



Testimony

Before the Subcommittee on Government Management,
Information and Technology
Committee on Government Reform
House of Representatives

For Release on Delivery
2:00 p.m. EDT
Thursday
October 28, 1999

COMPETITIVE CONTRACTING

Preliminary Issues Regarding FAIR Act Implementation

Statement of
J. Christopher Mihm
Associate Director, Federal Management
and Workforce Issues
General Government Division



G A O

Accountability * Integrity * Reliability

Competitive Contracting: Preliminary Issues Regarding FAIR Act Implementation

Mr. Chairman and Members of the Subcommittee:

I am pleased to be here today to discuss our observations on the initial implementation of the Federal Activities Inventory Reform (FAIR) Act of 1998.¹ As you know, as a first step, the FAIR Act requires executive agencies² to identify their activities that are not inherently governmental and make this information publicly available.³ The implementation of the FAIR Act is in the early stages—many agencies have only recently released their inventories. Many other agencies' FAIR Act inventories still have not been made available to the public—including 14 of the 24 agencies covered by the Chief Financial Officers (CFO) Act.

At the request of this Subcommittee we are beginning a body of work to assess agencies' efforts under the FAIR Act. As agreed, my statement today will discuss the progress to date in developing and releasing agencies' FAIR Act inventories. I will briefly describe the status of the initial steps taken to implement the FAIR Act. Then I will highlight some of the questions that are being raised by our examination of the Department of Commerce, the Environmental Protection Agency (EPA), and the General Services Administration (GSA) FAIR Act inventories. We are examining FAIR Act efforts at these and selected other agencies at the request of the Chairwoman, Subcommittee on Oversight, Investigations, and Emergency Management, House Committee on Transportation and Infrastructure.

Initial Steps to Implement the FAIR Act

The FAIR Act requires executive agencies to submit each year to the Office of Management and Budget (OMB) inventories of activities that, in the judgment of the head of the agency, are not inherently governmental functions. The first FAIR Act inventories were due to OMB by June 30, 1999. According to an OMB official, most agencies met this requirement.

OMB, after a period of "review and consultation" with the agencies about their inventories, is to publish a notice in the Federal Register stating that the agencies' lists are available to the public. The agency heads are responsible for promptly transmitting a copy of the FAIR Act inventory to Congress and making the list available to the public. The FAIR Act requires

¹ Public Law No. 105-270, 112 Stat. 2382, 31 U.S.C. 501 note (1998).

² Executive agencies are broadly defined in the FAIR Act to include civilian or military departments, or independent establishments within the meaning of 5 U.S.C. 101, 102, and 104 respectively, with certain specified exceptions.

³ Inherently governmental functions are those functions so intimately related to the public interest as to mandate performance by government employees. An inherently governmental function includes activities that require either the exercise of discretion in applying government authority, or the making of value judgments in making decisions for the government.

these inventories to include information about (1) the fiscal year the activity first appeared on the FAIR Act list, (2) the number of full-time-equivalent (FTE) staff years necessary to perform the activity by a federal government source,⁴ and (3) the name of a federal government employee responsible for the activity from whom additional information about the activity may be obtained. It is important to note that the FAIR Act does not require an agency to list activities that the agency determines are inherently governmental and therefore not commercial.

OMB published draft guidance in March 1999 and issued final guidance on the implementation of the FAIR Act on June 24—about a week before the first inventories were due. OMB implemented the FAIR Act by revising its Circular A-76, “Performance of Commercial Activities,” and the A-76 Supplemental Handbook. Under Circular A-76, executive agencies are to conduct cost comparison studies of commercial activities performed by government personnel to determine whether it would be more cost efficient to maintain them in-house or contract with the private sector for their performance.

Under OMB’s revised guidance, agencies were expected to list the activities the agency determined are not inherently governmental using specific codes established for A-76. These include both “reason” and “function” codes. The “reason codes” are used to show whether the agency believes that an activity determined to be commercial should be subject to an A-76 cost comparison or not, including identifying those commercial activities that cannot be competed because of a legislative or other exemption.

The function codes are to characterize the types of activities that the agency performs. The function codes range from fairly broad categories, such as “family services,” to much more specific (and defense-related) activities, such as “Intermediate, Direct, or General Repair and Maintenance of Equipment—Missiles.”

OMB’s implementation guidance stated that OMB could not set a firm timetable for its review and consultation about agencies’ FAIR Act inventories but estimated that it would take about 60 days after receiving an agency’s inventory and any requested supplemental information. Because of the staggered submission of agencies’ inventories and the workload involved with reviewing the inventories, OMB officials said they

⁴ FTEs are used to measure civilian employment. 1 FTE is equal to 1 work year of 2,080 hours.

would group a set of inventories for release together, rather than releasing them on a rolling, agency-by-agency schedule.

In a September 30, 1999, Federal Register announcement, OMB listed the first group of FAIR Act inventories—from 52 agencies—that were made available to the public. Of these 52 inventories, 10 were from CFO Act agencies. Five of these were from cabinet agencies (Agriculture, Commerce, Education, Health and Human Services, and Housing and Urban Development) and the other five were from EPA, GSA, the National Aeronautics and Space Administration, the Social Security Administration, and the Agency for International Development. The remaining 42 inventories released in September 1999 were from smaller executive agencies such as the Marine Mammal Commission and the Office of National Drug Control Policy.

The next step in implementing the FAIR Act includes potential challenges to the lists. According to the FAIR Act, within 30 days after publication of the notice of the public availability of the list, an interested party may challenge the omission of a particular activity from, or an inclusion of a particular activity on, the FAIR Act inventory. Within 28 days after an executive agency receives a challenge, it must decide the challenge and provide written notification, including a discussion of the rationale for the decision, to the challenger. This decision can be appealed to the head of the agency within 10 days after the challenger receives written notification of the decision.

Initial Implementation of the FAIR Act Raises Important Questions

Clearly, executive agencies and OMB still have plenty of work ahead to implement even the first step of the FAIR Act—the public release of inventories. Nevertheless, our initial review of selected inventories that have been released raise a number of important questions about the efforts thus far. On behalf of the Subcommittee, we will be seeking answers to these and related questions over the coming months in order to assess agencies' efforts and to develop a body of best practices, as efforts under the FAIR Act move forward.

What Decisions Did Agencies Make About Whether or Not Activities Were Eligible For Competition and What Were The Reasons For Those Decisions?

A major area of interest during the initial implementation of the FAIR Act concerns the decisions agencies made about whether or not activities were eligible for competition and the reasons for those decisions. The FAIR Act provides that when an agency considers contracting with a private sector source for a commercial activity on its list, the agency shall use a competitive process to select the source unless it is exempted from doing so. A commercial activity in an agency can be exempted from competition for a variety of reasons. These reasons include legislative restrictions, other actions by Congress, Executive Orders, OMB decisions, or separate decisions by the relevant agency. Our initial review of the selected inventories suggests that questions can be raised about how agencies decided whether or not a commercial activity could be subject to competition, particularly when an agency reports that relatively few of its commercial activities could be considered for competition.

EPA's Activities

Out of a total of 829 FTEs performing commercial activities listed in EPA's FAIR Act inventory, about 30 FTEs (about 3.6 percent) were listed in commercial activities that could be considered for competition. These activities were listed under six function codes, including (1) nonmanufacturing operations (such as mapping and charting or printing and reproduction activities); (2) maintenance, repair, alteration, and minor construction of real property; (3) regulatory management and support services; (4) installation services; (5) administrative support for environmental activities; and (6) other selected functions.

EPA listed about 24 FTEs, or about 3 percent of the total of the commercial activities listed, as performing activities that are exempt from competition because of actions by Congress, Executive Order, or OMB. Most of these FTEs provide support for two function codes—research, development, testing, and evaluation; or administrative support for environmental activities.

Overall, however, EPA's inventory shows that EPA has decided that most of its commercial activities are exempt from competition. This includes about 775 FTEs or over 93 percent of the total number of FTEs performing commercial activities at EPA. The function codes with FTEs listed as exempt include environmental activities; research, development, testing, and evaluation support; automated data processing; and finance and accounting. According to EPA, it has exempted a number of FTEs from competition because it needs to retain a core staff capability. In its July 1, 1999, letter to OMB, EPA stated that the majority of the functions on its FAIR Act inventory represent commercial core capability that should be retained in house. EPA's letter cited its need to maintain appropriate in-

house expertise to effectively apply and enforce the nation's environmental laws in fulfilling its mission and meeting emergency requirements. For example, EPA's Deputy CFO told us that the agency exempted selected positions requiring scientific expertise in its research and development office in order to oversee the work produced by laboratories run by contractors.

GSA's Activities

Out of a total of 7,249 FTEs GSA determined were providing commercial activities, it listed 4,556 FTEs (63 percent) who perform commercial activities that could be subject to competition. Almost half of these FTEs were involved in the maintenance, repair, or minor construction of real property. GSA also listed 874 FTEs (12 percent of the total commercial activities identified) as exempt from competition—more than half of these FTEs also perform activities involved with the maintenance, repair, or minor construction of real property.

According to GSA's FAIR Act inventory, 1,819 FTEs (25 percent of its FTEs performing commercial activities) should be retained in-house because the activities are being "reinvented."⁵ GSA plans to reassess the activities for possible recategorization once reinvention efforts are completed. The FTEs are devoted to various activities, including financial and payment services, information and telecommunication program management, and security and protection.

What Processes Did Agencies Use to Develop Their FAIR Act Inventories?

Agencies used a variety of approaches to develop their FAIR Act inventories. For example, a number of agencies used their "Raines inventories" as a basis for their FAIR Act inventories.⁶ The Raines inventories were developed as part of a 1998 effort led by OMB under which agencies were to identify commercial and other activities and provide that information to OMB. Specifically, agencies were asked to list agency functions and positions supporting activities that were

- inherently governmental;
- commercial, but specifically exempt from the cost comparison requirements of OMB Circular A-76;
- commercial and should be competed; and
- commercial, but must be retained in-house (including the reason why).

⁵GSA's FAIR Act inventory also reported that 7,029 FTEs performed inherently governmental activities.

⁶ Then-OMB Director Franklin D. Raines issued a memorandum on May 12, 1998, requesting agencies review their full time and part time positions and develop a preliminary inventory. According to the memorandum, agencies were to use their inventories to establish opportunities for generating reinvention and competition savings.

Officials from the Department of Commerce said that Commerce based its FAIR Act inventory almost entirely on the information from its Raines inventory. The Department asked its component organizations to update the information that previously had been prepared for OMB as part of its Raines inventory. According to Commerce officials, these organizations made only minor changes for the FAIR Act inventory.

GSA described its approach as starting from the top and working down, with agency management forming a team to develop its FAIR Act inventory. GSA's team was composed of one or two staff members from each of GSA's service divisions and regional offices. GSA officials said that this team held lengthy discussions about GSA's core mission and about which of its functions should be considered inherently governmental. In addition, a contractor was hired to train staff and to facilitate discussions on the topic of inherently governmental activities. GSA officials said that making the training as inclusive as possible was important to address the staff's apprehensions about privatization.

EPA delegated the responsibility for developing its inventory to its 10 regional offices because it decided that the regional officials closest to the work should make determinations about specific activities. EPA headquarters reviewed and compared the submissions from its regions and offices and worked to resolve any discrepancies. EPA's Deputy CFO said that he does not expect the percentage of activities EPA identifies as commercial to remain static. He predicted that it would increase in the future, although he also emphasized that EPA is already very reliant on contractor support to fulfill its mission.

How Useful Are the FAIR Act Inventories?

The inventories now being released represent the first time that agencies have produced inventories under the FAIR Act. Thus, it is not surprising that a variety of different reporting formats are being used. It will likely take several reporting cycles before a documented set of best practices emerges that meets the needs of Congress and other interested parties. Also, it is not surprising that these inventories will become more useful as they become clearer and more complete.

The Department of Commerce's list provides an example of a submission that could be clearer and more complete. The Department used the format of its Raines list with the "reason codes" to be used for the FAIR Act inventory. As a result, many of the inventory's entries are contradictory or ambiguous. In one case, five different entries, totaling 177 FTEs involved in mapping and charting activities, are listed as "commercial competitive"—that is, commercial activities that could be subject to

competition. However, Commerce also assigned these same entries a “reason code” indicating that these activities are “prohibited from conversion to contract because of legislation.” Thus, the information reported does not appear to be consistent. In addition, Commerce did not assign any “reason codes” for a substantial number of FTEs listed throughout its FAIR Act inventory, so it is not clear how Commerce is characterizing these commercial activities.

Officials in agencies we spoke to generally found that the A-76 codes needed additional refinement. Officials from the Department of Commerce noted that the function codes were oriented toward military activities and needed to be augmented to more fully capture the range of activities undertaken by civilian agencies. In response to concerns such as Commerce’s, OMB allows agencies to develop new function codes to better meet their needs. Commerce, EPA, and GSA are among the agencies that are using additional function codes. While such flexibility is important to accurately reflect the diversity of the types of specific activities that individual agencies perform, it also needs to be balanced against the need for comparisons of the types of activities that are common across agencies.

What Supplemental Information Can Be Included to Increase the Usefulness of Inventories?

Beyond the requirements of the FAIR Act, some agencies are including information with their inventories that can provide additional perspective on the contracting and management issues confronting agencies. In the inventories that we have examined, we found that, in some cases, the agencies included supplemental information that was helpful, such as

- listing inherently governmental activities,
- describing the scope of activities currently under contract, and
- discussing how listed activities contribute to agencies’ strategic and annual performance.

Including information about an agency’s inherently governmental activities (such as was provided to OMB as part of the Raines inventories) helps provide a fuller perspective about all of an agency’s activities, not just those the agency considers commercial. For example, although not required to do so, GSA’s FAIR Act inventory included inherently governmental activities. Such information can help provide Congress and other interested parties with a more complete picture of GSA’s activities and allows for more informed judgments about whether an activity currently characterized as inherently governmental should be considered commercial.

Similarly, describing the scope of activities that an agency has already outsourced can provide an important perspective on and context for the agency's operations. In their letters or other documents submitting their FAIR Act inventories to OMB, for example, GSA, EPA, and Commerce all describe their current levels of contracting. Commerce's letter said that its service contracting outlays increased by 36 percent from 1996 through 1998. GSA stated that nearly 94 percent of its budget is spent for contractors. EPA's letter estimates the amount of resources currently contracted outside of EPA translates into 11,000 to 15,000 FTE had it retained the work inside of the agency.

Finally, it is important to recognize how an agency's strategies, including any plans to contract for services, contributes to the achievement of the agency's mission and its programmatic goals. In its introduction to its FAIR Act inventory, GSA states that its strategic plan provides the road map for achieving its mission and the context within which it developed this inventory, citing four goals, such as one to "create loyal customers by providing excellence in customer service." EPA's FAIR Act inventory links each commercial activity with 1 or more of EPA's 10 strategic goals—such as linking the administrative support activities in the Office of Water with EPA's strategic goal of ensuring clean and safe water.

The FAIR Act inventories, then, can provide valuable information about the role of contracting in an agency's efforts to provide cost-effective products and services. OMB has encouraged agencies to understand and use a variety of tools and strategies to make sound business decisions and enhance federal performance through competition and choice. Efforts under the FAIR Act can best be understood within the context of other initiatives, such as the Government Performance and Results Act, performance-based organizations, and franchise funds, as part of a package of ways agencies can improve services and reduce costs. FAIR Act inventories that provide information and perspective on how various initiatives are being used together can be helpful to congressional and other decisionmakers in assessing the economy, efficiency, and effectiveness of an agency.

In summary, Mr. Chairman, most agencies' FAIR Act inventories have been submitted to OMB for review and consultation, and the first group of inventories is now publicly available. Clearly, executive agencies and OMB still have plenty of work ahead to implement the FAIR Act, including the public release of more inventories and the resolution of any challenges. Nevertheless, our initial review of selected inventories raise some

questions about the efforts thus far which we will be reviewing for the Subcommittee. These questions include the following:

- What decisions did agencies make about whether or not activities were eligible for competition and what were the reasons for those decisions?
- What processes did agencies use to develop their FAIR Act inventories?
- How useful are the FAIR Act inventories?
- What supplemental information can be included to increase the usefulness of inventories?

By enacting the FAIR Act, Congress has increased the visibility of agencies' commercial activities. Continuing congressional interest in the FAIR Act process is needed in order to maintain serious agency attention to developing and using the FAIR Act inventories. Oversight hearings, such as today's hearing, send clear messages to agencies that Congress is serious about improving the efficiency and effectiveness of government operations and the effective implementation of the FAIR Act. We look forward to continuing to work with you and other Members of Congress as your oversight efforts continue.

Mr. Chairman, this concludes my prepared statement. I would be pleased to respond to any questions you or other Members of the Subcommittee may have.

Contacts and Acknowledgements

For further contacts regarding this testimony, please contact J. Christopher Mihm at (202) 512-8676. Individuals making key contributions to this testimony included Steven G. Lozano, Thomas M. Beall, Susan Michal-Smith, Susan Ragland, and Jerome T. Sandau.

Ordering Information

The first copy of each GAO report and testimony is free. Additional copies are \$2 each. Orders should be sent to the following address, accompanied by a check or money order made out to the Superintendent of Documents, when necessary. VISA and MasterCard credit cards are accepted, also. Orders for 100 or more copies to be mailed to a single address are discounted 25 percent.

Order by mail:

**U.S. General Accounting Office
P.O. Box 37050
Washington, DC 20013**

or visit:

**Room 1100
700 4th St. NW (corner of 4th and G Sts. NW)
U.S. General Accounting Office
Washington, DC**

Orders may also be placed by calling (202) 512-6000 or by using fax number (202) 512-6061, or TDD (202) 512-2537.

Each day, GAO issues a list of newly available reports and testimony. To receive facsimile copies of the daily list or any list from the past 30 days, please call (202) 512-6000 using a touch-tone phone. A recorded menu will provide information on how to obtain these lists.

For information on how to access GAO reports on the INTERNET, send e-mail message with "info" in the body to:

info@www.gao.gov

or visit GAO's World Wide Web Home Page at:

<http://www.gao.gov>

**United States
General Accounting Office
Washington, D.C. 20548-0001**

**Bulk Rate
Postage & Fees Paid
GAO
Permit No. G100**

**Official Business
Penalty for Private Use \$300**

Address Correction Requested
