

GAO Commercial Activities Panel:

STATEMENT of ESOP Advisors, Inc.
August 8, 2001

In response to Federal, state and local government requirements to restructure and rationalize the provision of commercial activities, ESOP Advisors has utilized private sector Employee Stock Ownership Plan (ESOP) techniques to develop a process of ESOP Privatization and ESOP Enhancement of the A-76 Cost Comparison process.

These ESOP approaches provide a more employee friendly alternative to traditional privatization or A-76 practices, provide a seamless transition to contractor performance with less loss of institutional knowledge, and have been shown to produce real cost savings to the government. The ESOP process provides a mechanism for input from affected employees into the privatization process, and rewards federal employees with, an ownership interest or other economic rewards in the successor contractor that will provide the Federal government with the required continuing services. ESOP approaches may provide economic incentives and retirement security for current federal employees impacted by A-76 procedures, base closures, business line terminations, reimbursable business line withdrawals, or other required restructurings.

ESOP Advisors, on behalf of the federal government, has utilized ESOP Privatization (as discussed in the May, 1995 [draft] Federal Policy Guidance) as an alternative to traditional A-76 approaches and to implement direct privatization. ESOP privatization has been successfully employed in the termination of a business line resulting in the direct privatization of the Office of Personnel Management's Office of Federal Investigations in 1995-6 (OPM-OFI), where it has produced proven cost savings and operational/quality improvements in the performance of Federal civilian background and security investigations. The ESOP approach has also been used in the context of BRAC activities to transition 425 Navy environmental remediation employees to the private sector in 1999, as well as to provide a means to facilitate the closure of the Army Management

Engineering College in 1998. The USPS has just announced its intention to proceed with the ESOP Privatization of its EEO investigations function, rather than employ traditional outsourcing or public-private competition.

The OMB and DOD have recently recognized that ESOP approaches can enhance competition and provide a more employee friendly approach in the current A-76 process. In this approach, the affected employees have the option of forming an ESOP partnership with a private sector firm which will enter a bid in the private sector competition within the A-76 process. If this partnership wins the private sector competition, then the employees will “win” either by virtue of the success of the MEO or by joining the private sector as a result of their private sector partner’s success in the final public private competition. Such an enhanced A-76 competition has recently received the approval of OMB and DOD, but has not been implemented.

ESOP approaches can be combined with non-profit approaches to provide future comparable retirement security for current federal employees impacted by A-76 procedures. Under the combined nonprofit and ESOP approaches, current federal employees who become the employees of a public non-profit corporation can continue in federal retirement programs for up to four years after joining the private sector as a result of privatization or A-76. These employees and their business units can then transition to for-profit operation in the private sector where ESOP and other private sector retirement plans can additionally enhance their retirement security.

ESOP and Non-Profit approaches to privatization and commercial activities rationalization are good for the federal government and the taxpayer. They demonstrate good employer relations by providing a more employee friendly alternative to traditional commercial activities practices, and they promote efficiencies and cost reductions. Independent analysis of the privatization of OPM-OFI has documented cost savings much greater than the \$30 million initially projected by OMB [on the basis of traditional outsourcing] and additional federal income from tax revenues generated by USIS, the private sector employee owned (ESOP) company created in the privatization.

ESOP privatization expands the competitive base for provision of federal services, as demonstrated by the OPM-OFI privatization which created a new source for the very large unified federal requirement for civilian background and security investigations, where existing contractors had only the capability to service less than 20% unified federal requirement.

ESOP Privatization directly reduces the size of the federal government, and can lead to improved quality through the ability to improve the licensing and certification of employees providing future required commercial activities and can improve quality control and assurance. ESOP Privatization has also proven to reduce employee resistance to privatization and commercial activities competitions, as it must be undertaken on a voluntary basis by the affected [groups of] employees. It also provides for a seamless transition to contractor performance and minimizes the loss of required institutional knowledge about the federal operation, as well as providing more potential for “surge” capacity that may be required in the future.

ESOP privatization is good for the federal employee because it minimizes the potential adverse impacts of current commercial activities approaches. It reduces the employment risk inherent in current A-76 and privatization procedures and reduces job losses. ESOP companies have the incentive to expand to serve additional markets beyond the workload being privatized or competed under A-76. The success of an ESOP company directly promotes and leads to increased equity ownership and capital wealth, and this has been recognized by the US Congress which has provided incentives to broaden equity ownership in the US economy and strengthen US international competitiveness through encouraging the adoption of ESOP plans in the private sector. ESOP privatization also provides new career growth opportunities for federal employees, and the economic incentives and future retirement security provided by employee ownership and non-profit approaches can provide a new mechanism for redirecting federal career paths.