



**COMPETING FEDERAL COMMERCIAL ACTIVITIES:
A CRITICAL TIME FOR
CONGRESSIONAL DIRECTION**

February 1998

THE PROCUREMENT ROUND TABLE

COMPETING FEDERAL COMMERCIAL ACTIVITIES: A CRITICAL TIME FOR CONGRESSIONAL DIRECTION

EXECUTIVE SUMMARY

The Procurement Round Table (PRT) presents this paper as a part of its continuing series of publications and seminars targeted at prompting discussions and actions that will help improve the Federal acquisition process. In addition to outsourcing and divestiture, the PRT currently is focusing on centralization of DOD's acquisition requirements process, ethics (particularly as related to post government employment), acquisition program stability (through biannual budgeting and multi-year contracting), and readying the Federal acquisition work-force for the 21st century. The PRT is a nonprofit organization chartered in 1984 by former Federal acquisition officials. Its members are private citizens and serve pro bono. The PRT's chairman is Elmer B. Staats, former Comptroller General of the United States with former Congressman Frank Horton serving as acting chairman.

Opening Federal commercial activities to competition has long been an effective method for reducing government costs and improving efficiencies. Despite this fact, decades of divisive debate and numerous barriers have prevented optimizing their use. This PRT paper explores those barriers. It further analyzes several conditions which today provide a unique opportunity for significant breakthrough in the long-standing paralysis that has inhibited effective competition of Federal commercial activities.

To seize this unusual opportunity, legislation is necessary to guide and sustain meaningful action. Absent congressional consensus, Federal agencies have proceeded in a haphazard manner, achieving some notable successes but frequently colliding with Congress and failing to capture the maximum benefits of outsourcing and divestiture actions. This paper outlines a proposed statutory approach to lead outsourcing and divestiture initiatives in both the Department of Defense and civilian agencies. A call for standardized technology and an exploration of some of the myths and realities inhibiting Federal outsourcing and divestiture are detailed in two appendices to the paper. As a first step, competition between public and private activities may be necessary to increase the extent of outsourcing, in the long run the aim should be to confine competition to the private sector only.

If the Federal government is to lead rather than follow opportunities of the 21st century, bold thinking and bold reforms are necessary. Nothing is more critical than applying such boldness to the specific manner in which our government manages its business. The time has come to go beyond noble visions and broad goals and get to the bottom line. The time has come for competition in the business of the Federal government.

COMPETING FEDERAL COMMERCIAL ACTIVITIES: A CRITICAL TIME FOR CONGRESSIONAL DIRECTION

A Position Paper Presented by the Procurement Round Table

February 1998

The Procurement Round Table (PRT) is a non-profit corporation chartered in 1984 by a group of former acquisition officials concerned about the economy, efficiency, and effectiveness of the Federal acquisition process. Its directors are private citizens who are serving pro bono with the objective of advising and assisting the government in making improvements in the process.

INTRODUCTION

"Outsourcing", "privatization", "contracting out", "divestiture" (see Appendix A for PRT definitions) have long been seen as effective methods to achieve several important goals for enhanced government efficiency by:

- (1) capitalizing on the competitive market forces of the private sector thereby reducing costs,
- (2) increasing productivity, quality and innovation, and
- (3) responding to expressed public policy and sentiment for less government intrusion in the business of the nation.

Yet despite these goals and methods being firmly embedded in numerous Federal statutes, regulations and policies (some dating back more than 40 years), operational attainment has proven far more difficult in specific practice.

Since OMB Circular A-76, "Performance of Commercial Activities", was adopted in 1966, Federal agencies have outsourced and divested a limited number of functions. For instance, the Department of Defense completed over 2000 A-76 studies between 1979-1994. But these studies only covered about 90,000 Full Time Equivalents (FTEs). DOD estimates that of the 850,000 FTE positions currently classified as providing commercial services for the military, 640,000 are still held by Federal employees, but admits that the 850,000 figure is under-estimated. Defense Secretary Cohen has directed that DOD review and standardize its classification system by 1999.

After decades of effort, significant success in using outsourcing and divestiture to improve the Federal government and cut costs still remains elusive for two basic reasons:

1. Lack of strategic planning and concerted focus by Federal agencies.
2. Lack of Congressional consensus on an approach that would sustain meaningful Federal action.

Lacking strategic focus and direction, outsourcing and divestiture have proceeded in an ad hoc, haphazard manner, resulting more often than not in a divisive debate over control, trust, money, employment protection, philosophy, and/or agency inaction depending on the specific perspective and function(s) proposed or not proposed to be outsourced or divested. (For further discussion of some basic myths and realities about outsourcing and divestiture, see Appendix B.)

For perhaps the first time in four decades of such debate, however, unique conditions for a resolution are at hand. What remains to be seen is if they will be seized.

THE TIME IS NOW

For 10 years, a similar political paralysis also confronted the complex issue of military base realignments and closures. From 1977 to 1988, despite a bloated base structure, no major military installation was closed. Then in 1990, after a fitful start in 1988, Congress enacted the "Defense Base Closure and Realignment Act (P.L. 101-510). This landmark legislation broke the long-standing base closure logjam in an exercise of superb congressional leadership.

Why and how? Two simple reasons: the conditions were right, and Congress adopted a realistic political approach.

The identical conditions which led to the breakthrough on military infrastructure and the unique process devised by Congress to achieve base closure action also can resolve the paralysis which continues to inhibit outsourcing or divestiture of Federal commercial activities. Conditions for success exist --

Only Congressional consensus and leadership are needed.

THE CONDITIONS FOR SUCCESS

With Defense base realignments and closures (BRAC), critical mass was achieved when three conditions needed for significant breakthrough aligned. Two of these same conditions, **NEED** and **CULTURAL READINESS**, exist today with respect to Federal outsourcing and divestiture. The third element, **CONGRESSIONAL CONSENSUS**, however, is essential for success.

1. **NEED EXISTS:** With the end of the Cold War and the fall of the Warsaw Pact, U.S. military force structure and budgets changed dramatically. The challenge was not to do less with less but to do more with less. The roles and missions of the military services were expanded, readiness needs became more critical given contingency missions, and training, equipment modernization, and readiness became more challenged. In the last 7 years, the U.S. military has been involved in 25 major operations, as compared with 10 between 1945 and 1989. Yet, from 1985 to 1997, the DOD budget declined nearly 40%, and between 1990 and 1997, DOD spending on procurement declined by 53%. Between 1989 and 1997, the total DOD active, reserve component and civilian workforce was reduced by 1.3 million people, and is scheduled for a further reduction of 315,000 by 2005. Previously excess infrastructure became totally unjustifiable and unsustainable in this environment. The Department of Defense literally begged Congress for relief.

With respect to outsourcing and divestiture, these same conditions of **NEED** exist today. According to the Vice President's fourth annual National Performance Review Report (issued November 5, 1997), the Federal workforce has declined by 309,000 since 1993, and the budgets for civilian and military agencies continue to decline (with fiscal year 1998 a distinct aberration). Yet, expectations for high level performance have not declined and indeed have increased, and the need for training and technological modernization and innovation (with their concomitant costs) are growing exponentially. In this environment, Federal agencies cannot sustain or justify costly and inefficient in-house performance of functions which can be provided in the private sector. And, as with BRAC, they are asking for Congress for increased latitude to address this dilemma.

2. **CULTURAL READINESS EXISTS:** Within the DOD workforce, the culture was ready by 1990 to accept significant base closures. Where previously, passive resistance and outright opposition existed, the fall of the Berlin Wall and the precipitous downsizing of personnel and budgets changed the opinion of many within DOD, not to mention the public at large and Members of Congress. Infrastructure overhead became a costly burden that impeded critical modernization and quality of life improvements for those in uniform. BRAC provided the Pentagon with the leadership direction to address this problem.

While the private sector has long advocated contracting out Federal activities that are not inherently governmental, today this same cultural readiness also exists or is beginning to exist within the Federal agencies. Faced with downsized staff and budgets but increased expectations for performance, the Executive Branch, today more than ever before, is ready to embrace a culture of public-private sector competitions, direct outsourcing, and outright divestiture in the quest to stretch budget dollars to meet high priority needs.

Examples of this cultural readiness abound.

- a. In 1993, the Administration established the National Performance Review (NPR), with the goal to reinvent and improve the Federal government. While Congress and the Administration may differ on the specific achievements thus far, the focus on measurable results through adopting the best private sector business practices is

having a beneficial effect on bureaucratic culture. Central to the NPR initiative is an assessment of every government program in terms of whether it is critical to the agency's mission. If no, the NPR recommends that it be privatized or terminated. If yes, the NPR calls for an analysis of whether it can be performed as well or better by devolving the activity to state or local governments or by competing its performance with the private sector.

b. Federal agencies, facing significant budget reductions with about \$200 billion in procurement dollars at stake, have established their willingness to outsource and divest through recent initiatives such as the May 1995 DOD Commission on Roles and Missions report "Directions for Defense"; the Department of Energy's January 1997 report on "Harnessing the Market: The Opportunities and Challenges of Privatization"; the August 1996 Defense Science Board Task Force Report on "Outsourcing and Privatization" which projects a savings of \$7 to 12 billion through outsourcing and divestiture of DOD functions; the independent (but DOD supported) Business Executives for National Security "Tooth-to-Tail Commission"; Defense Secretary Cohen's November 1997 Defense Reform Initiative Report, and numerous civilian agency reviews undertaken as part of the NPR.

c. In addition, Federal agencies have shown increasing creativity and a willingness to innovate through outsourcing. A few such examples include: the National Park Service's 1997 Plan to outsource functions at the Gettysburg National Park and NASA'S major privatization efforts in the Space Program. In the case of NASA, for instance, a private sector joint venture is gradually taking over space shuttle operations under a six year, \$7.2 billion contract which is expected to save taxpayers over \$400M. This private sector joint venture is proposing to go even further into "Commercialization" whereby shuttle services could be purchased commercially and possibly produce profits for the shuttle program.

d. Many State and local governments are already leading the way, with such initiatives as Indianapolis' public-private bidding success story for city services (25% reduction in the cost of Indianapolis' municipal services and reduction of the city workforce by one-third, for a total city taxpayer savings of \$240 million since 1992).

e. The public also has established its interest and intent in not having the government (Federal, state or local) perform those functions that do not have to be performed by that government through public opinion poll and support of outsourcing initiatives.

3. CONGRESSIONAL CONSENSUS ON A PROCESS IS NEEDED: Congress responded to the base closure paralysis with a unique process. Congress had perceived previous base closure recommendations as being based on unsound data and political motivation. Yet, Congressional recognition of the changing military requirements and growing need to respond led to the 1990 BRAC legislation, establishing a process and criteria that Members of Congress could politically

sustain, if not embrace.

The similarly politically and emotionally charged issue of outsourcing or divestiture of Federal commercial activities has yet to be addressed by Congress with the same clear direction and resolve.

Congress has initiated the elements of its intent and leadership through a series of statutes related to Federal acquisition, to include the 1993 Government Performance and Results Act; the Government Management Reform Act of 1994, the Federal Acquisition Streamlining Act (FASA) of 1994; the Federal Acquisition Reform Act (FARA) of 1996 and the Information Technology Management Reform Act (Clinger-Cohen Act); and the 1998 Defense Authorization bill, but none directly providing comprehensive leadership direction on Federal outsourcing and divestiture. Conversely, the landscape of Federal statutes and policies is still littered with inconsistent and conflicting direction with respect to this issue which feeds divisive debate, confusion and frustration.

Congress has the opportunity now to seize on this need and cultural readiness for reform and at long last break through this morass, following the same process they did with base closures.

TWELVE ELEMENTS OF SUCCESS

The "Defense Base Closure and Realignment Act" (BRAC) had a number of unique elements which led to its success. These elements, outlined below, would work equally well as a framework of congressional leadership for outsourcing or divestiture of Federal commercial activities. What made these elements work was the assurance of a process that was fair and open, strategy-driven, analytical, and executable. The 12 elements of BRAC success were:

1. An impartial review Commission established by law with appointment by the President (4 in consultation with Senate and House majority leaders, 2 with the advice of Senate and House minority leaders and 2 independently by the President) and confirmation by the Senate.
2. Specific criteria to guide the process, finalized after public comment, and reviewed by the Commission to support each of the intended actions (for BRAC, DOD established 8 criteria of which 4 received preference).
3. A plan submitted to Congress in advance of the BRAC proposals (in the case of DOD, this was a force-structure plan; for outsourcing/divestiture decisions, this could be a mission-structure plan). The 1993 Government Performance and Results Act requires that Federal agencies establish and submit to Congress strategic plans reflecting their major responsibilities and how they will be attained through long-range goals.
4. A plan for action submitted to the Commission from the Federal agency head based on elements

2 and 3 above with the commitment to initiate action within a set period (2 years for BRAC) and complete it (6 years for BRAC) and a terminus for the entire process (3 rounds of recommendations for BRAC).

5. Review by the General Accounting Office (GAO) of the agency information and data for accuracy.

6. Open public hearings and onsite visits by the Commission for major affected functions.

7. A set time frame for the Commission to finalize its review and make final recommendations to the President (in the case of BRAC, DOD sent the recommendations to the Commission by April 15 with the Commission's final recommendations due to the President by July 1).

8. A statutory test for any Commission modifications to the agency recommendations (in the case of BRAC, this was "substantial deviation" from the agency plan provided -- see 3 above -- and the criteria -- see 2 above).

9. A requirement for Presidential approval or disapproval after a two week review period of the Commission's recommendations. If approved, the report was sent to Congress; if disapproved, the report was sent back to the Commission which then had one month to submit a revised report to the President. The President then had 15 days to approve or disapprove. If no approval was received by September 1, the process ended.)

10. Once (and if) approved by the President, a set period for Congress to approve or disapprove the recommendations with no line item changes allowed.

11. Once approved, facilitated agency implementation through waiver of a number of statutory restraints.

12. Perhaps most important, however, the BRAC legislation for its duration, was the EXCLUSIVE authority for selection and closure or realignment of any military installation, except for specific actions already approved in law. This exclusivity was critical given numerous other statutory restraints on base closures.

NEXT STEPS

The declining Federal budgets and workforce of the 1990s challenge Federal agencies as never before to do business smarter and differently. Where outsourcing and divestiture may at one time have caused fear and loathing in Federal bureaucracies, they are seen today as critical to agency survival. As one DOD leadership report recently stated: "(w)e need to realize that the benefits of competition are not a luxury, but a necessity...."

Congress needs to similarly respond and give focus to this cultural readiness and provide the legislative leadership direction needed to guide its structure and cohesiveness.

The general parameters for such congressional leadership and action are outlined below.

"The Federal Outsourcing and Divestiture Act of 1998"

1. A single BRAC-like statute is needed to guide both civilian and defense agencies for 3 to 4 rounds of outsourcing and divestiture recommendations. No ongoing agency outsourcing or divestiture action should be halted that has been initiated under prior authorities, however, unless the agency determines it preferable to do so. Defining which ongoing actions are to be "grandfathered" potentially will be complex, but is critical to avoid hindering many agency initiatives already underway.
2. Agency plans for each round, which would be published for public comment before they are finalized, should be comprehensive, reflecting the current status of outsourcing/divestiture actions not covered by the Act, the new proposed functions to be outsourced under the Act, and the strategic planning on which the new proposals are based. The plans should also reflect the rationale for any outsourcing and divestiture action for which a public-private competition is not proposed using a business case analysis, and where such competitions are proposed, the plans should reflect the specific set of rules and procedures the agency will use to compare public and private sector bids (e.g., whether A-76 or rules unique to the agency such as DOD has for depot maintenance).
3. It is important that the legislation further revisit and strengthen the Senior Acquisition Executive function, renaming it the Chief Acquisition Officer (CAO), putting that individual on a par with the agencies' CFOs and CIOs, and holding the CAO accountable for implementation of this new Act. Throughout the implementation of BRAC, the Office of the Secretary of Defense maintained close coordination and oversight over the execution of the process by the military services. Such coordination provided for shared insights, innovations and consistency. By making each agency's newly reconstituted CAO responsible, each agency will have a central focal point both for accountability and for sharing of innovations and lessons learned.
4. Federal agencies should be given maximum authority to proceed in the most efficient manner possible with waiver of as many existing statutory constraints as feasible. Congress cannot possibly legislate all of the specific conditions for the functions proposed to be outsourced or divested under this Act as it previously has attempted to do. As with BRAC, the agencies must be allowed to propose the actions and methodologies they believe appropriate. Making the new Act the exclusive authority for the proposals made under its aegis would have the effect of suspending many of the barriers that currently constrain sound business decisions by the agencies, to include the new increase in percentage (50-50) of depot level maintenance and repair that can be contracted for performance by non-government personnel. In addition, specific to divestitures, the Act should permit

noncompetitive procedures when there is only one bidder expressing interest.

5. For DOD, the legislation should further provide for immediate and permanent authority for additional rounds (every two years) of base closings, and to include authority to privatize military base housing. Under current projections (baseline in 1989), by 2003 the defense budget will have declined by 40%, the force structure by 36%, but the domestic base structure by only 21%. Excess infrastructure continues to place an unconscionable drain on declining military resources to the detriment of national security. With two-thirds of military housing already provided by the private sector, there are still today approximately 200,000 DOD owned units that house soldiers in an unacceptable standard. If DOD relied on its own resources to fix these units, soldiers would wait 30 years. If DOD can proceed on a permanent basis with previously authorized privatization initiatives, the Pentagon estimates that all inadequate housing can be eliminated by 2010.

6. As an incentive (a critical component to this legislative initiative), all net cost savings achieved should be retained by the agencies to pay for identified modernization needs in the areas of management improvements, technological upgrades or innovations (to include DOD weapons systems), and acquisition workforce training.

SUMMARY

Outsourcing and divestiture are critical elements in the Federal government's entry to the 21st century. Federal agencies in the new millennium will continue to face dwindling budgets, a declining workforce, and the public's growing expectations and demands for improved service and efficiencies. The private sector is already successfully responding to such changes in an unprecedented decade of mergers, consolidations, reinventions, reengineerings, restructurings, outsourcings, and divestitures. The Federal government requires the same opportunity. The need is there; the cultural readiness for action is there. Congressional consensus and direction are needed to make it happen.

The Procurement Round Table stands ready to assist.

APPENDIX A --DEFINITIONS

In establishing legislation to guide Federal outsourcing and divestiture, Congress needs to standardize clear definitions to ensure that intent is met. The absence of standardized definitions has led to confusion and misuse. The PRT offers the following definitions for consideration. By these definitions, there are only two major ways by which Federally-funded activities can be transferred to the private sector: outsourcing or divestiture. Whether these definitions are accepted or not, the more important issue is to standardize semantics.

Outsourcing - involves transferring (or contracting out) activities that traditionally are being or have been performed in-house at in-house facilities to an outside activity provider; in the case of the Federal government, from federal employees at federal facilities to private contractor employees at federal or private facilities. (1)

Privatization - a subset of outsourcing that applies solely to the public sector and also typically involves transferring the control or ownership of assets (land, facilities, and/or equipment) from the public sector to private entities, or through providing vouchers. A subset of privatization is privatization-in-place (PIP) where an entire workforce, workload, and facility are transferred "as is" to a private sector contractor. Without assessing the workload and capacity before privatizing-in-place, however, costly inefficiencies can be perpetuated. For instance, a May 1997 GAO report estimated that operational costs at two Air Force depots could be \$182 million a year more per year than if the workload had been redistributed to other underutilized Air Force depots. (2)

Contracting Out - is essentially used synonymously with "outsourcing". The PRT, however, prefers the term outsourcing since "contracting out" carries a connotation that the function contracted out "belonged" to the Federal government in the first place.

Inherently Governmental Function - "means, as a matter of policy, a function that is so intimately related to the public interest as to mandate performance by Government employees....Governmental functions normally fall into two categories: the act of governing, i.e., the discretionary exercise of Government authority, and monetary transactions and entitlements." This definition is provided in the Final Rule to 48 CFR, Parts 7, 11, and 37, Federal Register, Vol. 61, No. 18, January 26, 1996, pages 2627-2630.

Commercial Activities - defined in this paper as all those governmental functions (activities) not determined to be "inherently governmental" and therefore eligible for outsourcing or divestiture.

Divestiture - involves divesting and no longer funding an activity or function previously performed in-house (can also include land, facilities and equipment). Divestiture entails a decision to get out of the business of performing and funding the divested service or function. Unlike outsourcing or privatization, pure divestitures are based on business analyses of core competencies and not based on A-76 competitions.

These definitions are consistent with a General Accounting Office, Glossary of Terms, July 1997.

APPENDIX B

OUTSOURCING AND DIVESTITURE MYTHS AND REALITIES

To further focus discussion on the issue of outsourcing and divestiture, the Procurement Round Table offers the following points for consideration to counter some of the current misconceptions which impede progress in this matter.

1. Federal Outsourcing and Divestiture Save Money--Reality

The issue of quantifying monetary savings from divestiture or outsourcing is easily challenged through accounting techniques, and opponents of specific outsourcing or divestiture initiatives are often successful in blocking such initiatives on this basis. However, consider the following:

- a. DOD estimates savings of 30-40% through outsourcing support services. Indeed, DOD has estimated that its current cost of performing commercial activities in-house by government employees is about \$23-30B annually and believes they can achieve the savings needed for modernization through outsourcing 1/2 to 2/3's of this workload by 2002. (3)
- b. Private sector savings from outsourcing in 1996 were estimated at 10-15% (source: Outsourcing Institute).
- c. The GAO found that public-private competitions for DOD depot-level maintenance generally resulted in savings. (4)
- d. In public-private sector competitions, GAO has stated that government costs are lower (i.e., the government wins the competition) about 40-50% of the time. (5)
- e. An OMB study of A-76 competitions from 1981-1988 cited average 20% savings when the Federal government won and 35% savings when the private sector won. (6)
- f. DOD reports that of the A-76 studies it undertook between 1979-1996, about half of the competitions were won by the government. (7)

Divestiture similarly produces cost savings. Reductions-in-force, military personnel drawdowns, base closures (which can be considered divestitures if the Federal government has stopped funding and performing a particular function) all have significant upfront costs to recoup, but have all resulted in long-term savings. Federal agencies like the Department of Veterans Affairs and Defense Logistics Agency that have divested themselves of warehousing and distribution functions for a variety of products and relied on private sector systems have all realized significant savings.

2. Outsourcing and Divestiture Cost Savings Can Be Disputed but ...--Reality

Despite such evidence as provided above, arguments still abound to counter savings achieved. For instance, in the case of military depots, the General Accounting Office (GAO) consistently questions excess capacity in the depot system for the function proposed for outsourcing. Indeed, GAO has estimated excess DOD depot capacity at 50% by FY 1999. Critics of specific depot outsourcing, mostly from Congress and/or the affected Federal workforce, state that any savings realized from outsourcing can be offset by not calculating into the cost equation the increased overhead of the underutilized depot capacity remaining. A practical remedy to this is to require excess Federal infrastructure capacity to be addressed as part of the requirements determination.

Another example from the private sector side is that public-private competitions are deemed essentially unfair because comparable cost estimates of direct and indirect costs between the public and private sectors are impossible under current

Federal cost accounting practices. This indeed can be true, but there is nothing that precludes Federal agencies from developing cost accounting practices which resolve this problem. DOD has done just that and reinstated public-private sector competitions in 1996, after a two year hiatus. Even without "apples to apples" comparisons, however, savings are still being achieved, and private sector firms are still winning the competitions 50-60% of the time. Just to get the issue of outsourcing off dead center, industry is increasingly demonstrating great equanimity when they lose public-private sector competitions. Rather than following the normal protest-as-usual, when the Warner Robins Air Logistics Center recently won a competition over Lockheed Martin and Boeing with a bid 6-7% less than was offered by the private sector, bidders for the \$434 million maintenance program for the C-5 actually touted the government's ability to effectively compete.

Statistics, particularly financial statistics, are slippery at best, and all of the above citations can indeed be countered in one fashion or another by one group or another. GAO consistently criticizes Federal agencies for achieving less savings than anticipated through outsourcing. The bottom line, however, is that competition produces savings whether it results in outsourcing, divestiture, or public sector contracting after competition.

3. Public-Private Competitions Are Unfair--Both Myth and Reality

Nothing spurs Federal agency efficiencies like a public-private sector competition, if the public involvement in the competition can be otherwise justified. The reason is simple: competition forces the agency to achieve a "most efficient" organization in order to compete.

Despite the fact that added efficiencies are achieved through public-private sector competitions, a strong case can be made that there should be no public-private sector competitions for commercial activities because of: (i) the lack of current direct and indirect cost comparability, and (ii) more importantly, because the Federal government, by policy, has no business competing in functions that are not "inherently governmental". Federal cost accounting procedures, however, can and need to be changed to reflect private industry practice. While the philosophical issue remains whether the Federal government should be involved at all in commercial activities, a realistic interim solution calls for allowing public-private competitions in outsourcing. Even though competition, whatever its limits, can and does produce cost savings, there will always be concerns about the level playing field. Ultimately, public-private competitions should give way to direct outsourcing or divestiture of commercial activities to the private sector.

4. Outsourcing and Divestiture are Just a Way to Cut Federal Jobs--Myth and Some Reality

During the 1970s and 80s, outsourcing and divestiture in the Federal government were viewed primarily as mechanisms to downsize government. The notion of the Federal government having to be competitive and be better at its "public service" than a private sector entity were somewhat alien thoughts. By policy (published for comment in December 1991 and finalized in March 1996), however, the Federal government is precluded from contracting or divesting "inherently governmental services". With such activities protected, why shouldn't the remaining functions be provided by whomever can provide the taxpayers with the best service for the best price?

The reality is that the issue is not about replacing Federal workers with private sector workers. The issue is about competition, and in such competitions, Federal workers should take distinct pride that they win 40-50% of the time. In those instances where the private sector wins, a 1989 Department of Labor analysis on "The Long-Term Employment Implications of Privatization" found that only 7% of Federal government workers had been laid off due to outsourcing decisions, with more than 58% gaining work with the new private sector company, 24% transferred to other government work, and 7% retiring.

The Congressional Budget Office has estimated that 1.4 million Federal employees are engaged in activities which can be deemed "commercial".

5. Federal Outsourcing/Divestiture are Means to an End--Reality

While it may be philosophically cathartic to recall national concepts of free enterprise, limited Federal powers, and the 200+ year old debates and intentions of our Founding Fathers, outsourcing and divestiture in terms of the Federal government are a practical approach to freeing up needed resources. Philosophical debate has contributed to a hardening of positions on the subject. More to the point, Federal budgets, particularly in the acquisition field, have diminished substantially. In reality,

outsourcing today (and the even bolder initiative of divestiture) represent a unique and substantial potential for obtaining resources needed to meet critical Federal needs.

For instance, budget support for DOD equipment modernization has declined nearly 70% since FY 1985, even with inclusion of the military services' first real net savings from BRAC in 1996. Further force structure reductions pose significant risk, national military readiness is in jeopardy, and further base closures are unlikely in the near future. Where else will the critical resources needed for modernization come? DOD has estimated that aggressive outsourcing could generate savings of up to \$7-12 billion annually by FY 2002. Again, GAO, or anyone else, can dispute the projected savings, but whether it is billions or millions, it is "real money" that can be applied to meet critical military modernization needs. Civilian Federal agencies recognize the same potential.

6. Outsourcing and Divestiture are Standard in the Private Sector--Reality

While political angst and incalculable Presidential and Congressional commissions, hearings, conferences, reports and task forces continue to characterize any serious attempts to substantially outsource or divest Federal functions, the private sector has been doing it for decades, has demonstrated that it works, and recognize that outsourcing and divestiture are critical if they are to survive in a rapidly changing world economy and marketplace. Outsourcing and divestiture decision-making, in the private sector, is not rocket science, not a new management mantra, and is not a new fad. Only entrenched federal sector business practices, supported by legislative and regulatory impediments, have made it regrettably seem so in the Federal sector.

7. Outsourcing and Divestiture are Federal Policy--Reality

Federal policy, for over 40 years, has been and remains clear: "the Federal Government will not start or carry on any commercial activity to provide a service or product for its own use if such product or service can be procured from private enterprise through ordinary business channels" (Bureau of the Budget, 1955). Clarity of policy, however, is rarely sufficient.

The old adage: "where there is a will, there's a way" applies more to tough decisions. The Base Closure and Realignment Acts (P.L. 100-526 and P.L. 101-510) that resulted in 4 rounds of base closings after a 10 year hiatus are an excellent example of that adage.

8. Federal Impediments to Outsourcing and Divestiture are Numerous--Reality

Despite stated policy, Federally performed and funded functions are protected like the Queen's crown jewels, both by the Executive and Legislative branches of government. The most onerous of the barriers to overcome include, but are by no means limited to:

a. Time consuming and complicated acquisition regulations and practices, including OMB Circular A-76 (first adopted in 1966). To quote the August 1996 DOD report on "Outsourcing and Privatization", this circular "mandates a cumbersome, time-consuming, and legalistic process that discourages DOD activities from initiating outsourcing actions". The recommendation in this DOD report is to make the "detailed administrative procedures established in A-76...advisory, not mandatory...."

b. OMB scoring rules which require Federal agencies to account for all liabilities in the first year preclude the standard business practice of amortizing these over a period of time.

c. Congressional micro management through such legislative restrictions as the "60-40" rule (10 U.S.C. 2464, wherein not more than 40% of annual depot-level maintenance funding in DOD can be used for private sector performance, recently revised to the 50-50 rule) and numerous other statutory impediments. The issue here is that Congress has mandated a percentage of workload in-house that had nothing to do with capability or reliability or cost effectiveness. Why? Presumably because of constituent jobs but a large percentage of those same constituents can and do still, perform those jobs through privatization. The real question that should be asked is: Is the function being performed in the most efficient and effective fashion, not who is performing it.

d. Executive branch reluctance to fully implement statutory authorities, e.g., the requirement for civilian

agencies to "fence" a budgetary line item for acquisition workforce training. DOD requested a \$100M line item in FY 98 for the Defense Acquisition University. The civilian agencies should have budgeted a comparable \$20M. They didn't. While this lack of action may not be perceived as having an immediate impact on Federal outsourcing and divestiture, a direct relationship between a well-trained acquisition workforce and its effectiveness in such specialized contracting is documented. In a GAO report, "PRIVATIZATION: Lessons Learned by State and Local Governments" (GAO/GGD-97-48, March 14, 1997), GAO noted that the majority of state and local officials and experts that they surveyed "said that having qualified employees with specific skills related to privatization was important to successfully implementing privatization."

e. Poor government cost accounting capabilities which are more an excuse for nonaction than reform.

f. Cumbersome, confusing and inconsistent rules and procedures that burden and delay outsourcing and divestiture action. It is interesting to note that Operations Desert Shield/Desert Storm were accomplished in far less time than it takes DOD to do a simple A-76 process for "simple, narrow functions requiring only the submission of sealed bids". The United States victory in WWII took not much more time than it normally takes DOD to do a more complex or multiple function A-76 process. As a consideration regarding outsourcing or divestiture, these time frames seem, at the very best, unseemly.

g. Lack of incentive. Beyond the growing internal motivation to increase outsourcing and divestiture to address declining agency budgets, Congress has yet to provide perhaps the most critical incentive: allow the Federal agencies to retain all of the net cost savings from outsourcing and divestiture actions to meet specified, high priority needs which could be annually reported to Congress and evaluated as part of a GAO audit.

FOOTNOTES

- (1) Agnes P. Dover, Briefing Papers, Federal Publications, "Outsourcing and Privatization: Recent Developments," March 1997. Also, see Report of the Defense Science Board Task Force, "Outsourcing and Privatization," August 1996
- (2) Ibid.
- (3) Defense Science Board Task Force, "Outsourcing and Privatization," August 1996
- (4) GAO Report, "Defense Depot Maintenance," July 1996 (GAO/NSIAD-96-161)
- (5) Ibid.
- (6) Ibid.
- (7) Defense Reform Initiative Report, November 1997.