance of recurring commercial activities and provides guidance and procedures for determining whether recurring commercial activities should be operated under contract with commercial sources, in-house using Government facilities and personnel, or through inter-service

support agreements (ISSAs). In principle, Circular A-76 is not designed to simply contract out. Rather, it is designed to: (1) balance the interests of the parties to a “make or buy” cost comparison, (2) provide a level playing field between public and private offerors to a competition, and (3) encourage competition and choice in the management and performance of commercial activities.

The A-76 process, however, was established in an era where cost was the principal award determinant for all competitions. In today’s era of best value procurements, which recognize that cost is but one of many important factors which assure taxpayer interests are most appropriately served, the old “cost-based” decision tree is no longer valid. Current OMB A-76 and Federal agency specific implementation guidance inhibits achievements of the Government-stated quality performance and cost reduction goals and severely hinders the implementation of outsourcing plans central to savings already incorporated into recent budget request.

Change is already evident within the private sector. Routinely, even in A-76 competitions, private offerors are now evaluated in a “best value” manner, with such items as past performance, technical competence, and management experience being considered factors and in some cases, more significant factors than cost. In today’s environment, however, these factors also become highly problematic since A-76 by design, does not seek to account for such items within the public sector. As anyone familiar with the award process knows, when one compares a cost-based proposal (in this case, the Government’s Most Efficient Organization, MEO) to a proposal which also evaluates, in real, and significant terms, non-cost factors, the cost-based proposal has a significant advantage. However, within DOD, past performance – a key acquisition reform initiative – is, by policy, supposed to account for at least 25% of every award decision.

In addition to the specific recommendations detailed below, in the attachment is listed existing policy guidance and statutes that require review and revision or repeal to ensure fair and uniform implementation of future competitive sourcing, outsourcing & privatization initiatives.

Recommendations

- **Need for a New Government-wide Commercial Activities Policy.** The nation is best served by implementing a new “Government-wide Commercial Activity Policy” suited to emerging 21st century requirements and based on commercial practices as defined in recent acquisition reform initiatives which would eventually replace the A-76 process.
- **Mandate Independent Government Estimate.** Next to a good specification (including reliable workload data), there is nothing more critical to the evaluation of offers (public or private) than a competent, thorough, and responsible independent government estimate (IGE) of the manpower and non-labor resources needed to successfully perform the specified work with minimum risk of unsatisfactory performance. Unfortunately, an IGE is seldom done – although it is common in the hardware world. Or, if one is prepared, it is typically seriously flawed because it was

based on factoring from the staffing and other resources of the existing contract. Clearly, if the existing contract is not optimized, any IGE produced by such factoring will also be sub optimal. Ideally, a responsible IGE should be derived from a thorough work breakdown structure estimate that is zero-based and which reflects an appreciation of modern commercial practices. It is recommended that an Independent Government Estimate (IGE) be prepared for every solicitation.

- **Increase the level for exempted activities from 10 FTEs to 100 FTEs.** This will increase the flexibility for agencies wishing to pursue different options under A-76.
- **Provide for the Efficient, Fair and Full Implementation of the FAIR Act.** Industry believes that Congress intended the FAIR Act's provisions to have broad and continuing coverage over all agencies and all methods available to the Federal government for managing its procurement of commercial activities. We remain concerned, however that the DOD Depots were exempted from this legislation and believe this issue should be addressed during the panel's review. The specific implementation elements of the act that should be addressed through regulation or review of the FAIR Act are as follows:
 - **FAIR Act Information Inadequate for Detailed Review.** The information provided in the Federal Agency Fair Act inventories is inadequate to describe the positions and functions listed in sufficient detail that a non-Government interested party, within the meaning of the FAIR Act, could determine the suitability of the classification codes assigned. There also is no way to determine what functions or activities were omitted by the various agencies or service branches, or the total number of other positions that may not be included for the activities identified – in order to validate the accuracy of the list.
 - **FAIR Act Classification Misused.** Agencies classified such a high proportion of the total positions as being “other than eligible for competitive sourcing” that it calls into the question the entire inventory. Lacking supporting detail and rationales for the classifications, industry cannot determine which classifications are reasonable and which are not.
 - **FAIR Act Classification Inconsistent.** There are many instances of apparent inconsistency where functions, which are contracted to private industry at one location, are classified as ineligible for competitive sourcing at other locations. Where positions have been classified exempt from competition due to public law or executive decision, no supporting detail citing the claimed basis of exemption has been provided. And, in many cases, positions have been rolled-up into single large categories. Such aggregated numbers are of little help in reviewing the inventory – these generic codes should be broken down into the specific functions as called for in Appendix No. 2 to OMB Circular A-76 Supplemental handbook.
 - **Inventories Do not Include Military Personnel.** Finally, many of the positions

listed in the DOD's Fair Act inventory of commercial activities are not performed by civilian Government employees, but rather by military personnel – and have not been included on the inventory. The justification was that these are personnel attached to a squadron that must be available to be deployed overseas in time of war. However, OMB Transmittal Memorandum #20 (6-21-99) specifically states that the requirements to inventory commercial activities *“is not limited to civilian employees. Accordingly, military personnel performing commercial activities are subject to the FAIR Act and must be inventoried.”*

The Contract Services Association of America, the Industry Logistics Coalition and the Coalition for Outsourcing and Privatization strongly supports this national-level review of outsourcing activities, as mandated by Section 832 of the FY2001 National Defense Authorization Act. This review to make the process more equitable and attractive to both public and private sector is clearly necessary.

We have an extraordinary opportunity to put momentum behind a policy first initiated by President Eisenhower, but which today remains largely ignored. The ability of Federal agencies to meet the tough budgetary and mission targets that Congress has set for them hinges, in large part, on the ability of Congress and the American public to know how agencies are using their resources to meet their core missions, and ensuring that scarce resources are used most efficiently.

(ATTACHMENT)

Statement by Gary Engebretson – June 11, 2001 (cont)

Attachment

Policy guidance requiring review and revision to ensure fair and uniform implementation of future competitive sourcing, outsourcing & privatization initiatives includes, but not limited to:

- OMB Circular A-76, “Performance of Commercial Activities,” August 4, 1983
- DOD Instruction 4100.33, “Commercial Activities Program and Procedures,” September 9, 1985
- DOD Directive 4100.15, “Commercial Activities Program,” March 10, 1989
- Government Performance and Results Act (GPRA), 1993
- OMB Circular A-76 Revised Supplemental Handbook, “Performance of Commercial Activities,” March 1996 including OMB Transmittal Memoranda relative to these procedures
- Department of the Army Regulation (AR) 5-20, “Commercial Activities Program”, 1 October 1997
- Department of the Navy (DON) Competitive Sourcing Handbooks: “Succeeding at Competition” and “Business Unit Definition and Analysis Guide”, 31 December 1997
- Department of the Army Pamphlet (DA PAM) 5-20, “Commercial Activities Study Guide”, 31 July 1998
- Chief of Naval Operations Instruction (OPNAVINST) 4860.7C, “Commercial Activities Program Manual”, 7 June 1999
- Department of Defense Strategic and Competitive Sourcing Programs Interim Guidance, April 3, 2000 (issued by the Under Secretary of Defense for Acquisition, Technology and Logistics)
- Department of the Air Force, Headquarters Air Education and Training Command (AETC) Pick-a-Base Action Plan, 1 Jan 2000
- Department of the Air Force Instruction (AFI) 38-203 (Draft), “Air Force Commercial Activities Program Instruction”
- OFPP Best Practices Guide to Performance-Based Service Contracting Independent Review Guide

Those statutes that should be repealed include:

- 15 U.S.C. 3704(b) - Prohibits outsourcing of the functions of the National Technical Information Service
- 10 U.S.C. 2461 - Requires notice to Congress of all DoD A-76 studies, and mandates public-private competitions
- 10 U.S.C. 2462 - Requires contract award to the Government if the Government is “low bid,” thereby prohibiting the application of best value principles to such procurements (ILC and COP recommend that this provision be repealed or, alternatively, amended to replace the terms “low cost” with “best value”)
- 10 U.S.C. 2463 - Requires semi-annual report to Congress of all conversions of workload at DoD involving more than 50 full time equivalents (FTEs)
- 10 U.S.C. 2464 - Limits the contracting out of logistics support activities to 50 percent of the total workload. ILC and COP support outright repeal of this provision. At a minimum, however, ILC and COP support a change that would base the workload calculations on the facilities utilized rather than personnel; this is necessary in order to fulfill DoD’s and Congress’ vision of partnerships and innovative teaming arrangements
- 10 U.S.C. 2465 - Prohibits the contracting out of firefighting and guard services at DoD facilities
- 10 U.S.C. 2466/2469 - Limits the contracting of depot maintenance workload and requires public-private competitions for workloads exceeding \$3 million
- 10 U.S.C. 4532/9532 - Mandates use of Government factories and arsenals
- 40 U.S.C. 490(c) or Section 507 (P.L. 100-440) - Prohibits GSA from contracting for guard, elevator, messenger or custodial services
- 16 U.S.C. 668(d) - Prohibits the Fish and Wildlife Service from outsourcing the management and operations of wildlife refuges