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DURING THE

PANEL DISCUSSION ON THE SERVICE CONTRACT ACT

AT THE

NATIONAL CONTRACT MANAGEMENT ASSOCIATION'S
MID-WINTER REGIONAL SYMPOSIUM IN MELBOURNE, FLORIDA

FEBRUARY 12-13, 1981

I am pleased to be here today to participate in this panel discussion of the Service Contract Act. In particular I would like to discuss the recently issued General Accounting Office report entitled, "Service Contract Act Should Not Apply to Service Employees of ADP and High-Technology Companies."

LABOR'S SERVICE CONTRACT ACT DECISION

On June 5, 1979, the Department of Labor notified the General Services Administration (GSA) that the maintenance and repair service specifications of all contracts for the purchase or rental of supplies or equipment were subject to the Service Contract Act (SCA), thereby denying GSA's request that such contracts be temporarily exempted from SCA and the prevailing wage determinations issued by Labor.

Soon thereafter, several major automatic data processing (ADP) manufacturers publicly announced their refusal to bid on or enter into any Government contract subject to SCA coverage. Other firms appeared ready to follow suit. Recognizing the industry concerns, congressional and Federal agency pressures were brought to bear on Labor to exercise its authority under

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the act and grant an administrative exemption for the ADP, telecommunications, and other high-technology commercial equipment industries. On August 10, 1979, Labor granted a 90-day temporary exemption from SCA coverage, but only for ADP and telecommunications equipment purchase or rental contracts falling within the purview of the Brooks Act (Public Law 89-306). Specific contracts for maintenance and repair services only and those involving other high-technology commercial products were not covered by the temporary exemption.

At the end of the 90-day exemption period (November 8, 1979), the Secretary of Labor decided not to further extend the Department's exemption for the ADP and telecommunications industry. Since then, the Labor Department has required that all bid or proposal packages and all contracts having maintenance and repair specifications must contain the applicable SCA provisions, including appropriate wage and fringe benefit rate determinations.

To minimize the initial impact of its decision and to buy time while appropriate wage and fringe benefit data could be gathered from the ADP industry, on November 30, 1979, the Labor Department issued an interim, nationwide wage determination covering ADP maintenance and repair services only. This determination accepted the currently paid wages and fringe benefits as being those deemed by Labor to be prevailing for such services in the ADP industry. Nevertheless, some major manufacturers continued to reject Government contracts subject to SCA coverage.

THE COMMITTEE'S REQUEST

Recognizing that Labor's SCA decision and the computer manufacturers' refusals to contract with the Government could seriously affect the maintenance and repair of the Government's enormous inventory of computers--more than 14,300 as of September 30, 1979--many of which are critical to our national defense and security, on November 23, 1979, the Chairman of the House Committee on Government Operations asked the General Accounting Office to review Labor's decision to apply SCA to ADP and telecommunications products.

On January 29, 1980, Congressman Frank Horton, the Committee's Ranking Minority Member, requested that we broaden our study to cover other high-technology commercial equipment industries directly affected by Labor's June 1979 notification to GSA.

REVIEW OBJECTIVES AND SCOPE

Our review objectives were to:

--Determine and assess the rationale for Labor's June 1979 SCA exemption denial decision.

--Determine the cost and other impacts, if any, of Labor's SCA decision on both Government and contractor operations.

--Assess the merits of industry arguments that they should be exempted from SCA coverage.

--Assess the need for administrative and/or legislative actions to equitably resolve the various issues involved.

In performing our review, we contacted 114 Federal contracting agencies located in 26 States and the District of Columbia, and we

visited 42 of those locations. We also contacted or visited 18 companies--all of them being Government contractors--that manufacture, sell, and service ADP or other high-technology commercial equipment, as well as several major trade associations, including the Computer and Business Equipment Manufacturers Association, the Scientific Apparatus Makers Association, and the National Micrographics Association.

In addition, we interviewed key headquarters officials and obtained pertinent documentation from the Department of Labor's Employment Standards Administration, GSA's Automated Data and Telecommunications Service, the Department of Defense, and the National Aeronautics and Space Administration.

LABOR'S DECISION INAPPROPRIATE

The Department of Labor contends that the act applies to all contracts, as well as any contract specification, whose principal purpose is to provide services through use of service employees. Labor's position relies on its interpretation of the act. While acknowledging that no remedial purpose will be served by applying SCA to ADP and other high-technology industries, Labor believes none is required since it interprets the act as applying to all contracts that contain specifications for services provided to the Government by service employees. Accordingly, Labor has not made any studies of the impact of SCA on (1) contractors' recordkeeping systems, pay practices, employee assignment practices, and the costs of compliance or (2) Government operations if agencies are unable to acquire needed services.

We believe that Labor's position is not supported by the act's language and legislative history, by Labor's own regulations, or by its administrative manual. The Service Contract Act was not intended to cover maintenance services related to commercial products acquired by the Government. ADP, high-technology, and other commercial product-support service contracts, where Government sales represent a relatively small portion of a company's total sales, do not have the same characteristics, or incentives, for contractors to deliberately pay low wages to successfully bid on Government contracts.

Accordingly, Labor's application of the act to contractor services sold primarily in the commercial sector, such as provided by ADP and other high-technology industries, in our view, is inappropriate.

LABOR'S WAGE PROTECTION UNNEEDED

The industries' central argument, that the act's application to commercial product-support services is not needed, has merit. All of the 18 corporations we contacted stressed their belief that the act's intent was not to cover industries providing commercial product-support services to the Government at established catalog prices. Of these corporations, 17 presented convincing evidence through financial statements, payroll records, price catalogs, and other documents that the act should not apply because:

--Substantial quantities of their products and services are sold commercially at established catalog prices.

--Government business represents a small portion (for some, 1 percent) of their total business.

--Their field service technicians receive adequate wages under merit pay systems, thereby eliminating the need for wage protection.

The most significant force behind the act was the Congress' desire to eliminate "wage busting" and prevent payment of substandard wages to persons whose employment either totally or substantially depended upon Government contracts awarded solely on the basis of price competition. Industry contends, Labor officials acknowledge, and our review has confirmed, that wage busting is not a problem in these industries.

INDUSTRY COMPLIANCE WOULD BE COUNTERPRODUCTIVE AND COSTLY

The most serious concerns presented by the 18 corporations we contacted were that Labor's decision would eventually:

--increase the administrative burdens and operating costs of each corporation and

--hinder employee productivity and morale by disrupting merit pay systems and staff assignment practices.

In addition, several corporations stressed the inflationary impact Labor's wage determinations could have on the industries' wage rates.

One corporation said a new system estimated to cost almost $1 million would be needed to track data on employees servicing approximately 700,000 of its machines within the Government. This corporation also stated that, to maintain its merit pay system and still comply with the act, a separate work force would have to be created to service its Federal contracts. To do this, the corporation estimated it would incur developmental and

implementation costs of more than $9 million--including the $1 million for a new data system--and annual recurring costs of $3.3 million.

Another corporation estimated that the cost to develop and implement new data processing systems and modify existing systems would be $1.5 to $2 million. A third corporation estimated the cost to design, develop, and install its system at over $1 million, with annual maintenance costs of $250,000.

Regarding inflationary impact, one corporation said the first-year impact on its field service technician wages would be $648,000. Another corporation estimated the impact at $12 million. A third and much larger corporation said the inflationary impact on technician wages would be $100 million the first year.

One major high-technology corporation uses varying salary groups, each with salary ranges for merit promotion, to provide geographic area differentials in salaries based on the cost of living in those areas. Corporate officials estimated the inflationary impact of SCA to be between $50 million and $100 million if their employees were paid at least the median salary rate reflected in two of their geographic areas.

Since issuance of our report, a fifth corporation has advised us that SCA prevailing wage determinations would produce a first-year inflationary impact on its service technician wages of almost $20 milli

Such increases in service technicians' wages would undoubtedly be reflected in future prices to customers for equipment maintenance and repair services.

IMPACT ON FEDERAL AGENCY OPERATIONS

To obtain information on the act's impact on Federal agency operations, we contacted 114 Federal installations. At 42 of these installations, contracting difficulties developed because contractors refused to accept contracts subject to the act.

To minimize impact or avoid shutdown of programs and activities, agency contracting officials either awarded contracts during Labor's 90-day exemption period or circumvented the act by:

--Issuing numerous purchase orders valued under $2,500.

--Designating service technicians as exempt professionals.

--Exercising contract options, extending terms, or adding to the scope of existing exempt contracts, sometimes due to misinterpretation of instructions.

Some agencies that had previously contracted directly with vendors for ADP maintenance services, often at substantial discounts, began issuing delivery orders against GSA's exempt fiscal year 1980 ADP schedule contracts.

Not all of these efforts were successful in minimizing the impact. For example, the Army Corps of Engineers in Vicksburg, Mississippi, had to shut down its $12 million computer system because the sole-source contractor would not accept a follow-on maintenance contract containing SCA provisions. The system is expected to be scrapped, and replacement computer services are being obtained from other sources at much higher cost and considerable inconvenience.

Various Federal officials cited other impacts they believed would occur if maintenance and repair services under expiring

contracts were discontinued and could not be renewed. Presently, however, many of the major corporations that have strongly objected to coverage under the act in any form appear willing to accept contracts containing Labor's interim wage determination, including GSA's fiscal year 1981 ADP schedule contracts.

LABOR'S RECOGNITION OF INDUSTRY CONCERNS

The Department of Labor recognizes that (1) SCA prevailing wage determination rates, by their very nature, affect merit pay practices; (2) legitimate merit pay systems do exist in the industry; and (3) to the extent feasible, Labor should not permit its normal administrative practices under SCA to destroy those systems. Labor's November 30, 1979, interim wage determination, allowing the ADP industry to continue paying their service employees the wage rates and fringe benefits currently being paid, was a tangible recognition of Labor's desire not to disrupt or destroy industry merit pay practices.

Between December 1, 1979, and mid-June 1980, Labor attempted to issue a specific wage rate for entry-level field service technicians, based on the Bureau of Labor Statistics' reported median wage of Class C electronic technicians. Labor had hoped that this variance from its normal SCA wage determination practices would meet industry concerns while allowing Labor to carry out its SCA enforcement responsibilities. However, the industry opposed this effort. Moreover, industry data obtained during our review showed that application of Labor's proposed entry-level rate would have disrupted the merit pay and staff assignment practices of a large segment of the industry.

On June 17, 1980, Labor abandoned, at least temporarily, its proposed entry-level wage determination in favor of issuing a revised expanded version of the earlier interim wage determination, to cover maintenance services not only for ADP equipment but also scientific and other high-technology equipment. Concurrently, Labor issued a separate wage determination, also patterned after the interim determination, to cover maintenance and repair specifications under GSA's Federal Supply Service schedule contracts for purchase or rental of automated office and business machines and related equipment. These actions, in our view, are a further indication of the difficulty of satisfactorily resolving the problem.

If the Labor/industry basic disagreement on the act's coverage is not permanently resolved, we believe the future impact on Federal agency programs and operations and on the affected industries could be severe.

RECOMMENDATIONS

Accordingly, we have recommended that the Congress amend the Service Contract Act to make it clear that the act excludes coverage for ADP and other high-technology commercial product-support services.

Pending such action by the Congress and to avoid further serious impairment to the conduct of Government business, we have recommended that the Secretary of Labor temporarily exempt from the act's coverage contracts and contract specifications for such services.

In closing, I would like to thank Ralph Brubaker and the Cape Canaveral Chapter of NCMA for inviting me to participate in this panel discussion of the Service Contract Act. During the question and answer period I will be happy to respond to any questions you may have about our report.