H.R. 4244, FEDERAL ACTIVITIES INVENTORY REFORM ACT

HEARING

BEFORE THE

SUBCOMMITTEE ON GOVERNMENT MANAGEMENT, INFORMATION, AND TECHNOLOGY

OF THE

COMMITTEE ON GOVERNMENT REFORM AND OVERSIGHT HOUSE OF REPRESENTATIVES

ONE HUNDRED FIFTH CONGRESS

SECOND SESSION

ON

H.R. 4244

TO AMEND THE OFFICE OF FEDERAL PROCUREMENT POLICY ACT (41 U.S.C. 401 ET SEQ.) TO PROVIDE FOR MEASUREMENT OF THE PERFORMANCE OF THE FEDERAL PROCUREMENT SYSTEM, TO ENHANCE THE TRAINING OF THE ACQUISITION WORKFORCE, AND FOR OTHER PURPOSES

AUGUST 6, 1998

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H.R. 4244, FEDERAL ACTIVITIES INVENTORY REFORM ACT

THURSDAY, AUGUST 6, 1998

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON GOVERNMENT MANAGEMENT,
INFORMATION, AND TECHNOLOGY,
COMMITTEE ON GOVERNMENT REFORM AND OVERSIGHT,
Washington, DC.

The subcommittee met, pursuant to notice, at 2:15 p.m., in room 2247, Rayburn House Office Building, Hon. Stephen Horn (chairman of the subcommittee) presiding.

Present: Representative Horn, Sessions, Lewis, and Kucinich.

Staff present: J. Russell George, staff director and chief counsel; Mark Brasher, senior policy director; Matthew Ebert, clerk; and Julie Moses and Faith Weiss, minority professional staff members.

Mr. SESSIONS [presiding]. I apologize for being late. I'm going to make an opening statement after your testimony.

STATEMENT OF HON. JOHN J. DUNCAN, JR., A REPRESENTATIVE IN CONGRESS FROM THE STATE OF TENNESSEE

Mr. DUNCAN. Thank you very much. I appreciate that. I would like to thank you for the invitation to be here with you today.

As you know, this committee accepted an amendment to H.R. 4244 a couple of weeks ago, which I understand is some Federal procurement legislation. This amendment contained most of the provisions of legislation which I have introduced in the House, H.R. 716, the Freedom from Government Competition Act. This amendment was offered by Representative Pete Sessions, and I would like to personally thank him for all of his interest and hard work on this issue.

The provisions included in the amendment are a scaled-back version of the original bill that I introduced. Recently the Senate passed this scaled-back version unanimously, and this legislation was introduced by our friend, Senator Craig Thomas, over in the Senate and has received strong support and bipartisan support in the Senate. The legislation in the House currently has 66 cosponsors, and it is, I think, mostly significantly supported by over 100 associations and organizations. Those are such a wide variety that I won't take the time to list all of them today, but I will tell you that some of these organizations include the U.S. Chamber of Commerce, the National Federation of Independent Business, and many, many others.

In addition, the Small Business Office of Advocacy supports these efforts to end unfair government competition with the private sec-

tor. The last time the White House Conference on Small Business met, it listed unfair competition with government agencies as one of it's very, very top concerns. Furthermore, Ms. Karen Hasty William, the Administrator of the Office of Federal Procurement Policy under President Carter, also has endorsed this bill.

The problem of government competition with a small business is not a new one. In fact, since the Eisenhower administration, it has been official U.S. policy promulgated in 1955 that "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." Every administration, Republican and Democratic, for the past 40 years has endorsed this policy, but, unfortunately, it has never been implemented; it has been more lip service.

Let me briefly explain the most recent draft of this bill and how it will address this problem. Simply put, this legislation will require Federal agencies to prepare a list of activities which are not inherently governmental functions that are being performed by a Federal employee. These lists are then to be submitted to the Office of Management and Budget for review and consultation. In addition, this legislation will make these lists public and require Federal agencies to give consideration to private sector sources for providing these goods and services. It does not make or require that the Federal agencies contract everything out. In fact, the bulk of the activities of most departments and agencies would continue as present, I would feel certain, even under this legislation.

I recognize that there are things that government does best, and that there are functions that only the government should do. This legislation requires only that Federal agencies look at those things they do presently, which are commercial in nature. If these commercial goods and services can be obtained from the private sector in a more efficient and, much more importantly, cost-effective manner, then, and only then, would the agency give consideration to contracting out that work. The goal of this legislation is to ensure that the public receives the best goods and services at the lowest cost to the taxpayers. In the long run, I think this legislation will help us do just that.

Within the last couple of years, for instance, the Defense Science Board found that $30 billion could be saved each year if the Department of Defense did more contracting out; $30 billion a year is a lot of money, even here in Washington, DC. This is $30 billion we would not have to ask the American public to send to Washington every year.

The Heritage Foundation and many other organizations have made similar estimates about cost-savings throughout the government. I think all of us would agree that the American public wants the Federal Government to improve the services it provides without increasing taxes.

Mr. Chairman, I would like to conclude by quoting one of our Founding Fathers, a great American, Thomas Jefferson, who once said, "It's better for the public to procure at the common market, whatever the market can supply, because there it is by competition kept up in its quality and reduced to its minimum price."

Mr. Chairman, I want to thank you again for giving me the opportunity to come here to explain why I believe that it is very important that the Congress pass this legislation. I can say, finally, that I personally, for a long time, have felt that we should almost pin a medal on anyone who survives in small business in this country today. Now, it seems to be that it's difficult even for medium-sized businesses to survive. I can tell you from many, many contacts throughout this Nation, and talking to many people, that it's tough enough for businesses to survive against ordinary competition, but when they have to take on their own government to boot, it becomes almost too much for many of them to handle. So this in a small way would help alleviate what has become a very, very serious problem. It would not only help the small to medium-sized businesses, but it would help the U.S. taxpayer.

I thank you for letting me come here today, and I thank you for your support for this very moderate attempt to help alleviate to some extent a very major problem.

[The prepared statement of Hon. John J. Duncan Jr. follows:]

I would like to thank the Chairman and Ranking Member for giving me the opportunity to come here today.

As you know, this Committee accepted an amendment to H.R. 4244.

This amendment contained provisions of legislation which I have introduced in the House, H.R. 716, the Freedom From Competition Act.

It was offered by Rep. Pete Sessions, and I would like to personally thank him for all his interest and hard work on this issue.

The provisions included in the amendment are very scaled back from the original bill I introduced.

Recently, the Senate passed the scaled back version of this bill by unanimous consent.

This legislation is bipartisan, with 66 cosponsors, and it is supported by over 100 associations and organizations.

Some of these organizations include the U.S. Chamber of Commerce, the National Federation of Independent Business, and many many others.

In addition, the Small Business Office of Advocacy supports these efforts to end unfair government competition with the private sector.

The last time the White House Conference on Small Business met, it listed unfair competition with government agencies as one of its top concerns.

Furthermore, Ms. Karen Hastie Williams, the Administrator of the Office of the Federal Procurement Policy under President Carter, also supports this bill.

The problem of government competition is not a new one.

In fact, since the Eisenhower Administration in 1955, it has been U.S. policy that:

> "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."

Every Administration, Republican and Democrat, for the past 40 years, has endorsed this policy, but unfortunately, it has never been implemented.

Let me briefly explain the most recent draft of this bill and how it will address this problem.

Simply put, this legislation will require federal agencies to prepare a list of activities which are not inherently governmental functions that are being performed by federal employees.

These lists are then to be submitted to the Office of Management and Budget for review and consultation.

In addition, this legislation will make these lists public and require federal agencies to give consideration to private sector sources for providing these goods and services.

It does not make the federal agencies contract everything out.

I recognize that there are things that government does best and that there are functions that only government should do.

It requires only that federal agencies look at those things they do which are commercial in nature.

If these commercial goods and services can be obtained from the private sector in a more efficient and cost-effective manner, then, and only then, would the agency give consideration to contracting out that work.

The goal of this legislation is to ensure that the public receives the best good or service at the lowest cost to the taxpayers.

In the long run, I think this bill will help us do just that.

Within the last couple years, the Defense Science Board found that $30 billion could be saved annually if the Department of Defense did more contracting out.

$30 billion a year is a lot of money even in Washington terms.

This is $30 billion that we would not have to ask the American public to send to Washington every year.

I think all of us would agree that the American public wants the federal government to improve the services it provides without increasing taxes.

Mr. Chairman, I would like to conclude by quoting one of our Founding Fathers, Thomas Jefferson, who once said:

> "It is better for the public to procure at the common market whatever the market can supply; because there it is by competition kept up in its quality and reduced to its minimum price."

Mr. Chairman, I want thank you again for giving me the opportunity to come here today to explain why I believe it is imperative that the Congress pass this legislation.

Mr. HORN. Well, we appreciate very much you taking the time to come. We know the tremendous hours you've spent on your legislation, and we thank you for following it, and all the niches and crannies the Congress can dream up for any piece of legislation. So thank you for coming.

Mr. DUNCAN. Thank you very much, Mr. Chairman.

Mr. HORN. You're welcome.

I'm going to read my opening statement now into the record, basically. Then when Mr. Sessions, the vice chairman comes, he can continue the hearing, if he gets back first from the floor.

Our hearing today will examine title II of H.R. 4244, the Federal Activities Inventory Reform Act. This title represents an amendment by Representative Pete Sessions. This topic has been the subject of previous hearings in the subcommittee in September 1997 and March 1998. Hopefully, our witnesses will be able to shed additional light on a much-debated topic.

[The text of H.R. 4244 follows:]

I

105TH CONGRESS
2D SESSION

H. R. 4244

To amend the Office of Federal Procurement Policy Act (41 U.S.C. 401 et seq.) to provide for measurement of the performance of the Federal procurement system, to enhance the training of the acquisition workforce, and for other purposes.

IN THE HOUSE OF REPRESENTATIVES

JULY 16, 1998

Mr. HORN (for himself, Mrs. MALONEY of New York, Mr. DAVIS of Virginia, Mr. SESSIONS, and Mr. KANJORSKI) introduced the following bill; which was referred to the Committee on Government Reform and Oversight, and in addition to the Committee on National Security, for a period to be subsequently determined by the Speaker, in each case for consideration of such provisions as fall within the jurisdiction of the committee concerned

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A BILL

To amend the Office of Federal Procurement Policy Act (41 U.S.C. 401 et seq.) to provide for measurement of the performance of the Federal procurement system, to enhance the training of the acquisition workforce, and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. SHORT TITLE; TABLE OF CONTENTS.

(a) SHORT TITLE.—This Act may be cited as the "Federal Procurement System Performance Measurement and Acquisition Workforce Training Act of 1998".

(b) TABLE OF CONTENTS.—The table of contents for this Act is as follows:

SEC. 2. ESTABLISHMENT OF PERFORMANCE MEASURES FOR THE FEDERAL PROCUREMENT SYSTEM.

(a) PERFORMANCE MEASURES.—The Office of Federal Procurement Policy Act (Public Law 93–400; 41 U.S.C. 401 et seq.) is amended by adding at the end the following new section:

"SEC. 39. PERFORMANCE MEASURES FOR THE FEDERAL PROCUREMENT SYSTEM.

"(a)(1) The Administrator shall establish a system for measuring the performance and effectiveness of the procurement system, including standards for measuring the performance of the various elements of the system. The performance standards shall be structured—

"(A) to enable the Congress, the Office of Federal Procurement Policy, and the heads of executive agencies to track progress of achievement of acquisi-

tion reform objectives on a Government-wide basis and to gauge the effectiveness of the procurement system in supporting the accomplishment of the mission of such agencies; and

"(B) to benchmark the performance of executive agencies against the performance of private and public sector procurement operations.

"(2) The objective of the procurement performance measurement system shall be to use the performance data to improve executive agency acquisition practices and policies in order to enhance support for the accomplishment of the mission of such agencies.

"(3) In developing and implementing the procurement performance measurement system, the Administrator shall, to the maximum extent practical, use existing data sources and automated data collection tools.

"(b)(1) The head of each executive agency for which more than 50 percent of the funds appropriated are expended for procurement shall include, as a part of the annual performance plan of the agency submitted under section 1115 of title 31, United States Code, an assessment of the performance of the procurement system of the agency in terms of its efficiency and effectiveness in supporting the agency in accomplishing its mission.

"(2) The assessment required under paragraph (1) shall—

"(A) address corrective actions and activities planned by the agency to improve the performance of the procurement system of the agency;

"(B) address the adequacy of the education and training of the acquisition workforce of the agency, including whether the workforce has the necessary competencies, skills, and knowledge to effectively support the achievement of the mission of the agency and information on the amount of funds budgeted and expended to ensure that the acquisition workforce of the agency is appropriately educated and trained; and

"(C) evaluate the effectiveness of acquisition workforce training programs in providing necessary competencies, skills, and knowledge.

"(c) The Administrator may require the heads of executive agencies that are not required to submit a performance plan under section 1115 of title 31, United States Code, to submit an assessment to the Administrator similar to the assessment described in subsection (b).".

(b) CONFORMING AMENDMENT.—The table of contents of such Act is amended by adding at the end the following new item:

"Sec. 39. Performance measures for the Federal procurement system."

SEC. 3. PROFESSIONALISM OF THE ACQUISITION WORKFORCE.

(a) MANDATORY TRAINING AND EDUCATION.—Section 37(f)(3) of the Office of Federal Procurement Policy Act (41 U.S.C. 433(f)(3)) is amended to read as follows:

"(3) MANDATORY TRAINING AND EDUCATION.—The head of each executive agency shall establish, for each career path, requirements for initial and continuing education in the critical acquisition-related duties and tasks of the career path. Such requirements shall include, at a minimum, the core curriculum, continuing education programs, and policy implementation training required by the Federal Acquisition Regulation.".

(b) ACQUISITION WORKFORCE.—Section 37(e) of the Office of Federal Procurement Policy Act (41 U.S.C. 433(e)) is amended to read as follows:

"(e) APPLICABILITY TO ACQUISITION WORKFORCE.—The programs established by this section shall apply to the acquisition workforce of each executive agency. For purposes of this section, the acquisition workforce of an agency consists of—

"(1) all employees serving in acquisition positions listed in subsection (g)(1)(A) of this section;

"(2) program managers with significant acquisition responsibilities;

"(3) contracting officers and contracting officer representatives with authority to award or administer contracts for amounts above the micro-purchase threshold; and

"(4) other Federal employees who are assigned significant acquisition roles and responsibilities.".

(c) CONTRACTING OFFICERS.—(1) Section 37(g) of the Office of Federal Procurement Policy Act (41 U.S.C. 433(g)) is amended by adding at the end the following new paragraph:

"(4) CONTRACTING OFFICERS.—(A) Beginning on October 1, 2000, the head of each executive agency shall require, in order to serve as a contracting officer with authority to award or administer contracts for amounts above the micro-purchase threshold, the following:

"(i) For appointments to serve as a contracting officer with authority to award or administer contracts that do not exceed the simplified acquisition threshold as specified in section 4(11) of the Office of Federal Procurement

Policy Act (41 U.S.C. 403(11)), completion of training in duties related to use of the simplified acquisition procedures authorized to be used under the appointed position (including any training mandated for such duties by the Federal Acquisition Regulation) and such additional requirements, based on the dollar value, nature, and complexity of the contracts awarded or administered pursuant to the appointment, as may be established by the Federal Acquisition Regulation or the appointing agency head.

"(ii) For appointments to serve as a contracting officer with authority to award or administer contracts for amounts above the simplified acquisition threshold as specified in section 4(11) of the Office of Federal Procurement Policy Act—

"(I) completion of the core curriculum established in the Federal Acquisition Regulation for contracting officers;

"(II) at least 2 years experience in a contracting or purchasing position;

"(III) satisfaction of other qualification requirements for contracting or pur-

chasing positions at the same grade level established under paragraph (1)(A); and

"(IV) such additional requirements, based on the dollar value, nature, and complexity of the contracts awarded or administered pursuant to the appointment, as may be established by the Federal Acquisition Regulation or the head of the agency for the appointment.

"(B)(i) The head of the executive agency may waive any of the requirements in subparagraph (A) (except those contained in qualifications standards approved by the Office of Personnel Management under subsection (g)(3)) with respect to an employee of the agency if the agency head determines that the employee possesses significant potential for advancement to levels of greater responsibility and authority, based on demonstrated job performance and qualifying experience.

"(ii) The head of the agency shall provide to the administrator in writing the rationale for any decision to waive such requirements.".

(2) Section 1724(a) of title 10, United States Code, is amended to read as follows:

"(a) CONTRACTING OFFICERS.—Beginning on October 1, 2000, the Secretary of Defense shall require, in order to serve as a contracting officer with authority to award or administer contracts for amounts above the micro-purchase threshold as specified in section 32(g) of the Office of Federal Procurement Policy Act (41 U.S.C. 428(f)), the following:

"(1) For appointments to serve as a contracting officer with authority to award or administer contracts that do not exceed the simplified acquisition threshold as specified in section 4(11) of the Office of Federal Procurement Policy Act (41 U.S.C. 403(11))—

"(A) completion of training in duties related to use of the simplified acquisition procedures authorized to be used by the appointment (including any training mandated for such duties by the Federal Acquisition Regulation); and

"(B) such additional requirements, based on the dollar value, nature, and complexity of the contracts awarded or administered pursuant to the appointment as may be established under the Federal Acquisition Regulation or by the Secretary of Defense for the appointment.

"(2) For appointments to serve as a contracting officer with authority to award or administer contracts for amounts above the simplified acquisition threshold as specified in section 4(11) of the Office of Federal Procurement Policy Act (41 U.S.C. 403(11))—

"(A) completion of the core curriculum established in the Federal Acquisition Regulation for contracting officers;

"(B) at least 2 years experience in a contracting or purchasing position;

"(C)(i) a baccalaureate degree from an accredited educational institution authorized to grant baccalaureate degrees;

"(ii) completion of at least 24 semester credit hours (or the equivalent) of study from an accredited institution of higher education in accounting, business, finance, law, contracts, purchasing, economics, industrial management, marketing, quantitative methods, and organization and management; or

"(iii) passage of an examination considered by the Secretary of Defense to demonstrate skills, knowledge, or abilities comparable to that of an individual who has completed at least 24

semester credit hours (or the equivalent) of study from an accredited institution of higher education in any of the disciplines listed in subparagraph (ii); and

"(D) such additional requirements, based on the dollar value, nature, and complexity of the contracts awarded or administered pursuant to the appointment, as may be established by the Federal Acquisition Regulation or the Secretary of Defense for the appointment.".

(d) QUALIFICATIONS STANDARDS.—Section 1724(b) of title 10, United States Code, is amended by adding at the end the following new sentence: "The Secretary of Defense shall also require employees to meet any additional qualification requirements established by the Administrator of the Office of Federal Procurement Policy for senior contracting positions in the GS–1102 series pursuant to section 37(g)(1)(ii) of the Office of Federal Procurement Policy Act (41 U.S.C. 433(g)(1)(ii)).".

(e) CERTIFICATION EXAMINATIONS.—Section 1732(c)(2) of title 10, United States Code, is amended by striking "is serving" and all that follows through "if the employee".

(f) COURSEWORK TUITION.—Section 37(h)(2) of the Office of Federal Procurement Policy Act (41 U.S.C.

433(h)(2)) is amended by striking "in accordance with" and inserting "notwithstanding the provisions of".

(g) ACCELERATED PROMOTIONS.—Section 37 of the Office of Federal Procurement Policy Act (41 U.S.C. 433) is further amended by adding at the end the following new subsection:

"(i) RECRUITMENT AND PROMOTIONS.—

"(1) RECRUITMENT.—(A) For purposes of sections 3304, 5333, and 5753 of title 5, United States Code, the head of an agency (including the Secretary of Defense) may determine that certain Federal acquisition positions are 'shortage category' positions in order to recruit and directly hire employees with unusually high qualifications, such as employees who—

"(i) hold masters or equivalent degrees from accredited institutions of higher education in business administration, public administration, or systems engineering; or

"(ii) have had substantial, outstanding private sector experience with commercial acquisition practices, terms, and conditions.

"(B) Personnel actions under this paragraph shall be subject to policies prescribed by the Office of Personnel Management for direct recruitment, in-

cluding the appointment of a preference eligible as long as preference eligibles are available who satisfy the stipulated high level of qualifications.

"(2) ACCELERATED PROMOTIONS.—(A) The Director of the Office of Personnel Management shall authorize the rapid promotion of Federal acquisition personnel (including personnel in the Department of Defense) who satisfactorily complete programs of training and education required by the Federal Acquisition Regulation for positions at higher General Schedule grade levels in their respective fields and otherwise meet or exceed standards for satisfactory performance.

"(B) The heads of agencies may provide any such personnel with a maximum of 2 promotions during any 52-week period.

"(C) No employee may be promoted under this paragraph without adherence to competition requirements under law or regulation.".

SEC. 4. RESPONSIBILITIES FOR ACQUISITION WORKFORCE TRAINING.

(a) ADMINISTRATOR FOR FEDERAL PROCUREMENT POLICY.—Section 6(d) of the Office of Federal Procurement Policy Act (41 U.S.C. 405) is amended—

(1) by striking "and" at the end of paragraph (12);

(2) in paragraph (13), by striking the period and inserting "; and"; and

(3) by adding at the end the following new paragraph:

"(14) establishing requirements for acquisition professionals to obtain and maintain certification by a relevant professional association or other entities as authorized in the Federal Acquisition Regulation.".

(b) FEDERAL ACQUISITION REGULATORY COUNCIL.—Section 25(d) of the Office of Federal Procurement Policy Act (41 U.S.C. 421(d)) is amended—

(1) by striking "and" at the end of paragraph (2);

(2) in paragraph (3), by striking the period and inserting "; and"; and

(3) by adding at the end the following new paragraph:

"(2) review, approve, and promulgate in the Federal Acquisition Regulation certification requirements, core curricula, continuing education programs, and policy implementation training recommended by the Director of the Federal Acquisi-

tion Institute under section 6(d)(5)(F) and (J) to ensure that instructional materials provided for the Federal acquisition workforce accurately incorporate the provisions and intent of the Federal Acquisition Regulation and are effective in providing the skills and knowledge necessary to competently implement those provisions and otherwise enable the workforce to obtain the best value in awarding and administering Federal contracts.".

(c) FEDERAL ACQUISITION INSTITUTE.—Section 6(d) of the Office of Federal Procurement Policy Act (41 U.S.C. 405(d)) is amended—

(1) in paragraph (5)(B), by inserting ", and provide fellowships and grants for researching acquisition issues" before the period;

(2) by amending paragraph (5)(F) to read as follows:

"(F) develop and recommend core curricula, continuing education programs, policy implementation training, and other instructional materials for acquisition personnel in coordination with private and public sector acquisition colleges and training facilities (to the maximum extent practicable), and integrate those instructional materials with electronic performance

support systems for just-in-time delivery of initial and continuing education in critical duties and tasks).";

(3) by striking "and" at the end of subparagraph (I);

(4) by redesignating subparagraph (J) as subparagraph (K); and

(5) by inserting after subparagraph (I) the following new subparagraph:

"(J) enter into partnerships with private and public sector employers of acquisition personnel and with nonprofit professional associations in developing and maintaining valid and reliable professional certification programs for acquisition disciplines; and".

SEC. 5. FUNDING FOR ACQUISITION WORKFORCE TRAINING AND EDUCATION.

Section 37(h) of the Office of Federal Procurement Policy Act (41 U.S.C. 433) is amended—

(1) by amending paragraph (1) to read as follows:

"(1) FUNDING LEVELS.—(A)(i) The head of each executive agency shall be responsible for ensuring adequate funding is included in budget requests of the agency and for ensuring any funds provided

for the education and training of the acquisition workforce are expended for such purposes.

"(ii) In requesting funding as a part of the budget request of the agency, the agency head shall take into consideration the results of the assessment of the performance of the procurement system of the agency in terms of its efficiency and effectiveness in supporting the agency in accomplishing its mission, including the adequacy of the education and training of the acquisition workforce and whether the workforce has the necessary competencies, skills, and knowledge to effectively support the achievement of the mission of the agency.

"(B) The Administrator shall—

"(i) review the agency budget requests to assess the adequacy of funding levels for the education and training of the acquisition workforce and make recommendations to the agency head for adjustments of the funding levels, as appropriate;

"(ii) include sufficient funds in the budget recommended to the Administrator of General Services for the Federal Acquisition Institute in accordance with section 6(d)(5) for the development and maintenance of the instructional ma-

terials for the core curricula, policy implementation training, and for the development of technology-based learning tools and support systems that will benefit the acquisition workforce across the Federal Government;

"(iii) prepare a report for inclusion in the President's annual budget on the amounts requested by agencies in terms of adequacy for accomplishing the purposes of this section, and for maintaining an efficient and effective acquisition system (including information on recommended funding levels for the Federal Acquisition Institute);

"(iv) in preparing the report under clause (iii), and after consulting with the head of each affected executive agency, recommend any appropriate consolidation of funding for interagency acquisition training and education programs and provide information on actual outlays in prior fiscal years for acquisition training and education along with an evaluation of the effectiveness of those programs in providing the workforce with the necessary competencies, skills, and knowledge.

"(C) The President shall include the report in the annual budget submitted pursuant to section 1105 of title 31, United States Code."; and

(2) by adding at the end the following new paragraph:

"(3) PROFESSIONAL ORGANIZATIONS.—Notwithstanding section 4109(b) of title 5, United States Code, the head of an executive agency may pay membership fees and fees for certification testing for individual employees to organizations to further acquisition professionalism.".

SEC. 6. EVALUATION BY THE COMPTROLLER GENERAL.

The Comptroller General shall conduct an independent evaluation of the actions taken by executive agencies to carry out the requirements of section 37 of the Office of Federal Procurement Policy Act. On or before February 10, 2000, the Comptroller General shall submit to the Committee on Government Reform and Oversight of the House of Representatives and the Committee on Governmental Affairs of the Senate a report on the evaluation required by this section. Such report shall include—

(1) an analysis of the effectiveness of the actions taken by executive agencies to carry out such requirements; and

(2) any legislative and administrative recommendations that the Comptroller General consid-

ers appropriate to meet the objectives of that section.

SEC. 7. FUNDING.

(a) IN GENERAL.—(1) Funds described in subsection (b) may be transferred to an account of the Office of Management and Budget for use by the Administrator of the Office of Federal Procurement Policy for the purpose of administering Governmentwide acquisition workforce training activities and related purposes consistent with the objectives of the Office of Management and Budget.

(2) The specific amounts to be transferred under this section shall be determined jointly by the Director of the Office of Management and Budget and the head of the applicable department or agency.

(3) Funds transferred under this section shall remain available for obligation until expended.

(b) FUNDS AVAILABLE FOR TRANSFER.—Funds available for transfer under this section are funds appropriated for fiscal year 1993 or a subsequent fiscal year.

(c) LIMITATIONS.—(1) Funds may be transferred under this section not later than the end of the fifth fiscal year after the fiscal year for which funds are appropriated or otherwise made available.

(2) The aggregate amount to be transferred in any fiscal year under this section shall not exceed the lesser of—

(A) the amount that is 20 percent of the unobligated balance of funds appropriated for operating expenses and salary and other expenses available to each department and agency during the fiscal year for which the funds are appropriated; or

(B) $30,000,000.

(3) Funds transferred under this section shall only be made available if—

(A) the Director of the Office of Management and Budget notifies the Chairmen of the Committees on Appropriations of the House of Representatives and the Senate of the proposed transfer of such funds; and

(B) 30 days have elapsed following the date of such notification.

O

Mr. HORN. Current policy is governed by Office of Management and Budget Circular A–76, which says that agencies ought to rely on private sources for commercial activities, and on government sources for inherently governmental activities; that agencies should not start new commercial activities if they can get a contractor to perform the activities; and that agencies will subject their in-house commercial activities to competition.

Are agencies following this policy? Sadly, the answer is no. Outside the Department of Defense, not one single agency uses A–76 competitions. Some agencies say they do not have any activities that can be contracted out at all. These agencies with zero commercial activities include some agencies that brought work in-house and others that clearly have personnel performing commercial activities. Agencies must understand something—if you have an activity that was contracted out, that is a commercial activity by definition.

So how has the Office of Management and Budget responded to this sleight-of-hand? It has given a try to getting agencies on the bandwagon, but has fallen short. The results demonstrate that clearly. The Federal Government needs a clearly-stated policy in law that describes policy toward commercial activities. That's what Mr. Sessions' amendment attempts to do.

In the private sector, specialization and competition have reduced costs and improved performance and consumer choice. The most competitive sectors of the economy are also the most innovative. Federal antitrust policy is designed to ensure competition in the private sector so that the customers do not get gouged. We need an antitrust policy for the Federal Government to ensure that taxpayers do not get gouged.

My own view is that some agencies already have the most experienced and efficient people doing the job, but other agencies do not, especially as buyouts have removed some of the most capable performers. But we will never know who is a good performer without review and competition. Competition can be a spur to improve performance. According to the General Accounting Office, competition can reduce the costs of government by an average of 20 to 35 percent.

I know that there are vendors who have been harmed by government competition. I also know that there have been Federal employees harmed by contracting out. There have been spectacular failures by contractors, equally spectacular failures in government agencies in functions performed by Federal employees. But our primary purpose here today is to focus on good government demanded by taxpayers who sent us here, and who ultimately pay the bills.

In addition, while the purpose of this hearing is to review title II of H.R. 4244, Mr. DeSeve decided to expand the scope to get into other provisions. These additional topics include work force training, performance measurement, and cost accounting standards. While we appreciate your input, this hearing will focus on Mr. Sessions' proposal. As for the other issues, we would welcome additional points of view from groups, such as trade associations, for acquisition professionals and Blue Cross/Blue Shield.

I want to add that the staff has received several unsolicited statements for the record of this hearing. The subcommittee would

like to encourage additional thoughts on this issue, and we will hold open the testimony for 3 weeks for any person to provide a statement. We do not mean to close the door to any point of view, and we encourage healthy debate.

Without objection, the letter from Dan Burton, chairman, and John Mica, chairman, Subcommittee on Civil Service, will be included at this point in the record. And, without objection, the letter of Steven W. Gamarino, senior vice president, Federal Employee Program, Blue Cross/Blue Shield Association, will be included in the record at this point.

[The information referred to follows:]

Congress of the United States

House of Representatives

August 6, 1998

Stephen Horn
Chairman, Subcommittee on
Government Management, Information,
and Technology
B373 Rayburn
Washington, D.C. 20515

Dear Chairman Horn:

We would like to express our support for H.R. 4244, as reported out by the full Committee. In particular, section 302 is extremely important in that it secures temporary relief for Federal Employee Health Benefit (FEHB) contracts from application of the Cost Accounting Standards (CAS), accounting standards that are not only incompatible with health insurance carriers' accounting systems, but have little value to the carriers, the federal government, and the federal employees who rely on the FEHB program.

After failing to receive a delay in implementing the CAS from the Cost Accounting Standards Board (CASB), the Office of Personnel Management (OPM) directed FEHB experience-rated carriers in a January 15, 1998 letter to commence all necessary adjustments to their accounting procedures and practices in order to conform to the requirements of 48 CFR Part 30 and 48 CFR Chapter 99. Carriers were directed to adopt the CAS to "the maximum extent practicable" for contract year 1998. This was imposed even though OPM informed the committee in a letter dated June 30, 1998, that, as a general matter, they are satisfied with the cost accounting information provided by the FEHB carriers, and they have sufficient regulatory authority to ensure that audits are conducted appropriately.

On the other hand, Blue Cross and Blue Shield Association (BCBSA), the largest carrier in the FEHB program (covering 42 percent of all federal employees), has raised concerns with the difficulties of implementation of the CAS on FEHB program plan contracts. BCBSA has stressed that implementation would be extremely complex, time consuming, and economically unfeasible. More importantly, such an imposition would

force BCBSA to make an assessment as to whether continued participation in the FEHB program is possible as a prudent business matter.

We are concerned that continued application of the CAS would run a real risk of increasing costs to the FEHB program and may result in program disruption if the impracticability of applying the CAS forces the withdrawal of plans from the FEHB program. Moreover, it seems imprudent to require FEHB carriers to implement such burdensome and complex standards when the CASB Review Panel, a panel established by Congress to examine and analyze the CASB's mission and the application of CAS to government contractors, is expected to report its recommendations by the beginning of 1999. Our staffs have conferred extensively with BCBSA, OPM, OMB, and others regarding the appropriateness of applying these standards to the FEHB. These consultations have convinced us that the wisest course for Congress at this juncture is to enact a temporary moratorium and await the report of the CAS Review Panel. Once these experts have analyzed the complex issues involved in this controversy and issued their recommendations, Congress will be better equipped to resolve this matter permanently.

In the meantime, section 302 of H.R. 4244 is necessary to ensure that no disruption or any other unforeseen consequences occur in the FEHB program. In no way would this provision limit or restrict OPM's authorities with respect to audits, oversight or program administration. OPM will continue to have the regulatory flexibility to adapt certain principles of the CAS. More importantly, this provision would ensure the continued stability of the FEHB program and the continued health care coverage of our federal employees.

Thank you for your attention to this important matter.

Sincerely,

Dan Burton, Chairman
Committee on Government
Reform and Oversight

John L. Mica, Chairman
Subcommittee on
Civil Service

BlueCross BlueShield Association

An Association of Independent Blue Cross and Blue Shield Plans

Federal Employee Program
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August 28, 1998

The Honorable Stephen Horn
Chairman
Government Management, Information and
Technology Subcommittee
Government Reform and Oversight Committee
U.S. House of Representatives
Washington, D.C. 20510

Dear Mr. Chairman:

We appreciate your invitation to submit the views of the Blue Cross and Blue Shield Association on the subject of Cost Accounting Standards ("CAS") and their application to the Federal Employees Health Benefits ("FEHB") Program. In earlier correspondence to you (August 4, 1998) and to Chairman Burton (July 28, 1998) we have set forth in some detail the reasons why FEHB Program experience rated contracts should be exempt from CAS as commercial item acquisitions, the very real difficulties faced by insurance carriers in trying to implement CAS, and the fact that CAS would add little or no value to the FEHB Program. In this letter we provide our comments on the written testimony submitted by G. Edward DeSeve, OMB's Acting Deputy Director for Management, to your committee on August 6, 1998.

Mr. DeSeve informed the Committee that the Administration is opposed to those provisions of H.R. 4244 that "would preclude the application" of CAS to the FEHB Program. He states that the Administration would also oppose any language imposing a temporary moratorium on the application of CAS pending receipt and consideration of the report of the CAS Board Review Panel.

Mr. DeSeve's statement implies that CAS has applied to the FEHB Program since the 1980s, and that Blue Cross Blue Shield is only "recently" trying to prevent the application of "certain" CAS provisions to their contract. The fact is that, until the early 1980s, even the Federal Acquisition Regulation ("FAR") did not apply to the FEHB Program. The cost principles in Part 31 of the FAR incorporate the requirements of certain CAS standards governing the measurement of costs, such as CAS 412 and 413 (pension costs). Thus, once the FAR applied, the CAS requirements incorporated in FAR Part 31 also applied. These requirements for the measurement of costs are, for the most part, not difficult to comply with and are followed by most government contractors, large and small. Other than through FAR Part 31, however, CAS has **not** applied to the FEHB Program until OPM made it applicable "to the maximum extent practicable" in the 1998 contract.

For over a year, the Association and the Plans have worked to ascertain how best to comply with OPM's directive. The studies and analyses performed in this period have highlighted the incompatibility between CAS and the typical Blue Cross Blue Shield accounting system, which we summarized in our August 4 letter to you and which were described in more detail in an attachment to our July 28, 1998 letter to Chairman Burton. As we earlier stated, most of the incompatibilities arise from the allocation and consistency standards, not from the measurement standards. The allocation and consistency standards have not historically applied to the FEHB Program. This is an important distinction that Mr. DeSeve's statement does not address. In addition, full CAS coverage would bring with it the requirements of the CAS Board regulations and Disclosure Statement requirements, which have also not applied to the FEHB Program. Mr. DeSeve's statement does not address the fact that OPM is currently satisfied with the cost accounting information provided by FEHB Program carriers, the fact that OPM believes that CAS must be modified to fit the Program, or the fact that OPM believes that some requirements of CAS, most particularly the Disclosure Statement requirements, pose heavy administrative burdens for both the carriers and OPM without adding value to the Program.

Mr. DeSeve advocates that Congress defer to the administrative CAS waiver process. This position fails to take into account the fact that the Association and OPM are currently engaged in negotiations for the 1999 contract, which must be concluded in a relatively short period of time. The statement that "CAS waivers and exemption should only be granted upon a thorough investigation and evaluation of the factual and technical merits of a specific accounting situation by the CAS Board" demonstrates that reliance on the administrative process is not likely to resolve the problem at hand in a timely manner. OPM has in fact submitted a request for waiver to the CAS Board. However, both the carriers and OPM favor at least a temporary moratorium while the larger issues of CAS modification and/or specific waivers are considered in crafting a long term solution. Otherwise, OPM may be forced to include in the 1999 contracts requirements that they have no practical means of either implementing or enforcing, and carriers will have to consider whether they can even enter into contracts with such provisions. Mr. DeSeve's statement reflects the opposition of CAS Board staff to a moratorium. This opposition, we believe, simply demonstrates that a great deal of education of the CAS Board staff is necessary before an appropriate long term solution can be agreed upon. This, in our view, underscores the need for a moratorium.

We thank you for the opportunity to express our views.

Sincerely,

Rod Collins for

Stephen W. Gammarino
Senior Vice President
Federal Employee Program

cc: Mr. G. Edward DeSeve

Statement

Of the American Congress on Surveying and Mapping To the House Committee on Government Reform and Oversight Subcommittee on Government Management, Information, and Technology On H.R. 4244, the Federal Activities Inventory Reform Act

The American Congress on Surveying and Mapping (ACSM) is pleased to submit its views on H.R. 4244, the Federal Activities Inventory Reform (FAIR) Act. ACSM is an individual membership society that represents more than 7,500 professionals in the fields of surveying, cartography, geodesy, and geographic information systems technology who work in both the public and private sectors throughout the world. ACSM is made up of four member organizations that serve as special interest groups. ACSM's member organizations are the American Association for Geodetic Surveying, the Cartography and Geographic Information Society, the Geographic and Land Information Society, and the National Society of Professional Surveyors.

In commenting on H.R. 4244, ACSM seeks to represent the interests of its private- and public-based members, the surveying and mapping profession as a whole, and the nation's long-term interest in ensuring the availability of comprehensive, timely, accurate, and useful geospatial information.

General Comments

ACSM commends Chairman Horn, Representatives Sessions and Duncan, as well as Senator Thomas for finding a common ground that addresses the needs of the Executive Branch, without unnecessarily burdening federal agencies. The substitute amendment proposed by Congressman Sessions is a major improvement over the original language in H.R. 716.

ACSM Supports H.R. 4244

In March 1998, ACSM submitted a statement on proposals known as the Fair Competition Act of 1998 and the Competition in Commercial Activities Act of 1998. At that time, we noted that these bills were improvements over the original proposals, termed the Freedom from Government Competition Act (S. 314 and H.R. 716), that we had opposed. However, at that time, we stated that we could not endorse either the Fair Competition Act of 1998 or the Competition in Commercial Activities Act of 1998. At this time, after review of the legislation, we feel that H.R. 4244 is consistent with our ideals and we would like to express our support of the bill.

The substitute bill avoids many of the problems that we had with earlier versions,

including restrictions on Inter Service Support Agreements (ISSAs) under which agencies obtain goods or services from, or provide goods and services to, other government entities.

Inventory Will Provide Useful Information

We agree with the provisions of the bill that will provide for a way to thoroughly identify and categorize all activities currently performed by Federal agencies. It should move forward a process found in Circular A-76 of the Office of Management and Budget, and strengthen efforts to identify activities in federal agencies that are "non-governmental" in nature.

The Inventory, we believe, will be a useful project for many agencies, although several of the agencies in our industry, including the U.S. Geological Survey and the National Geodetic Survey, have made great strides in recent years in improving their efficiency and in contracting.

We also note that the FAIR Act includes provisions that require the process be consistent with existing law, such as those requiring Qualifications Based Selection, and that the definition of "inherently governmental" is similar to that already in an Office of Federal Procurement Policy Circular.

We are somewhat concerned that provisions of the Bill would require an administrative burden on many of the agencies that our members deal with. However, in view of the benefits of the bill, we believe the compiling of an inventory of activities is a worthwhile one.

NAPA Study Still Needs to be Considered

Many of our members are involved in compiling geographic information, and in using that data. In 1996 and 1997, we worked closely with the National Academy of Public Administration (NAPA) on a study of government use of geographic information. The study's sections on balancing public and private sector roles, the public purposes served by geographic information, and outsourcing may be helpful to the committee as you consider this or future government competition bills.

ACSM believes it can look at outsourcing objectively because its membership includes surveying and mapping professionals who work in private firms as well as government agencies. ACSM also can contribute to the debate from its experience over the past two years in generating the NAPA study. Unfortunately, at least one Federal agency, the U.S. Department of the Interior, has expressed opposition to the findings of the NAPA study, particularly in regard to creation of a National Spatial Data Council, with representatives from public and private sectors. We feel that this position is not in keeping with the spirit of private-public partnerships, or in the spirit of the FAIR bill.

There are many examples of efforts in Federal agencies that already involve a cross-section of federal, state, private-sector, and local interests to compile geographic information. These efforts need to move forward to guarantee that the base data that is used to compile maps, charts, geographic information systems, and other spatially-based tools, is of the highest accuracy possible. In one recent example, the National Geodetic Survey has completed a 50-state "High Accuracy Reference Network" that will ensure that future surveys and mapping projects in all states will have an accurate base. While the overall guidance and technical standards were set by the Federal government, many states, counties, private firms, and state surveying organizations were involved in the project. States and local governments across America found the resources to help complete the project, even during a period of downsizing and reduced budgets. Many surveyors, realizing the importance of "getting it right the first time," as well as documenting their work, supported the effort. The result is a combined network of federal and non-federal reference points that can be used to prepare accurate geographic products.

Accurate Geographic Information Affects All Americans

Since the development and use of accurate geographic information is something that affects all Americans, we believe that outsourcing of this work should meet strict quality requirements, and that the government must be able to hold the contractor accountable for performing acceptably. Cost effectiveness is one of several factors that needs to be considered; and arbitrary percentage targets for contracting out should be avoided.

The American Congress on Surveying and Mapping is a unique organization that includes many of the individuals and organizations involved in the debate over what is "inherently governmental." We welcome the opportunity to participate further with you in the discussion.

ACSM appreciates this opportunity to present its views on the proposed Federal Activities Inventory Reform Act (FAIR) and will be pleased to provide additional information on any point in our statement. Please contact Kevin Flynn, Acting ACSM Government Affairs Director, at 301-493-0200.

PROCUREMENT ROUND TABLE
4410 Massachusetts Ave, NW, Suite 404
Washington, DC 20016
Tel 301-261-9918
FAX 301-261-9918

August 7, 1998

Congressman Steve Horn
438 Cannon House Office Building
Washington, D.C. 20515-0538

Dear Steve:

The Procurement Round Table (PRT) is a non-profit 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, and I serve as Acting Chairman.

The PRT is of the view that priority should be given to training and educating the civilian agency acquisition workforce if procurement reforms encompassed in the Federal Acquisition Streamlining Act and the Federal Acquisition Reform Act are to be fully implemented. Our position paper on this subject is enclosed for ready reference (Enclosure). In continuing pursuit of our objective to assist in efforts to enhance the civilian agency acquisition workforce, the PRT hosted a seminar of procurement professionals from federal civilian agencies in November 1997. At the seminar, there was universal agreement on the need to improve the professionalism of people involved in the acquisition of goods and services in the federal civilian agencies. All agreed the first step in this process is to improve training and education provided to civilian agency acquisition professionals.

The PRT believes H.R. 4244, "Federal Procurement System Performance Measurement and Acquisition Workforce Training Act of 1998," addresses many of the deficiencies in current efforts to train and educate the civilian agency acqusition workforce. We endorse provisions in the bill aimed at professionalizing the civilian agency acquisition workforce and urge early passage of the bill.

Members of the PRT have worked closely with you and your staff over the course of the last year to secure legislation addressing acquisition training and education shortfalls. Therefore, we will be pleased to assist you and your staff in efforts to secure passage of H.R. 4244 in the House.

With kindest personal regards,

Frank

Frank Horton

FYH:sms
Enclosure

cc: Congressman Dan Burton
2185 Rayburn House Office Building
Washington, D.C. 20515

Mr. Dan Moll
2157 Rayburn House Office Building
Washington, D.C. 20515

Mr. Mark Brasher
B373 Rayburn House Office Building
Washington, D.C. 20515

PRT CALL TO ACTION: PROCUREMENT WORKFORCE PROFESSIONALISM

Both the Congress and the Administration are taking action to improve the Federal acquisition system. In 1994 the Congress enacted the Federal Acquisition Streamlining Act (FASA) which, among other things, establishes a preference for the purchase of commercial items, raises the dollar threshold permitting the use of simplified procurement procedures, and requires eventual implementation of an electronic procurement system.

FASA builds in part on the recommendations of the National Performance Review (1993) which contains recommendations for simplifying the procurement process by shifting from rigid rules in the Federal Acquisition Regulation to a set of guiding principles, delegating more procurement authority to agencies for information technology, and substantially decreasing the procurement workforce with particular emphasis on the reduction of middle management layers.

The Procurement Round Table (PRT) applauds these efforts. The PRT is a non-profit entity of forty former senior Federal acquisition officials who volunteer their non-partisan pro bono, efforts to improving the Federal process for acquiring goods and services.

With these significant changes taking place by law and administrative initiative, the PRT believes that action is needed now to improve the quality of the procurement workforce. Government and industry managers alike describe a pressing need for a more professional, highly trained acquisition corps. A wide range of studies have pointed to the criticality of a highly qualified workforce to obtain the goods and services the government needs.

The Congress responded to this need in the Department of Defense by passage of the Defense Acquisition Workforce Improvement Act (DAWIA) in 1990. The Act established minimum education and experience levels for contracting personnel; formed a Defense Acquisition University to conduct mandatory contracting training financed by means of fenced funding and created an acquisition corps of seasoned professionals for the most challenging positions in defense contracting. While implementation of DAWIA has been slow and not altogether perfect, the PRT believes it is a step in the right direction and provides a strong legislative foundation to improve contracting professionalism throughout defense agencies.

No legislative counterpart to DAWIA, however, exists for civilian agencies. PRT discussions with senior procurement executives in civilian agencies with significant contracting activity indicate that there is a need for increased professionalism, but that the issue is not getting the same level of top management attention as is the case in DoD.

Furthermore, the Office of Federal Procurement Policy (OFPP), charged by law with fostering government-wide management programs for a competent workforce, does not possess DAWIA-type authority to exercise effective leadership for professionalism initiatives in civilian agencies. Nor has the Federal Acquisition Institute (FAI), an element of OFPP housed within the General Services

Administration, reached its full potential for offering quality procurement training to civilian agencies. The PRT concludes that civilian agencies would benefit from a civilian acquisition workforce improvement statute modeled after DAWIA.

The PRT proposes the following:

1. That the President and the Congress take action now to implement the NPR recommendation to improve the government-wide procurement workforce, and provide civilian agencies with the authority to do this similar to that of DoD.

2. That the Congress conduct periodic reviews of DAWIA implementation, with emphasis on employee career progression, assignment duration in key procurement positions, and quality of training programs.

3. That legislative mandates similar to DAWIA be established for each civilian agency with significant contracting activity containing the following features:

a. Endorsement of the initiative by top agency officials, with staff leadership and support provided by a qualified agency procurement executive.

b. Standards and qualifications for entry into the professional procurement ranks, with emphasis on judgmental aptitudes as well as educational requirements. Procurement intern programs have been effective in the past and are strongly recommended.

c. Fenced funding for the delivery and evaluation of quality procurement/acquisition training programs focussed on building business management and judgmental skills rather than on rules and regulations, and emphasizing program manager-contracting officer cross-training and rotation.

4. A legislative mandate for strong leadership in the OFPP to promote procurement professionalism in all federal agencies, and the proper level of support for FAI to meet its responsibilities.

5. Re-institution of an interagency council to assist OFPP in gui the professionalism effort.

In conclusion, legislative and executive steps to streamline the procurement process are taking place coincident with the downsizing of the procurement workforce, reduction of middle management layers, and empowerment of employees to use judgment rather than regulation. PRT believes that if these streamlining initiatives are to be successful and if many of the procurement problems of the past are to be avoided, a high-quality procurement workforce is the sine qua non to that success. That objective calls for action now.

BlueCross BlueShield Association

An Association of Independent Blue Cross and Blue Shield Plans

Federal Employee Program
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August 4, 1998

The Honorable Steve Horn
Chairman
Government Management, Information
And Technology Subcommittee
Government Reform and Oversight Committee
U.S. House of Representatives
Washington, D.C. 20510

Dear Mr. Chairman:

On behalf of the Blue Cross and Blue Shield Association (BCBSA), I am writing to express our strong support for the provision in H.R. 4244, as reported by the full Committee on July 23, that would provide a moratorium on applying the Cost Accounting Standards (CAS) to contracts under the Federal Employees Health Benefits Program (FEHBP) pending receipt by the Congress of the report by the CAS Board Review Panel. The BCBSA and the participating Blue Cross and Blue Shield Plans have administered the Government-wide Service Benefit Plan under the FEHBP since its inception in 1960. The Service Benefit Plan is the largest plan in the FEHBP, providing health insurance benefits to millions of federal employees, retirees, and their families.

The typical Blue Cross and Blue Shield Plan accounting system is a process cost accounting system combined with an activity-based, multiple cost center approach. This approach is a well accepted, and, in fact, preferable approach for health insurance carriers. The CAS Board Standards were developed for manufacturers of defense products, most of whom use a job order cost center, with only a few large indirect cost pools. Accordingly, there is a significant and, at times, irreconcilable conflict between the requirements of individual standards and the typical Blue Cross and Blue Shield Plan accounting system.

The CAS Board promulgated three types of cost accounting standards: standards on consistency in cost accounting; standards on allocation of cost to cost objectives; and standards on measurement of individual cost elements. Many of the measurement standards are incorporated in the Federal Acquisition Regulations cost principles and have been applicable to the FEHBP for some time. The provision in H.R. 4244 would not, in any way, alter the applicability of these principles to FEHBP contracts.

The consistency standards and the cost allocation standards are conceptually sound but their specific requirements are not compatible with the multiple cost center accounting approach used by Blue Cross and Blue Shield Plans. Further, the FEHBP business is integrated with the local Blue Cross and Blue Shield Plans' commercial business and the government contract, on average, accounts for only about 5 percent of the typical Plan's business. Thus, to implement the specific requirements of the CAS would require significant restructuring of the Plans' current accounting systems. Such a restructuring would require abandoning the multiple cost center process cost system approach that now provides Plan management with cost information for managing their commercial business and pricing their products. A change of this magnitude would require a significant monetary investment that would be costly to Plans and to the Government and at the end of the day, would provide no significant benefit to the FEHBP.

It is worth noting that the Office of Personnel Management (OPM), the agency that administers the FEHBP, has stated publicly that it is generally satisfied with the cost accounting information provided by FEHBP carriers, and believes it has sufficient regulatory authority to ensure that audits are conducted appropriately. OPM also has acknowledged that the CAS pose implementation problems and may require modification to fit insurance products. BCBSA agrees with OPM's views. Further, BCBSA wishes to assure the Congress that, in our view, the provision in H.R. 4244 would, in no way, weaken or undermine OPM's authority with respect to FEHBP oversight, administration, or audit.

Enactment of H.R. 4244 would eliminate a current ambiguity in the FEHBP with respect to 1998 and would enable the carriers and OPM to conclude negotiations for 1999 while avoiding unnecessary disruption and instability in the program.

Thank you for the opportunity to express our views.

Sincerely,

Stephen W. Gammarino

Stephen W. Gammarino
Senior Vice President
Federal Employee Program

SWG/jw

Mr. HORN. With that, I'm going to recess at 2:30, and when Mr. Sessions comes, he can begin with the witnesses. I will try to be back by 10 minutes of 3, and we'll just be in recess until that time.

[The prepared statement of Hon. Stephen Horn follows:]

"Legislative Hearing on
Title II of H.R. 4244, the Federal Activities Inventory Reform Act

August 6, 1998

OPENING STATEMENT
REPRESENTATIVE STEPHEN HORN (R-CA)

Chairman, Subcommittee on Government Management,
Information, and Technology

Our hearing today will examine Title II of HR 4244, the Federal Activities Inventory Reform Act. This title represents an amendment by Representative Pete Sessions. This topic has been the subject of previous hearings in this subcommittee in September of 1997 and March of 1998. Hopefully, our witnesses will be able to shed additional light on a much-debated topic.

Current policy is governed by Office of Management and Budget Circular A-76, which says (1) that agencies ought to rely on private sources for commercial activities, and on government sources for inherently governmental activities; (2) that agencies should not start new commercial activities if they can get a contractor to perform the activity; and (3) that agencies will subject their in-house commercial activities to competition.

Are agencies following this policy? Sadly, the answer is "No." Outside the Department of Defense, not one single agency uses A-76 competitions. Some agencies say that they do not have any activities that can be contracted out at all. These agencies with zero commercial activities include some agencies that brought work in house and others that clearly have personnel performing commercial activities. Agencies must understand something: if you have an activity that was contracted out, that is a commercial activity, by definition.

So how has the Office of Management and Budget responded to this sleight-of-hand? It has given a try to get agencies on the bandwagon. But it has fallen short. The results

demonstrate that clearly. The Federal Government needs a clearly stated policy, in law, that describes policy towards commercial activities. That is what Mr. Sessions' amendment attempts to do.

In the private sector, specialization and competition have reduced costs and improved performance and consumer choice. The most competitive sectors of the economy are also the most innovative. Federal antitrust policy is designed to ensure competition in the private sector, so that the customers do not get gouged. We need an antitrust policy for the Federal Government, to ensure that taxpayers do not get gouged.

My own view is that some agencies already have the most experienced and efficient people doing the job. But other agencies do NOT, especially as buyouts have removed some of the most capable performers. But we will never know who is a good performer without a review and competition. Competition can be a spur to improve performance. According to the General Accounting Office, competition can reduce the costs of government by an average of 20 to 35 percent.

I know that there are vendors who have been harmed by government competition. I also know that there have been Federal employees harmed by contracting out. There have been spectacular failures by contractors, and equally spectacular failures in government agencies in functions performed by Federal employees. But our primary purpose here today is to focus on good government demanded by the taxpayers who sent us here, and who ultimately pay the bills.

In addition, while the purpose of this hearing is to review title II of HR 4244, Mr. DeSeve decided to expand the scope to get into other provisions. These additional topics include workforce training, performance measurement and cost accounting standards. While we appreciate your input, this hearing will focus on Mr. Sessions' proposal. As for the other issues, we would welcome additional points of view from groups such as trade associations for acquisition professionals and Blue Cross/Blue Shield.

I want to add that the staff has received several unsolicited statements for the record of this hearing. The Subcommittee would like to encourage additional thoughts on this issue, and we will hold open the testimony for three weeks for any person to provide a statement. We do not mean to close the door to any point of view, and we encourage healthy debate.

[Recess.]

Mr. SESSIONS. I call the subcommittee to order and would ask that our witness, as he is rising, please raise his right hand.

[Witness sworn.]

Mr. SESSIONS. The record will please reflect that our witness has answered in the affirmative.

Mr. DeSeve, I am delighted to have you here today. I will forego any opening statement that I have, but will insert that in the record. Without objection, so ordered.

[The prepared statement of Hon. Pete Sessions follows:]

CONGRESSMAN
PETE SESSIONS
News

TEXAS FIFTH DISTRICT

1318 Longworth House Office Building • 202-225-2231 • Contact: Pam Arruda

STATEMENT OF THE HONORABLE PETE SESSIONS
BEFORE THE COMMITTEE ON GOVERNMENT REFORM AND OVERSIGHT
REGARDING HOUSE RESOLUTION 4244

August 6, 1998

Thank you, Mr. Chairman.

I appreciate your decision to take the opportunity to discuss this very important bill on procurement training for the Office of Federal Procurement Policy. The amendment I offered on July 23, 1998 was supported by both sides of the aisle, since identical language was passed on voice vote by the Senate Governmental Affairs Committee, and later by the entire Senate.

The business community, including the U.S. Chamber of Commerce, has publicly endorsed this language. Notably, the Executive Branch and the federal government unions have also publicly indicated their neutrality on this language. As a result of all of these groups coming together for a compromise, this language is **NOT** H.R. 716, the Freedom From Government Competition Act, which I have cosponsored with Representative Duncan, and have discussed with you in hearings and meetings throughout this year. Instead, this language only requires an inventory of commercial activities by the federal agencies and also a consideration for whether the agency should continue performing the activity in-house or compete it out to the private sector. I realize that there will be some on both sides of the aisle who believe that this language does not go far enough in one direction or the other, but it is a true compromise. This is important legislation that I believe will truly result in a government that works better and costs less.

Certainly, government agency officials should have the ability to contract with the private sector for goods and services needed for the conduct of government activities. This language will not inhibit that ability. However, it should not be the practice of the government to carry on commercial activities for months, years, even decades, without reviewing whether such activities can be carried out in a more cost effective or efficient manner by the private sector.

During the course of our hearings, it became abundantly clear that there are certain activities that the Federal government has performed in-house which can and should be converted to the private sector. Areas such as architecture and engineering, surveying and mapping, laboratory testing, information technology, and laundry services have no place in government. These activities should be promptly transitioned to the private sector.

Additionally, this language fixes some of the problems identified in the hearings with OMB Circular A-76. Among the problems we have seen with Circular A-76 are:

(1) agencies do not develop accurate inventories of activities;
(2) they do not conduct the reviews outlined in the Circular;
(3) when reviews are conducted they drag out over extended periods of time; and
(4) the criteria for the reviews are not fair and equitable.

These are complaints we heard from the private sector, government employees, and in some cases, from both.

There are several key provisions in the language of my amendment upon which I would like to comment today. In particular, section 2(d) requires the head of an agency to review the activities on his or her list of commercial activities "within a reasonable time." OMB strongly opposed a legislative timetable for conducting these reviews. As a result of the compromise language on this matter, it will be incumbent on OMB to make certain these reviews are indeed conducted in a reasonable time. These reviews should be scheduled and completed within months, not years. I will personally monitor progress on this matter, as will the Senate Committee on Governmental Affairs. I urge OMB to exercise strong oversight, as well, to assure timely implementation of this requirement by the agencies.

This provision also requires that agencies use a "competitive process" to select the source of goods or services. In my view, this term has the same meaning as the "competitive procedure" defined in Federal law (10 USC 2302(2) and 41 USC 259(b)). To the extent that a government agency competes for work under this section of the bill, the government agency will be treated as any other contractor or offeror in order to assure that the competition is conducted on a level playing field.

Essentially, I believe that this Congress is about right-sizing the federal government and getting the best value for the taxpayer. This language is a step in that direction and I am committed to work through this committee to use this bill as a vehicle to do further oversight on the problems of government competition until we have a satisfactory solution.

Mr. Chairman, thank you for allowing me to speak on this important matter. I yield back the balance of my time.

Mr. SESSIONS. Mr. DeSeve, welcome to this subcommittee, and I will ask you to please go ahead and lead off as our first witness.

STATEMENT OF G. EDWARD DeSEVE, ACTING DEPUTY DIRECTOR FOR MANAGEMENT, OFFICE OF MANAGEMENT AND BUDGET

Mr. DESEVE. Thank you, Mr. Chairman. This is the fourth time I've had the opportunity in the House of Representatives to testify on this issue. I'm going to limit my remarks today only to title II of the bill. My entire testimony covers the entire bill because I believe it's in a position to move to the floor and we wanted you to have the benefit of the administration's position to have a full setup on the bill within the next couple of days.

Mr. SESSIONS. Good. Thank you.

Mr. DESEVE. So we just wanted to let you know that.

I'd like to discuss the provisions of title II of H.R. 4244 entitled, the Federal Activities Inventory Reform Act of 1998, or the FAIR Act.

As you know, the government's acquisition of commercial support services has been the topic of extensive discussions involving the House and the Senate, the administration, private sectors, and unions who represent Federal employees. The administration has urged the Congress to ensure that any legislative initiative in this area contributes to the process of extending opportunities for public-private competitions.

As part of these discussions, we've developed—actually, before this committee—a set of fundamental principles for the development of legislation in this area. First, the legislation needs to promote competition to achieve the best deal for the taxpayer, not simply to outsource.

Second, the legislation needs to establish the principle that it would not increase the level of traditional involvement in the government's management decisions as to whether or not to outsource, or how that comparison is conducted.

Third, the legislation must recognize that current, and extensive, OMB Circular A–76 guidance to promote a level playing field is already in place. Any changes to the management document, employee participation, costing and source rules for the competitions must be well understood, as well as to be enforceable and remain impartial.

Fourth, the legislation must recognize the complexities of public-public and public-private competition.

Fifth, the legislation must be fair and equitable to all parties. One-way competition is unacceptable.

Sixth, the legislation must view public-public and public-private competition in the context of our larger reinvention efforts. Outsourcing is only one management tool to reinvent and improve the government.

And finally, it would be inappropriate, and, in fact, maybe detrimental, if the legislation were to require the head of each agency to undertake competitions according to its schedule mandated in law. The FAIR Act provisions do not violate these principles. In fact, they encompass and respect these principles.

In our view, the FAIR Act provisions serve to reinforce ongoing efforts to improve the identification and review support activities that are commercial or subject to contract. Agencies are already reviewing which support activities are inherently governmental and cannot be contracted out at any time; commercial and subject to contract, but specifically exempt commercial, and those which should be competed on the basis of quality and cost.

And finally, those which are commercial, but must be retained in-house for now, for reasons that need to be fully explained by the agency.

In essence, the FAIR Act preserves our ability to increase opportunity for public-private competitions and permits us to achieve the quality improvements and cost reductions we all seek in the acquisition of commercial support services. Accordingly, the administration would not object to the passage of the FAIR Act.

Mr. Chairman, this concludes my remarks here today. I'd be pleased to answer any questions that you, or other members of the subcommittee, may have.

[The prepared statement of Mr. DeSeve follows:]

STATEMENT OF
G. EDWARD DESEVE
ACTING DEPUTY DIRECTOR FOR MANAGEMENT
OFFICE OF MANAGEMENT AND BUDGET

BEFORE THE U.S. HOUSE OF REPRESENTATIVES
COMMITTEE ON GOVERNMENT REFORM AND OVERSIGHT
SUBCOMMITTEE ON GOVERNMENT MANAGEMENT, INFORMATION AND TECHNOLOGY

AUGUST 6, 1998

Mr. Chairman and Members of the Subcommittee:

I am before you today to discuss H.R. 4244. I would like to address three matters in particular: (1) performance measurement and acquisition workforce training; (2) the Government's acquisition of commercial support services; and (3) the proposed moratorium on the application of the CAS to FEHBP contracts.

Performance Measurement and Acquisition Workforce Training

Let me begin by addressing the provisions on performance measurement and acquisition workforce training. While the Administration shares the Committee's goal of ensuring the quality and professionalism of the Government's acquisition workforce and measuring the performance of procurement operations, the Administration opposes those sections of H.R. 4244 that would establish a new statutory basis for measuring progress in procurement performance and would require reporting by agencies that allocate greater than 50 percent of their budget to procurement programs. Section 6 of the Office of Federal Procurement Policy (OFPP) Act already assigns the development of government wide procurement system standards to OFPP.

Working with OFPP, the President's Management Council commissioned the Procurement Executives' Working Group to develop agency procurement system performance measures. A menu of 54 measures was established. Agencies selected measures from the list based on their individual missions, organizational structures, types of procurement, and availability of data collection systems. OMB has made increased use of performance based service contracting a priority management objective requiring regular progress reports from the 20 agencies that award the most service contracts. OMB also is committed to working with the agencies to determine whether other core performance measures should be required. In addition, certain agencies submit specific performance measurement information as part of their annual performance plans under the Government Performance and Results Act (GPRA).

Thus, we believe that the performance measurement sections of proposed H.R. 4244 would duplicate existing requirements for the establishment of government wide procurement system standards already contained in both the OFPP Act and GPRA, and would impose potentially burdensome and duplicative reporting requirements.

The Administration also opposes those sections of H.R. 4244 which address the Government's acquisition workforce. The Administration shares the goal of ensuring the quality and professionalism of the Government's acquisition workforce. Rather than reflecting an emphasis on the goals of flexibility and streamlining of personnel policies, these sections would instead impose rigid and inflexible personnel, training, and associated budgetary policies upon agencies. This would detract, rather than enhance, their ability to manage and train their

acquisition workforce. These sections would also drain limited training funds from the various agencies in order to enhance the budget of the Federal Acquisition Institute (FAI), a small subdivision of the General Services Administration. Proposals to increase funding for FAI should instead be addressed through the regular budget process. The bill would also assign to OFPP, an operational role in the funding and direction of FAI. This is not an appropriate role for an office whose primary mission is to develop and oversee broad procurement policies. The Administration believes that the issues raised in the acquisition workforce sections of H.R. 4244 are better handled by administrative action tailored to each agency's specific needs, rather than through inflexible statutory requirements.

In addition to these basic concerns about the acquisition workforce provisions of H.R. 4244, the Administration also notes that neither FAI nor the Federal Acquisition Regulatory Council has the expertise to determine functional training requirements for members of the Government's acquisition workforce beyond contracting personnel. H.R. 4244 would also upset many of the Administration's recent initiatives designed to improve the education and training of the Government's contracting workforce, including activities sponsored by the Department of Defense, the Office of Personnel Management (OPM) and OFPP.

The Federal Activities Inventory Reform Act

I would now like to discuss the provisions of Title II of H.R. 4244, entitled the "Federal Activities Inventory Reform Act of 1998" or the "FAIR Act." As you know, the Government's acquisition of commercial support services has been the topic of extensive discussions involving

the House and the Senate, the Administration, the private sector and the unions who represent Federal employees. The Administration has urged the Congress to ensure that any legislative initiative in this area contributes to the process of expanding opportunities for public-private competitions.

As a part of these discussion, we developed a set of fundamental principles for the development of legislation in this area. First, the legislation needs to promote competition to achieve the best deal for the taxpayer - not simply to outsource. Second, the legislation needs to establish the principle that it would not increase the level of judicial involvement in the Government's management decisions as to whether or not to outsource or how that comparison is conducted. Third, the legislation must recognize that current and extensive OMB Circular A-76 guidance to promote a level playing field is already in place. Any changes to the management documentation, employee participation, costing and source selection rules for the competitions must be well understood so as to be enforceable and remain impartial. Fourth, the legislation must recognize the complexities of public-public and public-private competitions. Fifth, the legislation must be fair and equitable to all interested parties. One-way competition is unacceptable. Sixth, the legislation must view public-public and public-private competition in the context of our larger reinvention effort. Outsourcing is only one management tool to reinvent and improve Government performance. We must not treat competition as a variable independent from our other reinvention and management improvement efforts. And finally, it would be inappropriate and may, in fact, be detrimental, if the legislation were to require the head of each agency to undertake competitions in accordance with a schedule mandated in law. Such

schedules are likely to be extremely administratively burdensome and may preclude a mix of reinvention, re-engineering, consolidation, privatization, and cost comparison efforts.

The FAIR Act provisions do not violate these principles. In our view, the FAIR Act provisions serve to reinforce ongoing efforts to improve the identification and review of support activities that are commercial or subject to contract. Agencies are already reviewing which support activities are: (1) inherently governmental and cannot be contracted out any time, any place or for any reason; (2) commercial and subject to contract, but are specifically exempt from the cost comparison requirements of the Circular A-76 for reasons of, for example, the national defense, patient care, or other specified reasons; (3) commercial and which should be competed with public and private sector offerors on the basis of quality and cost; and (4) commercial, but must be retained in-house – for now -- for reasons that need to be explained by the agency, including the involvement of that function in a larger re-engineering, reinvention, consolidation or privatization review.

In essence, the FAIR Act preserves our ability to increase opportunities for public-private competitions and permits us to achieve the quality improvements and cost reductions we all seek in the acquisition of commercial support activities. Accordingly, the Administration would not object to passage of the FAIR Act provisions.

Proposed Moratorium on the Application of CAS to FEHBP contracts.

Turning to the third issue, the Administration opposes those provisions of H.R. 4244 that

would preclude the application of Cost Accounting Standards (CAS) to experience rated contracts awarded under the Federal Employees Health Benefits Program (FEHBP). Various provisions of CAS have applied to FEHBP contracts since the 1980s. Recently, the Blue Cross and Blue Shield Association has sought to stem application of certain CAS provisions to their FEHBP contracts. CAS, and its underlying cost accounting principles, are applied to all contractors (including FEHBP contractors) that perform under negotiated, cost-based pricing arrangements with the Federal Government in order to ensure that costs are properly allocated to the Federal Government, and, in the case of the FEHBP, to the Federal employees and annuitants who pay more than one-quarter of the premium costs.

Congress has already provided in statute for a formal waiver process that appropriately considers circumstances that are so unique as to make the application of CAS inappropriate. For this reason, the Administration would also oppose any language imposing a temporary moratorium on application of CAS to FEHBP carriers pending future action to be taken by the CAS Board Review Panel. CAS waivers and exemptions should only be granted upon a thorough investigation and evaluation of the factual and technical merits of a specific accounting situation by the CAS Board. The proposed statutory CAS exemption for FEHBP contractors does not meet this important criterion.

Mr Chairman, this concludes my remarks. I will be pleased to answer any questions that you or the other Subcommittee Members may have.

Mr. SESSIONS. Thank you, Mr. DeSeve. I find, with great interest, that your evaluation talks very clearly about quantity and the cost improvement that can be achieved. What kind of discussions have taken place, at least within OMB, about how your work with agencies can improve these or offer some lead when this becomes law and signed by the President? Because I heard you said that the administration is supportive of this. What ideas and thoughts do you have about how this will improve quality and cost?

Mr. DESEVE. What we found is that when activities were exposed to competition, whether they were won by union offers or whether they were won by private sector offers, everyone sharpened their pencil and they learned how to do things more efficiently and more effectively. The GAO studies that exist on this show cost-savings in the 20 and 30 percent range, just from the conducting of competition along the way.

We are currently working with agencies under the OMB memo that Frank Raines put out this spring to make sure, even in anticipation of the legislation's passage, that the inventories are being updated in the agencies. We've had several meetings with them; I've been in meetings with them. I've talked to the chief operating officers of the agency and told them the seriousness which both Congress and the administration view this—the increased seriousness, if you will.

So I look forward in October to seeing those submissions come in, whether or not they are required to by law, and then to review those submissions with the agencies very directly as part of the overall budget review process in the fall to see that they are (1) looking carefully at the opportunities to conduct competitions; (2) that they haven't walled-off inherently-governmental functions; but, most of all, if they've bothered to comply at all.

As you and the chairman have indicated before, some agencies the last time out in the inventory process simply didn't submit any inventories that were responsive. So we want to make sure that doesn't happen in anticipation of whatever happens with this bill.

Mr. SESSIONS. So you believe that you will be able to be a catalyst and a leader in working each of the agencies? You believe that it is a very good thing for them to have within their arsenal of opportunities to work with, and that it will be seen as a favorable and positive step?

Mr. DESEVE. Yes, sir, I think so. And I think one of the nice things we have now is the lead of the Defense Department. They've shown us that by planning to expose more than 200,000 FTEs to competition, that it can be beneficial and it can give them the cost-savings they need to be able to spend more money more wisely on other things.

Mr. SESSIONS. One of the things that very clearly came up as a result of the discussion about this legislation was the need for labor and management to be able to work together on a bill that seems to indicate a direction that we would go, and that is the opportunity to have this available. But one thing that was very clear to me is that, what I would call, union representatives, were very interested in having part of a discussion, to being a part of the dialog, to understand the direction we were going. I am pleased to report, I believe—and you are aware of this—that this was an agree-

ment, if I could call it that, that we would pursue this avenue of legislation.

Do you believe that you will continue within the administration to listen to those concerns on the implementation of this, and that we provide you an element to do that?

Mr. SESSIONS. Very much so. I give you my commitment of the prior hearing. I know you question me very closely about our willingness to take on the leadership here.

I give Senator Thomas my commitment on the Senate side, as well as Senator Levin and others, that we would be activist in managing this process and we would find a way to get to a legislative solution that, if parties couldn't embrace, at least they would not object to. We found ourselves able to do that.

I believe you'll hear testimony later today from many of the commercial groups and associations. I believe the union has indicated that they have no objection at this time. So we've gotten to that legislative compromise that we think is appropriate, and we are fully committed to implementing that compromise.

Mr. SESSIONS. Good, good. I don't see any of my colleagues from the minority are here. Do any of my colleagues wish to engage in a discussion with Mr. DeSeve? No. No discussion.

Mr. DeSeve, I want to thank you for being a part of what we are doing today.

Mr. HORN. I would like to congratulate the gentleman on being confirmed as Deputy Director of OMB for Management. And now, maybe if we can pass our Office of Management bill, you'll be Director of Management. [Laughter.]

Mr. DESEVE. Thank you, Mr. Chairman. I must, however, for the accuracy of the record indicate, although my confirmation was slated on Friday, it did not occur. I suspect pressing business kept it from coming up. I believe there's a full agreement that it will go forward. We actually had a schematic on at one point at OMB, not during my tenure, to show an extension to the West Wing in the old Executive Office Building, which would house the new Department of Management. [Laughter.]

Mr. SESSIONS. We're getting there.

Mr. DESEVE. I look forward to it, Mr. Chairman.

Mr. SESSIONS. I want to add, or pile on, to the comments made by my chairman, Mr. Horn, and say that we are very impressed, not only with your forthrightness, but we're very, very proud of the work that you're doing on behalf of not only the President of the United States, but all the American people, and the spirit which you have presented yourself here today with an opportunity to keep this ball rolling and make it prove this opportunity, and we appreciate you taking time.

I will now excuse the witness, since there are no further questions.

Mr. DESEVE. Thank you very much, Mr. Chairman.

[Additional questions for the record follow:]

EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET
WASHINGTON, D.C. 20503

DEPUTY DIRECTOR
FOR MANAGEMENT

DEC - 7 1998

The Honorable Stephen Horn
Chairman, Subcommittee on Government
Management, Information and Technology
United States House of Representatives
Washington, D.C. 20515-6143

Dear Chairman Horn:

Thank you for your joint letter with Representative Kucinich, dated September 25, 1998, forwarding several follow-up questions to our hearing on H.R. 4244, "the Federal Procurement System Performance Measurement and Acquisition Workforce Training Act of 1998."

Based upon discussions with your staff, attached are responses to question numbers 8 through 17.

Again, thank you for you letter. Please let me know if we can be of further assistance.

Sincerely,

G. Edward DeSeve

G. Edward DeSeve
Deputy Director for Management

IDENTICAL LETTER SENT TO REPRESENTATIVE DENNIS KUCINICH

Questions for the Record for Ed DeSeve, Acting Deputy for Management, Office of Management and Budget

Legislative Hearing on Title II of H.R. 4244, the "Federal Activities Inventory Reform Act"

August , 1998

1. Very little is currently known about the pay, health care benefits, or retirement benefits of federal contractor employees. In a recent effort to provide some information on this issue, the General Accounting Office (GAO) contacted OMB, DoD, and OPM officials knowledgeable about the contractor workforce, but they could not offer much assistance (GAO/GGD/NSIAD-98-167R). However, in 1995 GAO did find that "53% of federal employees whose jobs were contracted out said that they received lower wages, and most reported that contractor benefits were not as good as their government benefits." (GAO/T-GGD-95-131)

   Why doesn't the federal government collect this information? What data can you provide on the contractor workforce? Do we even know how large that workforce is? Please provide your best estimate of the size of that workforce. Savings from contracting out often come through lower way and benefit levels. To what extent is this the case in federal contracting? Is a comprehensive survey of contractor wages and benefits possible? If so, will OMB commit to performing such a study?

2. The Federal Activities Inventory Reform Act codifies the requirement in OMB Circular A-76 that agencies inventory activities performed by federal employees which are not inherently governmental. This Administration has also stated that contractor-performed work can be contracted-in if federal employees can do the work more cost-effectively.

   Please list the instances of contracting-in that have occurred in the last five years and the value of those contracts. GAO has concluded that "personnel reductions that have occurred throughout the government could make it difficult to bring work back in-house." (GAO/GGD/NSIAD-98-167R) Do you anticipate that contracting-in will increase or decrease in the next few years? The inventories of federally performed non-inherently governmental activities may encourage agencies to consider contracting-out. Would an inventory of work performed by contractors be useful to agencies in considering whether to contract-in work?

3. Much contracting out in the federal sector takes place without any cost comparisons, either through OMB Circular A-76 or other informal means. According to GAO, OMB is "not able to provide data on the percentage of commercial activities contracting funds (1) completed under A-76, (2) competed under an informal competitive framework, and (3) not competed at all." (GAO/GGD/NSIAD-98-167R) This is clearly an unfortunate situation. Please provide answers to the following to the best extent possible.

What percentage of the $120 billion in services spent annually on government contractors was subjected to the OMB Circular A-76 process? How much work is contracted out annually without any cost comparison? Is it the Administration's position that work currently performed by contractors should not be subjected to public-private cost comparisons?

4. According to the GAO, "post-contract reviews of activities outsourced by military services have been limited; as a result, (GAO has) questioned whether they provide a basis for projecting with reliability the magnitude of savings achieved over time." (GAO/GGD/NSIAD-98-167R) In addition an internal DoD study has stated that "most of the contractor workforce has never been competed under the A-76 process; and when it has been, there is no on-going scrutiny..."

   What sort of follow-up does OMB conduct to ensure that contractors actually live up to the terms of their contracts? Is there need for legislation or regulation to address the savings problem -- to ensure that whatever savings are alleged by initial contracting out decisions will actually be generated?

House Subcommittee on Government Management, Information and Technology
Questions for
Mr. G. Edward DeSeve,
Deputy Director for Management,
Office of Management and Budget (OMB)
regarding

H.R. 4244, "The Federal Procurement System Performance Measurement and Acquisition Workforce Training Act of 1998."

FEDERAL ACTIVITIES INVENTORY REFORM

8. ***What percentage of the $120 billion in services annually spent on Government contractors is subject to the OMB Circular A-76 cost comparison process? Why don't you keep this information.***

As I testified earlier this year, the Fiscal Year 1997 expenditures for service contracts were about $112 billion. For Fiscal Year 1998, total expenditures for service contracts are now estimated at $108 billion. General downsizing, procurement reform, enhanced technology investment and changes within the DOD for its support services, such as Base Operating Support (BOS) contracts and the use of Direct Delivery contracts, combined with a very low inflation rate have served to keep these expenditures from growing.

All currently awarded service contracts (100 percent) are potentially subject to the OMB Circular A-76 cost comparison process. These contracts may be submitted to competition for the conversion of work from contract to in-house performance at the discretion of the agency and/or local commander or may be recompeted normally every three to five years.

9. **How much work is contracted out without any cost comparison?**

Work that is currently performed in-house by Federal employees can only be converted to contract performance, in accordance with the provisions of OMB Circular A-76. This includes the possibility of a conversion without a cost comparison if the function being performed by Federal employees meets certain conditions. As a general rule, A-76 does not require cost comparisons to convert work to or from in-house or contract performance if the primary reason for the conversion relates to the acquisition of needed or specialized skills. Exemptions from the cost comparison requirements of the Circular are provided in the Circular to meet, for example, the requirements of the national defense, direct patient care, research and development and core mission requirements. Work can also be converted to or from in-house or contract performance without a cost comparison if it involves ten or fewer FTE. Since 1979, the 10 or fewer FTE rule

has permitted conversions to contract performance without a cost comparison. The March 1996 Revision expanded that provision to permit the conversion of work from contract to in-house performance. It is felt that cost comparisons requirements at this limited level are burdensome and that the savings that could be generated by a public-private competition are unlikely to be offset by the delays and other costs of conducting the cost comparison. Work may also be converted to contract performance without a cost comparison if it is awarded to a procurement preference eligible contractor, such as those in the Small Business Administration's 8 (a) program or a workshop for the blind or severely handicapped. In yet other situations, waivers from the cost comparison requirements of the Circular may also be granted at the Assistant Secretary level.

The amount of work that has been converted from in-house to contract or from contract to in-house performance without a cost comparison and over the past 20 years is not known. Only two waivers are known to have been issued from the cost comparison requirements of the Circular A-76; the most significant of which was the decision to convert the Federal Aviation Administration's Level 1 Towers to contract performance. This was done on the basis of experience which indicated that savings in excess of 50 percent were being achieved by converting this work to contract performance.

10. How can we know that outsourcing work saves the taxpayer's money unless it has been determined the in-house performance is less cost effective?

We agree that cost comparisons should be conducted to justify the conversion of competitive work. As noted above, however, the conversion of work from in-house to contract performance is not always a function of the competitive costs to the taxpayer. In many cases, conversions may be justified on the need to access special skills (doctors, nurses, research scientists, DOD defense systems technicians, etc.), technology or to meet other requirements. For that recurring commercial work that is competitive and for which cost is a deciding factor, the OMB Circular A-76 requires that a minimum level of taxpayer savings be identified before work can be converted to or from in-house or contract performance. This minimum differential or savings is established at 10 percent of the in-house labor costs not to exceed $10 million. Outsourcing is not always the right answer and this is why we have insisted on the conduct of cost comparisons when appropriate.

11. Does OMB conduct post-contract reviews of outsourced activities to assess whether cost savings are achieved over time?

OMB does not conduct post-contract reviews of outsourced activities. The agencies are expected to conduct such reviews as a normal part of their procurement and contract administration process, with full recompetitions generally every three to five years.

The Government is doing business with better-performing contractors that are committed to excellence and to meeting cost, schedule, and performance goals. This achievement is the result of a concerted effort by contracting activities to increase their focus on the past performance of contractors when conducting competitions for work. There is also greater

attention being paid to the evaluation of contractor performance. Because completed evaluations (along with contractor responses thereto and any additional agency review comments) are used to support future award decisions, contractors are motivated to excel in their performance.

In addition, we are making greater use of contracting methods that will help improve the likelihood of successful contract performance. For example, we are using performance-based service contracts that include objective performance requirements and standards (which give contractors latitude to be innovative and adopt the latest, most cost effective management practices). These contracts are accompanied by a quality assurance plan that allows for the use of both positive and negative incentives. The contractor's payment is tied to the achievement of requirements and standards. Poor contractor performance may result in an immediate reduction in payment and would also be reflected in contractor past performance evaluations which could impact the contractor's future business opportunities.

If, however, contract performance is unsatisfactory within the time frame for full recompetition, the agency may terminate the contract and, if specified conditions exist, convert directly back to in-house performance. It is our view that any additional action beyond this would necessarily have to be applied to the in-house decision, including scheduled recompetes.

12. What are some of the problems the Government has experienced with outsourcing?

Certainly there are anecdotal stories that can be given to highlight problems with individual cost comparisons, contracts, contractors or with a particular transition from in-house to contract performance. Similar anecdotes can be gathered regarding in-house performance, incentives and costs. In our review of the literature and through reports by the General Accounting Office (GAO) or, for example, the Center for Naval Analysis (CNA) we find few trends that warrant fundamental policy changes.

As noted in question 11, above, the government is pursuing a variety of initiatives to motivate our contractors to excel in their performance, including the use of financial incentives through use of performance based service contracting. A recently completed Government-wide pilot project conducted by the Office of Federal Procurement Policy and endorsed by the President's Management Council demonstrated an average 15% nominal price reduction and 18% increase in satisfaction with contractor performance. These findings validated 20 years of anecdotally reported positive agency experiences with this contracting practice, showing how it can greatly contribute toward extending programs that rely on service contracts in a time of tight budgets.

13. When activities are outsourced, what happens to the Government jobs? What about workers with government pensions -- can they carry them over to the private sector? What about health benefits?

When activities are outsourced, those jobs that are not inherently governmental, such as those that are created to meet contract administration requirements, are converted to contract performance. Historically, the number of available jobs has decreased as a result of an A-76

cost comparison - whether or not the function is retained in-house or converted to contract performance. The in-house Most Efficient Organization (MEO), for example, has historically reduced the number of available jobs by - on average - 20 percent. While the number of Government jobs may be further reduced by a conversion to contract performance, the requirement is not terminated or otherwise eliminated. Jobs are created in the private sector to perform the work.

The employees themselves may be placed in other Federal jobs through, for example, the DOD placement program or other priority lists or they or may be placed in the contractor's workforce through the A-76 Right-of-First-Refusal-clause. Involuntary Reductions-in-Force into a non-employed status have been rare.

Federal employees cannot directly carry their current Federal pensions with them into the private sector. Of course, this is a more serious concern for those employees in the Civil Service Retirement System (CSRS) than it is for those in the Federal Employment Retirement System (FERS) which is much more portable, including its social security and 401(K) type Thrift Savings Plan provisions. FERS as a defined contribution plan is much more akin to the private sector pensions requirements as compared to the defined benefit plan of the CSRS. Federal employees with 5-years of service under CSRS are vested in this plan and are eligible for pension benefits at age 62. Health care benefits do not transfer directly, but are managed through the Service Contract Act, which requires that both wages and fringe benefits reflect those prevailing for that industry in that area - not minimum wages and benefits.

14. Could you comment on the review provisions for challenges to agencies' inventories under H.R. 4244, as amended; will these provisions impact agencies governmental activities?

The Administration did not object to the provisions of P.L. 105-270, the "Federal Activities Inventory Reform Act of 1998 (FAIR)." We believe the Act reinforces efforts to identify non-inherently governmental activities, permits agencies to assess which functions should be submitted to competition with the private sector and allows the Government to choose the source - public or private - which is the most cost effective and in the best interests of the taxpayer. As such, it places greater attention on the need to identify those functions that could be competed with the private sector.

The FAIR Act requires the head of each executive agency to submit to the Director of the Office of Management and Budget a list of commercial activities performed by Federal employees. The Director shall review the agency's list for a fiscal year and consult with the head of the executive agency regarding its content. Upon the completion of the review, the head of the executive agency shall transmit a copy of the list to Congress and make the list available to the public. An interested party, including the employees, the private sector and their representatives may submit to the agency a challenge of an omission or the inclusion of a particular activity on the list. This challenge is limited to an administrative review within the agency. Then, within a reasonable time after the final decision to include or exclude an activity on the list is made, the head of the executive agency concerned shall review the activities on the list for possible

competition with the private sector. Each time the agency considers contracting with a private sector source for the performance of an activity, the agency shall use a realistic and fair competitive process to select the most cost effective source (except as may otherwise be provided in a law other than this Act, an Executive order, regulations, or any Executive Branch circular setting forth requirements or guidance that is issued by competent executive authority).

15. **Can you provide a reasonable estimate of the numbers of contractor employees that currently work for the Federal Government. S. 314 and OMB Circular A-76 require agencies to report on the inventory the number of federal workers performing non-inherently governmental activities. Why is this information useful? Why don't we require Federal contractors to report the same information?**

There is currently no system of reports that will identify or aggregate contract employees by contract type, location or contract number. Agencies need to know the scope of contracted workload, that contract prices are reasonable, that the work is of appropriate quality, and the dollars being spent. It is not, however, useful or important that an agency know the specific number of employees hired by a contractor on a full-time or part-time basis to meet the performance requirements of the contract. Collecting this kind of information would be arduous and costly to both the agencies and to the contractors themselves. It would be time sensitive and subject to significant distortions over time, by contract, by contract type, by location, by function, individually or in aggregation. To collect this information, OMB would be obligated, in accordance with the Federal Paperwork Reduction Act, to demonstrate the practical utility of the information requested and that the administrative burden associated with its collection was outweighed by the benefit of having access to the information on a recurring basis. We do not believe that this information is particularly useful on a recurring basis. It would have little or no impact on the conduct of individual A-76 cost comparisons and would contribute little to understanding the growth or decline in overall Federal employment levels.

The OMB Circular A-76/FAIR Act inventory provides detailed in-house employment (FTE) information by location and industry function code for functions currently performed in-house, including savings (whether retained or converted to contract) and the function's current status. The Federal Procurement Data System (FPDS) is the primary source for information on contracted activities and provides, among other data, contract dollar information by agency, contract number, location and business type. Although the FPDS does not provide any contractor FTE data, the information that it contains, which is available to the public, could be used to develop reasonable estimates of the number of Federal contract employees, based upon a range of economic and performance assumptions and using reported contract dollar values.

16. **The Government has little information on contractor workforces. Moreover, very little is known about the pay, health care benefits, and retirement benefits for contractor employees. Why doesn't the Government collect this information? If the data indicates that pay and benefits for the contractor workforce are well below that of Federal employees, would the Administration support legislation that would address this issue?**

The Government collects an enormous amount of information on contract salaries and benefits, through the Department of Labor. In Federal contracting, each contract is given specific wage and fringe benefit requirements as a part of the contract that reflect the prevailing wages and benefits for that industry and location, under the Service Contract Act and/or the Davis Bacon Act.

17. Does the Administration support "contracting-in" when it is cheaper and more efficient to do so? Please list the instances when contracting-in has occurred and the value of those contracts. Do you anticipate that contracting-in will increase or decrease? Why doesn't the Federal Government compile inventories of work currently performed by contractors so that agencies can also be encouraged to consider "contracting-in?"

The Administration fully supports "contracting-in" when it is cheaper and more efficient. A number of important revisions were made to the March 1996 A-76 Revised Supplemental Handbook to facilitate this opportunity, including changes to permit the conversion of work from contract to in-house performance without a cost comparison when it involves 10 or fewer FTE and changes to the A-76 costing rules when applied to new starts and expansions.

Such conversions have taken place - though not in the numbers one would expect. This is partly due to the fact that the opportunities to accomplish such conversions were limited prior to March of 1996 and partly because agencies have opted not to conduct such studies since 1996, as they faced general downsizing pressures.

As a general matter, we expect more studies to be conducted to convert work from contract to in-house performance. OMB no longer manages by FTE controls, which should never be viewed as a barrier to either retain functions in-house or to convert them from contract to in-house performance. The perception that once a function is contracted the agency cannot reconstruct the function in-house needs to be overcome. We also believe that functions will be converted to in-house performance as a result of increased public-private competition, where the March 1996 Revision specifically permits public offerors to bid for recompeted contract work and for other Interservice Support Agreement (ISSA) work between agencies. Finally, it is our sense that as we move away from the lower graded commercial work (custodial, grounds and even mechanical maintenance work) and move into the more technical IT, communications, finance, inspections and other program oversight work, Federal salaries will be more and more competitive with those of the private sector.

Mr. SESSIONS. OK, we're going to call up panel two: Mr. John Palatiello—and he is entitled to say his name correctly since I butchered it—Mr. Gary Engebretson, and Dr. Elliott Sclar. Why did we get all these names? I'm a Texan. You shouldn't expect me to do this. [Laughter.]

And Mr. Max Sawicky.

So if I can have each of you rise please, and I'm going to administer your oath. If you'll please rise and raise your right hands.

[Witnesses sworn.]

Mr. SESSIONS. Thank you. If you'll please be seated. Let that reflect that all four of the witnesses have answered in the affirmative.

For the record, I'm going to ask, when you give your opening statements, if you'll please do me a favor and correct my pronunciation of your name and please accept my apology. Part of the problems that I have are that I'm from Texas, and the other half is I didn't practice before I got in here today.

So what we will do, please, is start with Mr. Palatiello. Sir, we are delighted to have you here to testify about the Federal Activities Inventory Reform Act, H.R. 4244, title II. You're the executive director, Management Association for Private Photo—anyway, you like to take pictures and you're a surveyor—[laughter]—and chairman of the Business Coalition for Fair Competition. I might suggest that Mr. Horn, next time, recheck before he has his vice chairman, and at least have me practice.

Sir, please go ahead.

STATEMENTS OF JOHN PALATIELLO, EXECUTIVE DIRECTOR, MANAGEMENT ASSOCIATION FOR PRIVATE PHOTOGRAMMETRIC SURVEYORS, AND CHAIRMAN, BUSINESS COALITION FOR FAIR COMPETITION; GARY ENGEBRETSON, PRESIDENT, CONTRACT SERVICES ASSOCIATION; ELLIOTT SCLAR, PROFESSOR OF URBAN PLANNING, GRADUATE SCHOOL OF ARCHITECTURE, PLANNING AND PRESERVATION, COLUMBIA UNIVERSITY; AND MAX SAWICKY, ECONOMIST, ECONOMIC POLICY INSTITUTE

Mr. PALATIELLO. Thank you, Mr. Chairman. I am John Palatiello, executive director of the Management Association for Private Photogrammetric Surveyors. You have it right; those are folks that do make maps from aerial photographs and from surveying data.

We are pleased to appear today to indicate our very strong support for the Federal Activities Inventory Reform Act, and we commend you, Mr. Sessions and Mr. Horn, all the members of the subcommittee, for their hard work in bringing about this compromise.

This legislation is a true compromise between the interests of the private sector, the Federal employee unions, OMB, and the bipartisan leadership of the committees of jurisdiction of both the House and Senate. We commend you for the time and effort that you have put into to developing this consensus.

The FAIR Act, for the first time in more than 40 years, will codify a governmentwide policy and process on the issue of government reliance on the private sector. We believe that in itself is significant and commendable.

As was stated by Mr. Duncan, and mentioned in previous hearings, it was in 1932 that the House first created a special committee to investigate the issue of the Federal Government's starting and carrying out of activities that are commercial in nature and competitive with the private enterprise system. In 1954, a bill to address this issue was reported by this committee, passed the House, and was reported by your counterpart committee in the Senate. At that point, the Eisenhower administration indicated that they could resolve this matter administratively. Bureau of the Budget Bulletin 55–4 was issued and further action on the legislation was suspended.

That policy is now found in OMB Circular A–76. It is our view, and has been reflected in recommendations of the White House Conference on Small Business, that that administrative policy has not worked well.

Today, Federal Government agency officials certainly have the ability to contract, and they do that with great regularity. This bill would not, in our view, interfere with that very important management tool. It is our view, however, that Federal agencies should not be able to carry on commercial activities for an indefinite period of time and never have to review or consider whether using the private sector for those activities is a better deal for the taxpayer.

I must say that our members do not believe that the government should be competing with or duplicating private sector capabilities. I know in our organization we've gone through a long and very deliberative process on this legislation, and our members really do not like the idea of the Federal Government taxing a business, collecting money, and starting a business to duplicate what that taxpaying entity was doing in the first place. However, we do support this legislation and we think it is a major step in the right direction.

As you know, Mr. Chairman, the legislation would ask for an annual inventory. It does set up a very fair challenge process that is administrative and not judicial. It requires agencies to use a competitive process for those activities on the list within a reasonable time. It requires fair and realistic comparisons when there are public-private competitions conducted. And it requires that procurement processes be consistent with existing law, such as the Brooks Act, which applies to our services. Finally, it establishes in statute a definition of what is an inherently governmental function.

Mr. Chairman, as was mentioned by Mr. Horn at the beginning, OMB Circular A–76 does not work. When you have an activity, like surveying and mapping, with a capable and qualified private sector, when you have a government that spends over $1 billion a year on these activities and employs nearly 7,000 Federal employees to do this work, and contracts out less than 10 percent of that $1 billion annually, and that no agency has ever done a start-to-finish A–76 review of any of their surveying or mapping activities, I think what you have, is what Senator Brownback appropriately termed in his hearing, "a systems failure." This legislation will correct that.

I'd make one final point with regard to the profession that I represent. We recently obtained information from the Immigration and Naturalization Service that showed that, between 1985 and 1995,

an average of 10,000 engineers, surveyors, and mapping scientists have emigrated into the United States each year during that time period. This shows clearly that there is a job market for people in the private sector in our field. One of the benefits that we see from this legislation is tremendous employment opportunities for those Federal employees who wish to transition themselves to private sector employment, and our member firms welcome that.

Again, we commend all those involved with this compromise. This is a good bill. We look forward to working with the Congress on oversight and with OMB on implementation of this important legislation.

Thank you for the opportunity.

[The prepared statement of Mr. Palatiello follows:]

Management Association
for Private
Photogrammetric Surveyors

Statement of John M. Palatiello
Before the Subcommittee on Government Management,
Information and Technology
House Committee on Government Reform and Oversight

Federal Activities Inventory Reform Act

August 6, 1998

Mr. Chairman, members of the Subcommittee, I am John Palatiello, Executive Director of the Management Association for Private Photogrammetric Surveyors, (MAPPS) a national trade association of more than 120 private mapping firms, and Chairman of the Business Coalition for Fair Competition (BCFC), a coalition of trade associations in a variety of industries all of whom are affected by various forms of government-sponsored competition.

I am pleased to appear today to indicate our strong support for the Federal Activities Inventory Reform Act (FAIR), a adopted by the Senate in S. 314 and as approved by the full House Government Reform and Oversight Committee as the amendment by Representative Sessions to H.R. 4244.

This legislation is a true compromise between the interests of the private sector, the Federal employee unions, OMB and the bi-partisan leadership of the committees of jurisdiction in the House and Senate.

Although this bill is significantly different than S.314 and H.R. 716 as introduced, is indeed different from several draft alternatives discussed over the past several months and is not everything the private sector would like to see, we do support this compromise. We commend the Committee and the staff for the time and effort they have dedicated to developing a consensus on this legislation.

The FAIR Act for the first time in more than 40 years codifies a government-wide policy and process on the issue of government reliance on the private sector. That is significant and commendable.

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As you know, Senator Thomas and Representative Duncan introduced S.314/H.R. 716, the Freedom from Government Competition Act. The intent of that legislation was to establish in statute a workable process by which Federal agencies utilize the private sector for commercially available products and services. As your hearings and those convened by Senator Brownback demonstrated, in 1932 the House created a special committee to study the Federal government's starting and carrying out activities that are commercial in nature and competitive with the private sector. In 1954, a bill to address this issue was reported by this Committee, passed the House and was reported by the Committee on Governmental Affairs of the Senate. At that time, the Eisenhower Administration indicated that it could resolve this matter administratively. Bureau of the Budget Bulletin 55-4 was issued and the Senate suspended action on the legislation. That budget document established a federal policy of reliance on the private sector and said the government should not compete with private business

That policy is now found in OMB Circular A-76. It has been endorsed by every Administration, of both parties, since 1955. However, because that policy is in a non-binding circular, implementation has been uneven from one Administration to another. In recent years, the problem has been so critical that all three meetings of the White House Conference on Small Business, in 1980, 1986 and 1995, ranked government competition as one of the top problems facing America's small businesses.

Certainly government agency officials have the ability to contract with the private sector for goods and services needed to carry out governmental activities. Agencies do that and this bill will not interfere with that important management tool. It is our view, however, that the Federal government should not start and carry out commercial activities for an indefinite period of time without even considering whether using the private sector is a better deal for the taxpayer.

I must say that our members do not believe the government should be competing or duplicating private sector capabilities. However, we support this compromise legislation which will require the following:

*agencies must annually inventory their activities that are not inherently governmental.

*interested parties can challenge either the inclusion or exclusion of an activity on the list. The challenge is administrative (not through a judicial review).

*agencies must use a "competitive process" on those activities on the list within a reasonable time

* establishment of realistic and fair comparison for determining whether to use a private source or government source.

* requires that the process be consistent with existing law (such as the Brooks Act's qualifications based selection process for architecture and engineering services, including surveying and mapping, as required in 40 USC 541 et. seq.)

*establishes a definition of "inherently governmental" similar to that already in an Office of Federal Procurement Policy letter.

*covers all Federal agencies, except the General Accounting Office, Government corporations, non appropriated instrumentalities and depots.

*effective date is October 1, 1998

Mr. Chairman, your hearings have demonstrated that OMB Circular A-76 does not work. When you have a clearly commercial activity, like surveying and mapping, with a capable and qualified

private sector, and the government spends $1 billion each year on these activities, and employs nearly 7,000 Federal workers in this activity, and contracts out less than 10% of that $1 billion, and no agency has performed a start-to-finish A-76 review on a surveying or mapping function, you have what Senator Brownback called a "systems failure".

This legislation will replace OMB Circular A-76 with a more workable and fair process. It will help assure proper implementation of Executive Order 12615, the Economy Act (31 U.S.C. 1535), with regard to services for other agencies and the Intergovernmental Cooperation Act (31 U.S.C. 6505(a)) with regard to services for State or local government by assuring that the rights of the private sector under those provisions are indeed honored.

Mr. Chairman, we recently obtained information from the Immigration and Naturalization Service showing that between 1985 and 1995, an average of 10,000 engineers, surveyors and mapping scientists have emigrated to the United States annually. That shows clearly that when contracting out is applied to our field, there will be jobs in the private sector for any Federal employee who wants to make that move or is requested to make that move.

We commend all those involved in working out this compromise. We believe this is a good bill and we look forward to working with the Congress on oversight and with OMB on implementation on this important legislation.

Mr. SESSIONS. Thank you.

Our next witness will be Mr. Gary Engebretson, president of Contract Services Association. Sir.

Mr. ENGEBRETSON. Mr. Chairman, members of the committee, my name is Gary Engebretson and I am president of the Contract Services Association of America, CSA. It's the Nation's oldest and largest association of government service contractors. I'm also speaking on behalf of the Coalition for Taxpayer Value, of which CSA is a member. Collectively, the coalition represents thousands of employers and hundreds of thousands of government contract employees.

I thank you for the opportunity to testify today on the Federal Activities Inventory Reform Act of 1998, which was added as an amendment to the acquisition work force training bill, H.R. 4244.

While the legislation represents numerous compromises that were made of necessity, I applaud and encourage you to continue your efforts to pass this legislation, which embodies a number of key concepts. We support this compromise measure, which we believe should move forward without any changes. I want to add, however, that ensuring its full and proper implementation will take vigorous congressional oversight.

The language before you represents important progress and opportunities on many fronts. First, the legislation clearly delineates between activities identified as inherently governmental versus non-inherently governmental, and reiterates a longstanding policy of the Federal Government to rely on the capabilities of the private sector. While this policy, embodied in the Office of Management and Budget Circular A–76, which is more than 40 years old—there are still activities which are not inherently governmental that the government itself continues to perform—this bill will help the Federal Government focus on its core missions and responsibilities rather than competing with its own citizens. It will further the current efforts to streamlining the Federal Government.

This spring, Mr. Frank Raines, before leaving the Office of Management and Budget, issued a memo requesting all Federal agencies to develop a list of activities they perform. This bill will turn OMB's request into a mandate, ensuring a process that will thoroughly identify, categorize, and evaluate all the activities currently being performed by the government.

While there is concern that an agency may simply ignore the competition policy in the bill, I would argue that the agencies cannot afford not to compete their commercial activities. Thus, the legislation will help create an environment that promotes great efficiency and cost-savings.

In closing, let me just say that 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 the scarce resources are used most efficiently.

So I commend you, Mr. Chairman. I commend Senator Thomas and Congressman Duncan; of course, chairman, Congressman

Horn, and all the others, the respective staffs, for working so hard, and that has gone into crafting this legislation, and I offer our continued support.

This concludes my remarks and I stand by and ready to answer any questions that you may have.

[The prepared statement of Mr. Engebretson follows:]

STATEMENT OF
Gary D. Engebretson, President
Contract Services Association of America

BEFORE
The House Government Reform and Oversight Committee

HEARING ON:
The Federal Agency Inventory Reform Act of 1998

Mr. Chairman, members of the committee. My name is Gary Engebretson and I am the President of the Contract Services Association of America (CSA), the nation's oldest and largest association of government service contractors. Now in its 34th year, CSA represents more than 250 companies that provide a wide array of services to the federal government, as well as numerous state and local governments. I am also speaking on behalf of the Coalition for Taxpayer Value of which CSA is a leading member. The coalition membership includes the American Council for Independent Laboratories, the American Consulting Engineers Council, Chamber of Commerce, MAPPS and the Professional Services Council. Collectively, the coalition represents thousands of employers and tens of thousands of government contract employees. I thank you for the opportunity to testify today on Federal Agency Inventory Reform Act of 1998, which was added as an amendment to an acquisition workforce training bill, H.R. 4244.

First, let me stress that we have 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. However, we recognize the broad based support for public-private competition on the part of the Government. Given that reality, we support this legislation as a rational, appropriate and measured step towards achieving the proper balance between public and private resources.

While the legislation represents numerous compromises that were made, of necessity, I applaud and encourage you to continue your efforts to pass this legislation, which embodies a number of key concepts. We support this compromise measure, which we believe should move forward without any changes. I want to add, however, that ensuring its full and proper implementation will take vigorous Congressional oversight.

The language before you represents important progress and opportunities on many fronts:

First, the legislation clearly delineates between activities identified as inherently governmental

versus non-inherently governmental and reiterates a long standing policy of the Federal government to rely on the capabilities of the private sector. While this policy, embodied in the Office of Management and Budget Circular A-76, is more than forty years old, there are still activities which are not inherently governmental that the Government itself continues to perform. The purpose of this legislation is to identify and evaluate those activities which remain in house. In doing so, the bill will help the Federal government focus on its core missions and responsibilities and in the long run, allow the Federal agencies to focus on their core missions rather than competing with its own citizens. This measure will further the current efforts to streamline the Federal government.

This spring, Mr. Franklin Raines, before leaving the Office of Management and Budget, issued a memo requesting all federal agencies to develop a list of the activities they perform. However, like the A-76 policy itself, this request is not mandatory and such efforts in the past have not met with much cooperation from federal agencies. As Christopher Mihm of the General Accounting Office testified in a hearing before the Senate Government Affairs Committee (June 4, 1998), OMB had made a similar request in 1996 but did not receive any agency inventories or else those received were based on previous inventory efforts.

This bill will turn OMB's request into a mandate, ensuring a process that will throughly identify and categorize all activities currently being performed by the government. In other words, it will require the Federal government to do what business and taxpaying families do everyday: to take stock in how they can best direct their scarce resources. Activities determined to be commercial in nature should and must be subjected to competitive sourcing. The legislation also includes a reasonable timetable for phasing in the competitive process. This is designed to ensure that no significant disruptions to the Government's ability to carry out its missions occurs and forces a legitimate discipline in carrying out the intent of this legislation. While there is concern that an agency may simply ignore the competition policy in the bill, I would argue that the agencies cannot afford NOT to compete their commercial activities. Thus, the legislation will help create an environment that promotes greater efficiency and costs savings.

At this time, I would like to take a moment to dispute some of the inaccurate assertions that have repeatedly been made about our industry and these bills. 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[1]. 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 Contact Act can result in fines and debarment. CSA has a successful program with the Department of Labor to promote understanding of and compliance with the Service Contract Act.

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

Study after study, from sources as diverse as the GAO, OMB and innumerable think tanks, have

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1 *See* The Service Contract Act, 41 U.S.C. § 351: "Every contract entered into by the United States . . . through the use of service employees must contain the following; (1) A provision to specify the minimum monetary wages to be paid to the various classes of service employees in the performance of the contract . . . (2) A provision specifying the fringe benefits to be furnished. . . "

shown that competitively outsourcing the government's commercial activities saves money. The taxpayer an average 30% regardless of who wins the competition[2] 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.[3] 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 [4].

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.

And then there is the term "Shadow Government."

Is sounds provocative, but in fact 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 which 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. As we have already discussed, many of the employees on Government contracts are the same people who did the work before. The term shadow government is nothing more than a shadow argument.

In closing, let me reiterate that the legislation being considered will create an environment that promotes efficiency and encourages cost savings by identifying where and how the Federal government is directing its resources. 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.

I commend you, Mr. Chairman, as well as Senator Thomas, and Representatives Duncan, Sessions,

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2 *See* Testimony of Steve Klienman before the Senate Governmental Affair Committee, Subcommittee on oversight of Government Management and the District of Columbia (June 18, 1997) References cited: by Alan J. *CNA Research Memorandum 92-226.10. Analysis of the Navy's Commercial Activities Program (1993)*

3 Ibid

4 Outsourcing DoD Logistics: GAO Report: December 8, 1997

Horn and their staffs for all of the hard work that has gone into crafting this legislation and I offer our continued support. This concludes my remarks and I stand ready to answer any questions you may have.

Mr. SESSIONS. Thank you.

Our next witness is Dr. Elliot Sclar, professor of urban planning, Graduate School of Architecture, Planning and Preservation, Columbia University. Dr. Sclar.

Mr. SCLAR. Thank you, Mr. Sessions. Chairman Horn, and members of the subcommittee, I appreciate the kind invitation you've extended to me to testify on title II of H.R. 4244, the Federal Activities Inventory Reform Act of 1998.

My name is Elliott Sclar. I am professor of urban planning at the Graduate School of Architecture, Planning and Preservation, Columbia University in the city of New York. I'm an economist. I study the economics of privatization. In the American context, the term "privatization" is somewhat misleading. It tends to refer to efforts to increase reliance on contracting in the performance of public service. It's, therefore, more accurate to think of the subject matter of domestic privatization as effectively the economics of public contracting. The crucial issue, then, pertains to the dynamics of interorganizational behavior between a public agency and a private contractor. This relationship is often complex and can at times be problematic. Title II will vastly expand the scope of public contracting in the ongoing operations of Federal agencies. Therefore, the implications for the cost-effectiveness of Federal public service are potentially vast.

The main point I would make is that when you look at organizational behavior, and sources of organizational efficiency, you'll find that contracting, or what is known in the business world as the make-buy, is just one way of improving the situation. More importantly, if it's the main strategy, or the only one you use, you quickly learn that your problems have gotten worse and not better.

At the present time, there's a great deal of fascination with the notion of contracting out as an analogous way of bringing market pressures into government. But, if we look back at our rich experience with public contracting, we find that while it clearly has its place in the box of management tools, it has never proven to be a silver bullet for anything. More to the point, it has often been the source of some of our worst public scandals, as well as more day-to-day types of petty inefficiency.

Title II seeks to avoid these problems by mandating that Federal agencies "use a competitive process to select the source" from whom they will obtain services. The presumption here is that competition among private providers will ensure that the government receives the best product at the lowest price consistent with efficient production cost, and that competitors will help to keep one another on the straight and narrow.

That theory resides quite far apart from the actual practice of public contracting. As a matter of general observation, it's impor tant to note that approximately one-half of all public spending is now done via contracting. Too large a percentage of that contracting is carried out in situations in which there's only one bidder, or at most two or three, who scarcely meet the economic test of the competitive market.

A recent study by the State auditor in California found that a full two-thirds of all public contracts are let on a sole-source basis.

While the situation in Federal contracting may be better, I suspect that the order of magnitude is similar.

Scarcely a week passes in which somewhere in America a controversy erupts around the letting of public contracts. This happens for a complex set of reasons, not the least of which is that while we all love competition when we are buyers, we hate it when we're sellers. Sellers spend more time in the marketplace than do buyers, and hence, they devote a great deal of energy to undermining competition with its thin profit margins.

When we look at public contracting, it is noteworthy for the speed with which competition consistently evaporates on the supply side of the market. Situations in which the first round of bids on a new service produce many bidders are usually followed by rounds in which the agency and the chosen contractor merely moves to a stylized performer, and then back to doing whatever they got used to doing after several years together.

To say that government must learn to contract smarter is simply not helpful. It essentially puts the weight of blame for a situation in which the strongest incentives to undermine competition are "built-in" on the supply side on to the buyer. The committee must appreciate the difficulty of sustaining competition for public contracts. Firms engage in mergers and acquisitions, as well as other legal practices to eliminate and dominate competitors. This is especially true among firms engaged in public contracting. Absent meaningful competition, the rationale for extending contracting becomes weak to nonexistent.

It's also important to remember that privatization via contracting relies heavily on the belief that most contracts can be made almost self-enforcing. Yet the necessity for written contract arises precisely because each party to a transaction fears that the other party, or parties, may fail to deliver or perform. Thus, contracts contain descriptions of the future behavioral obligations of both parties, to the extent that such behavior can be anticipated, and the sanctions to be imposed if either party fails to hold up its end of the bargain. Such future-oriented obligations, created in an atmosphere of uncertainty, place the public agencies and its contractors in a far different relationship to each other than the cut-and-dried contracts typical of discrete purchases, such as a fresh coat of paint in the hearing room. The extent of this divergence between markets for clearly defined and limited products and ongoing services is critical in determining the comparative efficiency of the privatization option.

We do well to remember that a good portion of the lucrative practice of corporate law involves nothing more than litigation among parties claiming breach of contract or seeking resolution of differing interpretations of contract language. If contracting is that difficult and expensive in the private sector where the parties at least are clear about the bottom line they are pursuing, why would one suppose it is going to be easier in the public sector, where the output is not as easily valued by market criteria?

Public contracting is not an end in itself. To be an effective element in improved agency operation, it must be integrated into a comprehensive effort of agency reform. The problem with this title as it now stands is that it fails to address the other elements,

which must also be in place if increased contracting is to make a contribution to improvement. By itself, it would run the risk of making matters much worse.

Such far-reaching change will not occur by legislative fiat. It will require cooperation between the executive branch and the legislative branch, along with the active involvement of the managers and employees who actually carry out the important day-to-day work of the Federal Government. Congress can plan an important role in bringing players together to launch this change process.

I would just add—in going through the legislation and going through the A–76; I hadn't looked at it for a few years—the problem with the term "inherently governmental" is that really and truly, when you think of most things that government employees do, they really are very similar, and often identical, to the things that private employees do, even things that staff of this Congress does. The information processing, analysis, communications are all things which private firms do and supply. I would suggest in going forward with this that there be four principles rather than using the term "inherently governmental."

One test would be the centrality of a mission of a function to the overall mission of the agency. The second would be the frequency with which the transactions would need to occur. In the private sector it is the case that, the more frequent the number of transactions are, the more wisdom there is in using the make decision rather than the buy decision. The more uncertainty there is about—certain products are very clear. You know if the wall has been painted or the wall hasn't been painted. But when you start to deal with services where there can be real differences of opinion about what's been accomplished, it's often wiser to think about keeping those functions in-house. So that would be my third criteria.

My last one would be whether or not there are very highly specific assets that are used to undertake the work. When they're very specific and vital, it's much wiser to keep those things in-house and keep control of them. It's very different hiring somebody with a pickup truck to mow the lawn than to try and find someone with say an M–1 tank. That's to make the most polar case I can.

I would urge, in moving forward, if contracting is going to move forward, that these broader concerns be taken into account.

I thank you for your time in listening to me and I'll be more than happy to answer questions.

[The prepared statement of Mr. Sclar follows:]

Testimony of

Elliott D. Sclar,
Professor of Urban Planning,
Columbia University

before the

Subcommittee on Government Management, Information and Technology
of the
Committee on Government Reform and Oversight,
House of Representatives,
Congress of the United States.

August 6, 1998

Re: Title II of H.R. 4244
"Federal Activities Inventory Reform Act of 1998"

Introduction

Chairman Horn and Members of the Subcommittee, I appreciate the kind invitation you have extended to me to testify on Title II of H.R. 4244 the "Federal Activities Inventory Reform Act of 1998" (Title II).

My name is Elliott Sclar. I am Professor of Urban Planning at the Graduate School of Architecture, Planning and Preservation, Columbia University in the City of New York. I am an economist. I study the economics of privatization. In the American context the term privatization is somewhat misleading. It tends to refer to efforts to increase reliance on contracting in the performance of public service. It is therefore more accurate to think of the subject matter of domestic privatization as effectively the economics of public contracting. The crucial issue then pertains to the relationship between public contracting and organizational performance. It is always a complex relationship, and often problematic. Title II will vastly expand the scope of public contracting in the ongoing operations of federal agencies. Therefore the implications for the cost effectiveness of federal public service are potentially vast.

Is such change a good or bad idea? The answer depends upon the goal of the legislation. If the goal is simply to realize a value judgment that more public contracting is inherently a good idea, Title II is a promising piece of legislation. If the intention is to contribute to improvement in the

performance and cost efficiency of federal agencies. then this title is more problematic.

Implications for Organizational Efficiency

Although the language of Title II builds upon the language of the A-76 process, it adds a new and ultimately costly mandate to the operation of federal agencies. It not only requires that each agency distinguish activities which are deemed "inherently governmental in nature," from those which are not, but it subjects those executive judgments to challenge from outside parties with a pecuniary interest in the way the federal government serves the public interest.

The problem here is that it is often not easy to distinguish tasks which are inherently governmental in nature from those which are not. Much depends upon the relationship of those tasks to the overall mission of the agency. The clear intent of Title II as it is now written is to foreclose the possibility that agencies can use this type of argument, regardless of its validity, to avoid contracting on this score. By providing explicit standing for outside parties with a monetary interest in expanding contracting options to challenge executive decisions in this area is, in effect, an invitation to great and expensive mischief at taxpayer expense. The legislation in no way limits the right of aggrieved outside parties to seek judicial redress if they are not satisfied by the agency response to their objections.

It is easy to see this legislation leading inexorably to more, not less bureaucratization of the public sector. This new bureaucracy will arise to administer and defend the process by which federal agencies decide which tasks should be performed directly and which ones should be properly outsourced. The question of the actual effectiveness of agency performance will become a secondary consideration, as direct accountability is lost in the myriad of contractual clauses and rules.

The organizational problem is that two different parties with stakes in the outcome can look at the same task and draw different conclusions about its appropriateness as a contractual service. It is easy to foresee that, if the stakes are sufficiently high, the conflict will quickly spread from an administrative appeal procedure to a political one and inevitably into an expensive and time consuming legal adjudication of the decisions required under this title. Consider what might plausibly occur if Congress was not exempt from the legislation. Lawmaking is easily identified as an inherently governmental function. But the bulk of the activity which

surrounds the pure act of legislating is certainly open to question. Effective law making depends upon a host of information processing, data analysis and communication skills that can be supplied by many outside firms. At present these skills reside an army of competent staff assistants, secretaries and interns on the Congressional payroll. Although Members of Congress might disagree, an outside firm or industry association could make a compelling case under the terms of Title II that they could supply the needed services at a much lower cost. The nature of objections to such a "privatization" claim would rest heavily upon the qualitative nature of relationships among Congressional employees and between them and Members of Congress. The mission of the United States Congress depends critically upon the need for workplace flexibilities and individual employment continuities which would prove infeasible in the more rigid world of specific services delivered via a public sector contract.

As this legislation now stands, it is an invitation to slice public agencies into pieces which will become ever more unwieldy to coordinate and manage as a unit simply because the tasks look like what a private firm might be able to provide. As a general rule blanket provisos such as the ones inherent in this title, almost invariably invite the wrath of the law of unintended consequences to rain down upon us. Only if one believes that the organizational integrity of public agencies is essentially worthless, can the risks which inevitably accompany such a drastic policy change be perceived as a small price to pay.

The Market Economics of Contracting

Title II further mandates that federal agencies use "a competitive process to select the source" from whom they will obtain services. The presumption here is that competition among private providers ensures that the government receives the best product at the lowest price consistent with efficient production costs. That theory resides quite far from the actual practice of public contracting. As a matter of general observation it is important to note that approximately one-half of all public spending is done via contracting. Too large a percentage of that contracting is carried out in situations in which there is only one bidder or at most two or three who scarcely meet the economic test of a competitive market. A recent study by the State Auditor in California found that a full two-thirds of all public contracts are let on a sole source basis.[1] While the situation in Federal contracting may be better, I suspect that the order of magnitude is similar.

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[1]California State Auditor, "State Contracting Reforms are Needed to Protect the Public Interest," 1996.

Scarcely a week passes in which somewhere in America a controversy erupts around the letting of public contracts. This happens for a complex set of reasons, not the least of which is that while we all love competition when we are buyers we hate it when we are sellers. Sellers spend more time in the marketplace than do buyers hence they devote a great deal of energy to undermining competition with its thin profit margins.

When one looks at public contracting, it is noteworthy for the speed with which competition consistently evaporates on the supply side of the market. In 1988 the Colorado legislature passed a law requiring that, beginning in mid 1989, 20 percent of fixed route public bus operations in metropolitan Denver would have to be provided by private contractors. The experience there illustrates the way in which a seemingly competitive public contracting opportunity evolves into an oligopolistic market structure.

The Denver privatization experience is of particular note because of the lengths to which its architects went to try to ensure that the contracting would remain competitive. To discourage a new, private monopoly from developing, the statute prohibited any single contractor from winning more than half of all the contracted business. After four years, the packages were to be rebid. The intention was to create an ongoing system of competitive rebidding in which the Regional Transportation District (RTD) would always be able to purchase the needed service from the lowest-priced acceptable provider among a continuing cast of several potential contractors. This intention relied on what proved to be an untenable assumption--that a market with a sufficient number of qualified sellers could somehow be self-sustained.

Eighteen companies, some of them local charter operations and cab companies, attended the initial bidders meeting. The turnout gratified privatization advocates in Colorado, who, like advocates of privatization elsewhere, based their hopes that a large competitive market would materialize from the dozens of small transportation companies listed in the yellow pages of any metropolitan area. However, when one examines the actual market for privatized urban transit, it turns out that a handful of national firms consistently win the major contracts. These firms have the resources to write expert proposals that respond directly to an agency's request. They have easy access to the requisite bonding and insurance, and hence to the financing necessary to fulfill any commitments into which they enter. This is no small consideration for the public boards charged with fiduciary responsibility for public funds. Consequently, the effective contract transit market has never consisted of the many small suppliers

listed in telephone directories, but of the few big ones found side-by-side in the exhibition booths at national transportation conferences.

The RTD ultimately received eight bids and awarded three contracts. All of them went to national companies: Mayflower, Laidlaw and ATC/Vancom. Typically, the strategy of such large firms is to capture a new market quickly and drive out small competitors by submitting an extremely low initial bid. Sure enough, Mayflower offered an exceedingly low price of $28.26 per vehicle revenue hour on the first contract. A vehicle revenue hour is the cost of operating a bus one hour in passenger service. This bid price was below the cost that the RTD's privatization consultant, KPMG Peat Marwick, concluded was necessary to break even.[2] Even if smaller local firms could have cleared the hurdles of proposal writing and fiscal security, they lacked the cash reserves to take a loss on a first contract. KPMG Peat Marwick warned the RTD that the initial prices it was being charged were strategically motivated and did not reflect what the service actually cost.[3] By 1993 Mayflower's price had risen to $54.65 per hour, almost double the initial price but far more realistic. The 1996-97 rates ranged from $62.74 to $64.51 per revenue hour. This is about the same cost as public operation.[4]

Once the Denver market became established, there was scarcely a whiff of competition. Mayflower and Laidlaw merged in 1995. Under the terms of the 1988 privatization law, this should have triggered a search for new competitors for the next round of contracting. However, the consolidated operation successfully lobbied the Colorado legislature to modify the law, effectively legitimating its de facto market dominance.[5]

The original privatization bill had been sold to the legislature with the argument that the efficiency engendered by competitive privatization would reduce operating costs by 40 percent if enacted system-wide.[6] In 1988, the year the legislation was enacted, the RTD had an operating budget of approximately $100 million per year. By the end of 1990, the first full year of privatization, operating costs had jumped over 12 percent

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[2]KPMG Peat Marwick ("Denver RTD Privatization Performance Audit Update: July 1990 - June 1991," Final Report, November 1, 1991.

[3]"Without knowledge of the overall strategy of each contractor, which is subject to change, the financial performance of individual units of larger businesses may not give any indication of the future price strategy of each contractor." KPMG Peat Marwick ("Denver RTD Privatization Performance Audit Update: July 1990 - June 1991," Final Report, November 1, 1991, pg. 2.

[4]Sclar, Elliott, "Paying More, Getting Less: The Denver Experience with Bus Privatization 1990-1995," prepared for the Amalgamated Transit Union, February 1997.

[5]House Bill 96-1360, signed into law on June 8, 1996.

[6]"Bill would privatize RTD bus operations," Rocky Mountain News, January 9, 1988, pg. 12.

to $112.3 million.[7] This sharp increase was particularly troubling because when privatization was initiated, the RTD was one of the nation's most tightly run transit operations. Between 1986 and 1988, it had actually reduced operating expenses by about 4 percent. Between 1990 and 1995, the cost of contracted service swelled from approximately $14 million to almost $29 million--more than 100 percent. Meanwhile the cost of directly provided service increased by just a little over 11 percent. In six years, privatization cost the RTD more than $9.2 million.[8]□

Today two providers control the private transit market in Denver, and their oligopolistic interdependence has become apparent. A recent round of bidding resembled a game of musical chairs. There were only three bidders in 1997 for four newly configured packages of routes, and ATC/Vancom made the winning bid for all of them. (The second, higher-priced bid came from an "outsider," Grosvenor Bus Lines.) This turn of events might have seemed surprising, since Laidlaw had previously controlled the lion's share of operations. But this time around, Laidlaw bid on only one of the bundles. In early 1997 Laidlaw purchased ATC/Vancom's national school bus business. ATC/Vancom was shedding its school bus operations in order to concentrate on public transit. And Laidlaw? Perhaps it bowed out of the bidding in Denver because it preferred to concentrate on the school bus market. But that did not deter the company from lobbying the Colorado legislature during its spring 1997 session to expand privatization to 50 percent of the RTD's service. The campaign failed.[9] Since then Laidlaw has purchased the operator of the RTD's paratransit service.

The cost and efficiency considerations that should be the alpha and omega of competitive contracting are now besides the point. Contracting decisions in Denver are driven by the strategic considerations of the contractors in control of the Denver market. Once a regional leader in public transportation, RTD's management has been reduced to a nearly passive broker attempting to mediate the often conflicting claims of the riding public, taxpayers, labor unions and the powerful contractors with greater designs on the national transit business.

Westchester County, New York privatized its entire bus service in 1975. In the beginning, sixteen companies were operating routes, none of them carrying more than a third of the county's passengers. Within a

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[7]Unless otherwise specified, all the financial data in this report are taken from the Comprehensive Annual Finical Reports of the Regional Transportation District. They are all audited by a national CPA firm.
[8]These figures are derived from "RTD Bus Cost Model Documentation. October, 1996."
[9]A subsequent campaign was attempted in early 1998. It too failed.

decade the number of contractors was cut by half. and the largest remaining company was collecting 93 percent of the fares.[10] By 1997, the largest operator controlled 97 percent of the operation.

To say that government must learn to contract smarter is simply not helpful. It essentially puts the weight of blame for a situation in which the strongest incentives to undermine competition are "built-in" on the supply side on to the buyer. The Committee must appreciate the difficulty of sustaining competition for public contracts. Firms engage in mergers and acquisitions as well as other legal practices to eliminate and dominate competitors. That is especially true among firms engaged in public contracting. Absent meaningful competition, the rationale for extending contracting becomes weak to nonexistent.

It is also important to remember that privatization via contracting relies heavily on the belief that most contracts can be made almost self-enforcing. Yet the necessity for a written contract arises because each party to a transaction fears that the other party or parties may fail to deliver or perform. Thus contracts contain descriptions of the future behavioral obligations of both parties, to the extent that such behavior can be anticipated, and of the sanctions to be imposed if any party fails to hold up its end of the bargain. Such future-oriented obligations, created in an atmosphere of uncertainty, place the public agency and its contractors in a far different relationship to each other than cut-and-dried contracts typical of discrete purchases such as a contract to put a fresh coat of paint on the dome of the Capital. The extent of this divergence between markets for clearly defined and limited products and ongoing services is critical in determining the comparative efficiency of the privatization option.

In much of the privatization debate, the expensive transactional complexity of ongoing contracts is typically ignored. The contracting process is treated as if it were effectively a trivial modification of discrete contracting situations. Accordingly, all one need do is announce the availability of the contract through a request for proposals or RFP, specify the contract contingencies and terms to all the potential bidders and allow the bidders to set the price competitively - typically lowest bid wins. To the extent that it is that simple and straight forward, the use of contracting for long term service provision becomes identical with discrete purchasing. However the type of contracts which will be encouraged by Title II will most likely be for less standardized and more specialized outputs in which

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[10] D'Adamo, R. Raleigh "Westchester's Public/Private Partnership in Transit: A Decade of Experience." Paper presented at the APTA Annual Meeting, Los Angeles, CA, October 1985.

the less obvious, but highly important, aspects of quality and the greater degree of uncertainty, force a more complex managerial decision and monitoring process upon agencies.

We do well to remember that a good portion of the lucrative practice of corporate law involves nothing more than litigation among parties claiming breach of contract or seeking resolution of differing interpretations of contract language. If contracting is that difficult and expensive in the private sector where the parties at least are clear about the bottom line they are pursuing, why would one suppose it is going to be easier in the public sector where the output is not as easily valued by market criteria?

When is it less expensive to maintain the size of an organization to accomplish necessary tasks? When is it more economical to purchase them from outside vendors? Together these two questions comprise the essence of what is known as the "make-buy" decision. Put slightly differently and from an organizational perspective, when are the internal bureaucratic costs which accompany larger agency size less than the external transactions costs of using the market?

To answer that question it is necessary to understand that the word market is too broad a frame of reference for policy making. A helpful starting point is to distinguish between spot markets and contract markets. Spot markets are akin to "buying off the rack," and contract markets are similar to custom tailoring. When an organization decides to buy rather than make, it goes shopping in either a spot market or a contract market. Spot markets are typically used to acquire products such as office supplies and motor vehicles, which come in sufficiently standardized forms that commercial vendors routinely maintain them in inventories and which would be virtually impossible for firms or agencies to make themselves. But some long-term services that organizations can readily perform themselves also fit in this spot market category. A business firm might prepare its payroll internally, in its own bookkeeping office, or it could hire an outside payroll service. A periodical publisher could process its own subscriptions and mail its own journals, or it could hire an outside fulfillment company.

When the choice is between spot purchases of standardized products or internal production, the decision rule is essentially a matter of comparative direct production cost analysis. The organization must compare its internal production costs with the cost of purchase. The transactions costs are virtually zero as a result of the standard units in

which the product is traded and used. Learning the price and quality often entails little more than two or three phone calls. Typically, goods available in spot markets are sold in competitive environments. Product quality is usually obvious to all buyers and sellers. Competition ensures that retail prices hover just above the level of wholesale prices and that average quality suits the taste of average buyers.

Such simplicity is not the rule when the make-buy decision involves contracting for ongoing customized services, as will be the case with this title. The choice of sellers is almost invariably more limited, and both product quality and the relation of contract price to underlying costs are governed at best vaguely by market competition. Indeed in many instances quality is not known until the product is purchased. Economists make a distinction between search goods and experience goods. Most of the goods sold in spot markets are search goods. Quality is known and price is the principal concern. Experience goods are goods which can only be evaluated once they are tried. This is almost invariably the situation agencies face when they hire contractors to take over tasks they formerly performed. As a consequence of these characteristics of the markets and goods, decisions to contract out usually involve complex and significant time and money transactions costs related to the specification of product, the negotiation of prices, the close monitoring of quality, and the need to anticipate unforeseen contingencies. In such cases the managerial decision process involves analyzing not only the comparative production costs typical of spot markets, but also the less tangible transactions costs associated with contract design and monitoring in cases in which the short comings of a particular supplier only become apparent after the deal is struck and breaking the contract imposes new costs.

Comparative Costs

Title II does properly call for a comparative cost analysis as part of the process of deciding on contracting. However it fails to consider some of the important complexities of comparative cost accounting. Three sets of cost must be considered when deciding between public contracting and public production: the direct costs of public production, the costs of the outside service and the internal transactions costs a contractual arrangement incurs. Public production costs include the personnel, equipment and materials. The costs of outside service are typically the agreed upon price of the contract. Transactions costs include everything related to bidding the contract, letting it, and supervising the contract work. The calculus comparing public and private production must include the transactions costs. It does not matter whether the private sector is more efficient at

production than is the public sector. What is crucial is whether the sum of both the contract price and the transactions costs are less than the cost of direct public provision.

During the 1980s a spate of comparative cost studies seemed to provide overwhelming support for the notion that privatizing public transit yields massive savings. If true, these findings were of major consequence. They figuratively meant that we could have our cake and eat it too. Transit, which is so vital to the functioning of our great metropolises, could be expanded and budgets could be held constant or even cut. Ralph Stanley, the UMTA head in those years summed up the findings as follows:

> ...we've done a number of policy studies and economic analyses that show savings in bus operations ranging from 10 to 50%... We've taken a look at the economics of running a bus system, and shown beyond a shadow of a doubt that it's more efficient to be run privately.[11] (emphasis added)

Like most "beyond a shadow of doubt" conclusions, these numbers are in fact too good to be true. Virtually all of them were generated using an inappropriate accounting methodology. Known formally as fully allocated cost accounting, it essentially requires that the direct public operating costs of transit routes such as driver compensation and fuel which would obviously disappear as a result of privatization be combined with an estimate of the proportion of fixed system overhead for items such as payroll administration and marketing which can't diminish. The result is to grossly overstate the amount of money which can be saved by comparing an artificially inflated estimate of the reducible internal costs of public operation.

Both economic and accounting theory are unanimous on this point. The proper way to measure the savings resulting from privatization is through the use of an analytic method called, among other things, avoidable cost accounting.[12] This method compares only the additional costs incurred as a result of an action with resulting actual cost reductions or revenue improvements. If the avoided costs exceed the new contract related costs, savings will result. If not the status quo is preferable.

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[11] Andy Ryan "Public vs. Private Testing Buses in Miami," Mass Transit, Vol. 14, no.1/2, January-February 1987, pgs. 12 & 68.

[12] The technique is sometimes call marginal or incremental cost accounting. These two terms are typically used by sellers, rather than buyers to assess their additional costs of providing a given product to a new customer.

The differences between fully allocated cost accounting and avoidable cost accounting can be substantial. Indeed, fully allocated cost accounting often demonstrates savings even when an agency actually loses money as a result of the privatization. This is precisely the trap into which the Santa Barbara Metropolitan Transportation District fell when privatization was vigorously promoted by UMTA as the solution to the nation's transit problems. According to then General Manager Gary Gleason:

> We had a private sector bid a year ago...They bid about $980,000 on this 20 percent segment of our service and our fully allocated costs are within the neighborhood of $1,000,000 so that there was about a $20,000 savings over a year's period to operate this part of Santa Barbara's service. However, in looking at our incremental costs and being able to identify... what people in the shop would be laid off, we were able to identify very precisely where a cost reduction would be and as we found out, our cost reduction would, in fact, only be about $380,000 per year. So in order to take advantage of this so-called private sector situation, it was actually going to cost us an additional $600,000 to participate with the private sector. And right now we are in the process where the sole bidder that we had on the project has protested both to the Washington headquarters of UMTA and the regional headquarters and they have won their protest... as the general manager, I'm the one that's responsible every year for writing the checks, and I know, in fact, that if I accepted the bid, that I would have an additional $600,000...cost.[13]

To understand in a less anecdotal and more systematic manner the way in which these costs can vary, consider a series of cost studies done of the Foothill Transit Zone (FTZ), established in 1988 by the Los Angeles County Transportation Commission as a privatized operation. The FTZ is a quasi public agency which contracts with private providers to runs 14 lines formerly served by the Southern California Rapid Transit District (SCRTD) in the San Gabriel and Pomona valleys. The Los Angeles County Transportation Commission hired Ernst & Young to conduct an FAC

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[13] Tape transcription, American Public Transportation Association tape #88-19, "Privatization: Is a Level Playing Field Possible?" Session held at the 1988 Annual APTA meeting, Montreal, Quebec, Canada, October 2-6 1988.

analysis of the FTZ. It concluded that the FTZ generated a 43% cost savings.[14] However the SCRTD commissioned an avoidable cost study by Coopers & Lybrand which found that in fact SCRTD and FTZ costs differed by less than one percent, and that when the figures were corrected for cost differences engendered by differences in the ages of the two operators' bus fleets, SCRTD, the public operator, was actually 7.6% less expensive.[15] This conclusion was confirmed by a follow-up study done by MIT for the Los Angeles County Transportation Commission.[16]

In general, fully allocated cost accounting is favored by those seeking to promote privatization. In a candid letter to Jack McCroskey, the former Chairman of the Board of Directors of the Denver Colorado Regional Transportation District Robert Peskin a senior manger at the consulting firm KPMG Peat Marwick wrote:

> There are convincing arguments that such a fully-allocated approach is not appropriate (my emphasis) in the context of contracting (Peat Marwick's emphasis) of transit service, as in the case of privatization.[17]

He concluded that "Incremental cost (read avoidable cost) analyses yield hard 'out-of-pocket' estimates of savings that are useful in real world decision-making." Even the staunchly pro-privatization Reason Foundation concurs:

> The use of fully allocated costs is generally inappropriate in estimating the savings to be realized by contracting out a target service that is currently being conducted in-house... When attempting to determine the potential cost savings associated with the contracting out of a target service, the appropriate in-house costs to use in the comparison are the "avoidable costs." [18]

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[14] Ernst & Young, "Evaluation of the Foothills Transit Zone, Fiscal Year 1990 Report to the LACTC," July 1991.

[15] Coopers-Lybrand "RTD/Foothills Transit Zone: Review of Marginal Cost Analysis Approach," July, 1991.

[16] Richmond, Jonathan, "The Cost of Contracted Service: An Assessment of Assessments," prepared by the MIT Center for Transportation Studies for the Los Angeles County Transportation Commission, July, 1992.

[17] Correspondence from Robert Peskin/KPMG Peat Marwick to Jack McCroskey, February 11, 1991.

[18] Martin, Lawrence, "How to Compare Costs Between In-House and Contracted Services," Reason Foundation How to Guide #4, March 1993, pp. 9-10.

Increasingly public audit and fiscal oversight agencies at the state and local levels are becoming unanimous in calling for the use of avoidable cost models to perform the kind of comparative analysis privatization decisions demand.[19]

Although it can be argued that fully allocated cost accounting can estimate long-term savings because as direct public service activity shrinks over time, so too will overhead, the contingent future is a poor basis on which to defend privatization in the present. If a change does not lead to cash savings in the short run, given the vagaries of public operations, it is unlikely that taxpayers will see them the long run.

In defense of fully allocated cost accounting, it is argued that it is "unfair" to private contractors who must absorb all of their costs to be forced to compete with a public agency that only has to consider its avoidable costs. The problem with this argument is that it loses sight of the goal. The goal is fairness to the taxpayer. Contractors are just a means to that end. The taxpayer is ultimately stuck with all the overhead costs, regardless of how they are allocated. The question from a taxpayer point of view concerns how to get the most intensive use of the resources for which they have already paid.

Conclusions

Public contracting is not an end in itself. Even in its own terms public contracting has a long and spotty history as a means of obtaining needed public goods and services. To be an effective element in improved agency operation, it must be integrated into a comprehensive effort of agency reform. The problem with this title as it is now stands is that it fails to address the other elements of which must also be in place if increased contracting is to make a contribution to improvement. By itself it runs a great risk of making matters worse.

Such far reaching change will not occur by legislative fiat. It requires the cooperation between the executive branch and the legislative branch along with the active involvement of the managers and employees who actually carry out the important day to day work of the Federal

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[19] See for example, New York City Office of Management and Budget "Contracting-In Cost Comparison Manual," Office of the State Auditor. Commonwealth of Massachusetts "Guidelines for Implementing the Commonwealth's Privatization Law"

Government. Congress can play an key leadership role in bringing the players together to launch this change process.

Mr. SESSIONS. Thank you, Doctor.

Our fourth panelist today is Mr. Max Sawicky, economist from the Economy Policy Institute.

Mr. SAWICKY. Thank you. That's Sawicky and it's the Economic Policy Institute. You were close enough; 9 out of 10 people would get the pronunciation, unless they are from Poland, I think. [Laughter.]

As you said, I'm an economist, and like Elliott, I study, among other things, the question of efficient public sector provision. I am grateful for the opportunity to address the committee. I understand that the topic in one sense is the amendment, but since you may think twice before inviting me back, I can't help myself in addressing some of the broader issues around the amendment and the other legislations. I will talk about both to some extent.

In a nutshell, I would suggest that the amendment and the bill put over emphasis on foresight and insufficient emphasis on hindsight. At the risk of being mistaken for Reverend Jackson, I think that doesn't add up to oversight.

First of all, there's an inconsistency in the remarks that I've heard from my copanelist in some of the legislation and in some of the language, between the right of private sector providers—so-called right—to win a contractor or be awarded a contract, versus the goal of efficiency. Efficiency meaning simply getting a good product at a low price—the relationship between cost and output.

The idea of freedom from government competition, it seems to me, clearly conflicts with an unambiguous goal of efficiency in public sector provision. If it proves to be the case, the Government can do a job more effectively; in other words, at a lower cost and with a better product than the private sector. Then from the taxpayer standpoint, that's where it should be—with Government. So that could indeed conflict with a private sector operator's ability to win a contract. To elevate that to a right seems to me extraordinarily unusual. We hear a lot—too many rights are being generated these days. As rights go, that seems to me one of the more unusual ones. Certainly there's a right to compete. There's a right to pursue a business, but the right to exclude a party to competition, namely, public sector employees or agencies, is quite a different thing.

I'm a little bit puzzled because it seems like some of the remarks have gone in both ways. We want efficient provision, but we want freedom from government competition, or some variation of that. Now that is an extension of what's been a more general crusade for privatization, which we've witnessed in the United States for the past two decades—crusade in the sense that the elevation of private sector providers over a public sector is taking on an axiomatic character that becomes an automatic or reflexive thing. As if in every case, a private sector operator could always be more efficient.

Now, unlike some people, I would take a firmly ambiguous position in the sense that, I would say, in some cases, unquestionably private sector providers are the preferred choice, but in others it would be public sector, and the current sorting out may not be the right one. So there's no question that some things that are now public might be privately provided, albeit publicly financed. Some things that are privately provided, or oursourced, might profitably be brought back into the public sector. That goes to my hindsight

point. It seems to me that's the emphasis that needs to be upheld, which I find lagging a little bit in the legislation.

As Elliott said, there is a presumption in this privatization crusade that contracts are self-enforcing; whereas, of course, the contract is only the first stage in the process which requires monitoring by public managers, collecting information, evaluation of that, and reaction to that information by public managers.

In the breach, it's typically those latter stages that are neglected. This is not only true of the Federal Government, but State and local governments. When you look at surveys of why contracting is done, you often do not get answers like, "This is the best way to do it." You get answers like, "This is the law," or answers like, "This is the way we've always done it"—or other things outside of what we would think would be our primary goal, which is efficiency—a better output for a lower price.

Now, in particular, in terms of the amendment, I would go a little further than Elliott and others in saying I don't see the point of a list at all based on an abstract criteria for what looks like government and what doesn't. If you look at the language of the amendment, it's not hard to tell a story that would qualify almost anything as on one side or the other, I think.

Rather than a list, my recommendation to the committee is that whether something ought to be public or not is a question of cost analysis or efficiency analysis. At the end of the day, it's whether you determine which method gives you the best bang for the buck that determines whether something is better done out of the public sector or via private sector providers. To promulgate abstract definitions in this vein, I don't think is helpful at all.

This goes to the value of competition being applied equally, not only to things that are now public, but which might better be done privately, but, as others have said, things that are now privately done which might better be done publicly. I think competition is the goal, not oursourcing per se, not contracting per se, not privatization per se. Efficiency is a goal. The taxpayer's interest is what's in question here—the public interest. I don't see an abstract list which refers to some empty philosophy as superior to the ongoing and perennial task of analyzing what we're getting, what it's costing, and how we feel about that result.

In closing, let me say I commend the committee for pursuing the goal of competition, but I urge you to, in promulgating rules that make it a fair competition, not set conditions or bias the process such that public sector employees, present or future, existing or potential, not have the opportunity to make their case that they can do something more efficiently than private sector providers can do. In the end, if that rule is followed, that rule of competition—unvarnished competition—with full participation on by both sides, in full Democratic evaluation, incidentally—by outside parties, not merely parties with a vested interest—one way or the other, I think in the end we'll all feel better about the results of this pursuit.

Thank you very much.

[The prepared statement of Mr. Sawicky follows:]

Efficiency Beats Ideology: Economizing in the Public Sector

Max B. Sawicky
Economic Policy Institute

Statement submitted to the
Subcommittee on Government Management, Information and Technology,
House Committee on Government Reform and Oversight

August 6, 1998

I would like to thank the Subcommittee for permitting me to provide my views on Title II of HR 4244, Federal Procurement System Performance Measurement and Acquisition Workforce Training Act of 1998.

I am afraid this proposal is of no help at all in improving the delivery of public services. A tip-off is its genesis as an effort to win "freedom from government competition." Such an effort is misbegotten and misconceived. Surely our business here is to improve efficiency, and in this endeavor we need to take a fresh look at all public services. What we really need is freedom from ideological prejudice. Such is my understanding of oversight.

A simple criterion for any effort to promote competition is its success in establishing fair and equal treatment for all participants and objects. The proposed legislation takes the wrong tack in basic respects:

- Defense-related functions are not treated the same as domestic ones. It's not as if our defense sector enjoys a marked superiority to the rest of the government in the realm of efficient procurement and management of contracts;

- Public employees and agencies are not afforded the same capacity to participate as are private entities. Often in public contracting there are few bidders, and this naturally inhibits the effectiveness of the policy. Preventing public entities from participation is the wrong policy. Strong advocates of contracting advocate a level playing field in this context. In this vein, the amendment confuses the process of cost comparison,

lumping overhead costs (which would apply in any case) together with the costs of provision under public auspices;

- The widest circle of democratic participation in the evaluation of the process, including public interest groups, is not encouraged. Often these groups are the only parties without a direct interest in the outcome of the privatization decision.

- Existing contracting arrangements are not subjected to the same scrutiny as existing publicly-provided services. There is no reason to expect that government functions are free of problems in one respect but not the other.

The notion of "freedom" conjures up that of "rights." Conservatives have said, with some merit, that we are more prolific in the generation of rights than of responsibilities. In the present context, the analogy is that we are better at issuing fiats about how government is supposed to work, but not as good at the timely evaluation and remediation of government performance. This is also true for state and local governments, incidentally. Giving contracts is easy; analyzing their effectiveness and using this information to take remedial action is hard and, not surprisingly, contract oversight is often neglected.

In the proposed legislation, rather than tools for the improvement of evaluation, we have an exercise in taxonomy. Specifically, we have an effort to promulgate standards for what is "inherently governmental" and what isn't. One problem is the type of standard at issue; the second is the specific content being proposed.

The type of standard is a definition of "governmental." I see no reason to seek such a definition. From an economic standpoint, what matters is input and output, or cost and performance. The method of provision that satisfies our goals for cost and performance should be the criterion for what is governmental or not. The legislation makes no contribution in this vein. Instead it proposes an abstract definition of what is "governmental." The taxpayer's interest is in cost and performance, not philosophical rumination.

Secondly, the definition proposed is sufficiently broad and vague to admit everything or nothing. For instance, consider the function of trash pick-up.

It does not take much imagination to tell a story of how trash pickup is or is not inherently governmental under the language of the bill.

In summary, the enterprise of defining what is governmental has no value, and the method proposed is vacuous.

In the spirit of reinventing government, I would commend to the Committee an entirely different approach: work to reduce the regulation of government operations and grant public agencies greater, not less, discretion. At the same time, take greater efforts to evaluate performance and establish good and bad consequences for outstanding or unsatisfactory results.

Thank you for the opportunity to address the Committee.

Mr. SESSIONS. Good. Thank you, Mr. Sawicky.

What I'd like to do is lead off the questioning, if I could, and then I will go to our ranking member. Then at that time, I will ask if he has any opening statement that he would like to make, now that he's here.

The first question I would like to ask both of you, Mr. Sawicky and Dr. Sclar. Dr. Sclar, your No. 4 was of the criteria highly specific assets. If these, I guess, critical mass, could be achieved, I heard you say it's better to keep in-house? I think that what we have tried to do is come up with a compromise that allows both government and industry that opportunity to compete for those inherently governmental functions, and I think the compromise that we've tried to reach here is because of the No. 4 that you talk about.

Many times we are finding within government that government, because of the allocation of resources from an outside body, meaning the Congress of the United States, does not have those tools—or I believe you mentioned the tools in the toolbox—that are necessary to effectively compete with and to be leading edge with a private sector. It then becomes a question—and I'd like for you both to discuss it—what is critical mass? How big does this have to be before we have highly specific assets and better to keep in-house, if you don't even have leading edge tools and cannot stay up with the marketplace? So it's a question of marketplace and leading edge, and then the ability to get money by government. Can you help me along that line?

Mr. SCLAR. I'll try. If I reinterpret or misinterpret your question, please keep me on track.

Where that came from—those four criteria—it came from looking at private organizations, private corporations, and looking at the conditions under which they would make and buy decisions.

And by critical assets, what I was referring to would come—it's often not possible sometimes to know what the specific assets are, but sometimes we do. The simplest, most famous recent story could be the International Business Machine Corp. IBM decided in 1982 to go into personal computers, and because they were hardware companies, they didn't think much about software. So they found a little company in Redmond, WA and said, why don't you produce the operating system and you can have the copyright on it? Now, whose stock would you rather own today? I mean, IBM has made a comeback for sure. The point was, they lost control of a very specific asset that would have made a very big difference in their business. General Motors has a story like that with the Fisher Body Co. way back in the 1920's.

My only point in this is, where this comes into effect is in items such as when you get management information systems and some of these other crucial areas. I consult with public agencies on this, and with working with management consulting firms, and what becomes clear is that you can't just say, well, contract out the whole thing. The Union Pacific Railroad, a few years back, decided to contract to IBM its management information system. We've all been hearing about the development coming in your home State, too, between Southern Pacific and Union Pacific. But this goes back even further.

Earlier in the decade, when they contracted, they turned over their whole MIS system to IBM, which would seem logical in terms of cutting-edge technology and who would know things. But the truth was that there was a lot of in-house information. As a result, they were at some point sorting out trains by hand because they lost control of it. I think the situation is getting better.

But my point simply is that one of the tests that one should use is, what technology or what assets does the government have that over time it wants to maintain control of, even if it parcels out pieces of it to private contractors?

On the question of leading-edge technology, I think in a lot of cases a lot of the things that we're talking about contracting out are often not at the leading edge. Oftentimes, they're very labor-intensive jobs and the technology that's used very much is in the public domain. The question there becomes, how do those jobs tie into a larger mission?

I mentioned Congress earlier. In my longer, lengthier testimony which I submitted, I hypothetically stated if Congress came under this, what would happen if you had to contract out all your secretaries and interns to an employment service? The argument against it would be that there is certain information-flow that would be lost in the discontinuities, and even though it's not an inherently governmental function, it very much is crucial to the legislation, which is inherently governmental function.

As I began looking through the A–76 and the legislation, I realized it had sidestepped the very important question by saying, "inherently government." So what I was trying to do was make some suggestions of a better way to begin to cut through that and to begin to look at those things. Of course, the other piece is my concern about how you sustain competitive markets.

Mr. SESSIONS. Mr. Sawicky.

Mr. SAWICKY. Yes. I just have a couple of things to add. The more grand and complicated a particular asset, that would be something less likely to be provided by a number of different suppliers in a market. It would tend to be dominated by relatively few suppliers, as we've seen in the defense industry. We need to distinguish between a market working well from the standpoint of efficiency, which means good product, least cost, and a market working well from the standpoint of quality, which means very good outcome but not necessarily low cost. A handful of providers could prosper in such a setting, but we wouldn't necessarily call it efficient.

That goes to Elliott's point that there's a case for keeping such things in government, because in the event that this is routinely contracted, then one could easily end up with a situation resembling government residence of such an asset; namely, a very few number of providers, or maybe only one for that kind of asset, and something very like a monopoly without some of the advantages of monopoly from a private sector standpoint; maybe not as much investment in innovation, and maybe less advantages from the public standpoint, because being as how it was provided by a private sector provider, there wouldn't be quite as much control over the asset that would be most consistent with the public mission.

Economists have quite a few arguments over whether innovation results from competition or its opposite. We see, in markets where there are relatively few firms, the ability of these very large firms which dominate markets to invest a lot and to innovate in that sense. But often in markets where there's most bitter, cutthroat competition, that margin of resource for investment isn't forthcoming. So it isn't clear to economists, which makes it more difficult as a problem for this committee, whether contracting in that context is the most effective course to take.

It also, incidentally, is an argument for government support for investment in areas which would benefit a number of firms, but where competition prevents individual firms from taking the risk and not making the expenditure, but not reaping the reward.

Mr. SESSIONS. Good. Thank you. Now I'd like to recognize the ranking member, the gentleman from Ohio, who has been very active with me in working on this issue. I know and you know we've got to vote, but why don't you take the time until we get very close, and then we can continue with the process? Mr. Kucinich.

Mr. KUCINICH. Thank you very much. I just wanted to make an inquiry. We've got about 10 minutes to go before we vote. I think it would add some continuity here. I'm willing to break now.

Mr. SESSIONS. You'd like to not begin, then, and like to go vote and then come back?

Mr. KUCINICH. You have a problem with that?

Mr. SESSIONS. I will be honest; I have no idea—there is one vote or two or three? One vote? Thank you.

If I could ask our panelists, please, to stick around, there's interest in the discussion that we're having and Mr. Kucinich would enjoy that. I will say that is the thing to do. We will be in recess until just immediately after the votes.

[Recess.]

Mr. SESSIONS. We will now resume this hearing, and I would defer to the gentleman from Ohio, Mr. Kucinich.

Mr. KUCINICH. Thank you very much, Mr. Sessions, and members of the committee, and to our witnesses.

I would like to just ask a few questions, first, that are somewhat philosophical in their import, and I just want to make sure I have the pronunciation right. Palatiello? OK, Mr. Palatiello, from a philosophical standpoint, what do you see as the purpose of government?

Mr. PALATIELLO. I think the purpose of government is spelled out pretty well in the Constitution.

Mr. KUCINICH. What do you think? I know what the Constitution says. What do you think government's about?

Mr. PALATIELLO. I think it's about governing, which means establishing the rules in free society, basically, being the umpire between competing interests.

Mr. KUCINICH. So you believe in regulation then?

Mr. PALATIELLO. I believe that there is a role for government in some degree of regulation, yes, sir.

Mr. KUCINICH. OK.

Mr. PALATIELLO. Providing for our national defense, coining money, providing for the general welfare.

Mr. KUCINICH. What do you mean by the general welfare?

Mr. PALATIELLO. Providing an environment where people can enjoy their liberties and the pursuit of happiness. I don't think it's the role of government to assure happiness, but to assure people have the right to pursue happiness. I think that's what providing for the general welfare means, in my view.

Mr. KUCINICH. Does government have any role in providing services to the public?

Mr. PALATIELLO. Yes.

Mr. KUCINICH. What would that role be? I really am interested in knowing your view because, you know, you do represent thinking of probably a broad cross-section of industry, and I'd really like to know.

Mr. PALATIELLO. Well, for example, I think if you had a completely unbridled, free enterprise system, you would leave any company to do business any way it wishes. And I think, for example, you would not be able to assure public health, welfare, and safety if that occurred. I don't think we would have an environment as clean as we have today if there were not a role for government. So I think there are things along those lines where the government provides services to help assure a certain quality of life to the American people.

Mr. KUCINICH. Maybe I could help this line of questioning by getting more specific. Do you believe that government ought to have—that there ought to be public education government to deal with the public education?

Mr. PALATIELLO. Yes, I'm a product of public education. I may not be the best poster child for that, but I'm a product of public education. [Laughter.]

Mr. KUCINICH. Believe me, all of us are modest in making our claims. Do you believe in public parks?

Mr. PALATIELLO. Yes.

Mr. KUCINICH. Do you believe in publicly-owned electric systems, of which there are over 2,000 in the United States?

Mr. PALATIELLO. I think that's an area where government, at all levels, should take a harder look at private sector delivery.

Mr. KUCINICH. And, what about airports?

Mr. PALATIELLO. I believe—well, we have a lot of private airports in this country and I think many of them function well.

Mr. KUCINICH. What about public airports?

Mr. PALATIELLO. I think that's another area where privatization can be explored.

Mr. KUCINICH. What about water systems?

Mr. PALATIELLO. Again, I think there's a good track record of private sector operation of water systems, and that's a good thing.

Mr. KUCINICH. And what about sewer systems?

Mr. PALATIELLO. Same thing.

Mr. KUCINICH. What about waste collection?

Mr. PALATIELLO. Waste collection—trash pickup? Clearly, I think that's something the private sector should do and should be able to do more cost-effectively than the public sector.

Mr. KUCINICH. And what about street repair?

Mr. PALATIELLO. The actual repair of the streets? I think government should look at contractors to do that. The responsibility for

assuring that streets are well maintained is a governmental responsibility.

Mr. KUCINICH. When people pay their taxes to government, what do you think they ought to get?

Mr. PALATIELLO. I think they ought to get, for example, a judicial system that provides a forum for people to resolve differences and grievances.

Mr. KUCINICH. Do you believe in privatization of prisons?

Mr. PALATIELLO. Yes, I do think that there is a good track record with private operation of prisons. Yes.

Mr. KUCINICH. So, do you see anything that government really ought to do as a service, that ought to be government and not private sector? Should there be, for example, would you believe in a professionally trained private army?

Mr. PALATIELLO. No.

Mr. KUCINICH. Why not?

Mr. PALATIELLO. Because I think if you had a professionally trained private army, you would create competing interests and you would not have a single unified force to defend the country.

Mr. KUCINICH. Do you believe that there's anything in public service that really ought best be handled by the government?

Mr. PALATIELLO. Certainly. I think police protection is clearly something the private sector should do. Again, as I said before——

Mr. KUCINICH. That who should do?

Mr. PALATIELLO. I'm sorry, the public sector should do. I think again, as I mentioned before, assuring a clean environment and providing a reasonable regulatory framework, and then a traditional framework for enforcing environmental laws is clearly a governmental responsibility.

Mr. KUCINICH. What's the overall goal of the private sector? Business, what's the goal?

Mr. PALATIELLO. I think what you're getting at is the goal of a private company is to make a profit.

Mr. KUCINICH. And what's the role of government?

Mr. PALATIELLO. The role of government is to serve the people.

Mr. KUCINICH. Is the role of government to make a profit?

Mr. PALATIELLO. No.

Mr. KUCINICH. If the role of government is not to make a profit and to provide service, do you see any difference then between the role of government and the role of the private sector?

Mr. PALATIELLO. Yes. I think that there's a very clear distinction between both——

Mr. KUCINICH. Are their goals, would you say, often exclusive?

Mr. PALATIELLO. Of one another?

Mr. KUCINICH. Yes.

Mr. PALATIELLO. Yes, I think, by their nature, the two goals are exclusive of one another.

Mr. KUCINICH. I think you're right. My constituents back in Cleveland, OH—I can see there's a relationship between what they pay for service with their taxes and the service that they get to public accountability. There's a great concern that they lose accountability and they lose the ability to hold the rein on their taxes once great amounts of service, public services, get out of their control. I thought we'd show this dialog here.

One of the reasons why I'm so skeptical about so much privatization is that, once contracts go from the public, the work goes from the public to the private sector, we often have a condition where people end up having limited accountability. Usually accountability is through elected officials (a), and (b), that they don't have any way of holding a line on cost, because once you let your infrastructure get out of your control, you're basically at the mercy of those who are providing the services.

That's some of the concerns that people have about privatization. And if you don't have that control, inevitably your taxes go up to pay for the same services that you used to have some control over. That's why privatization ends up being so contentious from the municipal level, where I have a few decades of experience.

On a Federal level, some of the other issues that people are concerned about are as follows: People are concerned about the wages which are paid to employees who may stay in a contractual relationship with a new contractor, and government often profits. The private sector comes about as a result of cutting wages and benefits, because at some point something has to give. You cannot tell the public you're going to give them the same amount of services, same quality of service, pay the same wage levels and the same benefit levels, and at the same time hope to make a profit where you're answerable to your stockholders. It's almost as if you have to serve two masters. You have to serve the public, on one hand, and then you have to serve the stockholders who put together the company.

I just offer these thoughts for your consideration, not to challenge your right to seek business opportunities in government, because certainly I happen to believe there are some areas where public-private partnerships can be quite healthy, and I propose such in the area of the National Aeronautics Space Administration. But I also have some doubts about privatization in some areas of the government where you might hurt the case for privatization by taking it over.

Mr. PALATIELLO. Can I comment in response? Thank you.

First of all, I'm saying this not to be critical, but to clarify the issues. Privatization is a very broad term. I don't view this legislation as a privatization bill. Privatization encompasses a number of different strategies. This legislation, in my view, provides a framework for potentially contracting out services. I think that's an important distinction, and I'll explain why I think that's important in a moment.

We believe in the fact that, particularly in the industry that I represent, there is the need for a core capability within the government. There is a governmental mission. For example, the government has to administer the contracts. The government has to set the specifications. If you're doing a national mapping program and you don't set good standards and specifications, particularly in digital mapping today, you go out and you want to map each of the 50 States—you're going to have 50 different datasets, and you're not going to be able to do environmental analysis or other applications if you don't have a coordinated database that's set to government standards. So, those are two areas right off the top that I

think are very important inherently governmental functions within the field of mapping.

Third, I serve in local government myself, and I'll give you one example of something that we're struggling with. Fairfax County, VA has a wonderful public park system that we're very proud of. The county happens to mow the lawns in the parks themselves. They patch the potholes in the roads themselves. And there is a serious question being asked as to whether doing that with government employees is the most efficient way to do it—not only efficient in terms of what it costs per unit, but productivity. How many potholes can you fill in a week?

That leads me to my final point. In the experience that we've had, you'll recall that one of the members of my association testified when we had the joint hearing over on the Senate side, and he mentioned the number of former Federal employees that his own firm had employed. What we are finding among people who move from the government to the private sector is that the private sector is much more productive in mapping. They're getting a lot more out of their people and their equipment than these people were experiencing when they were working in the government. That's where a private company can provide the same, if not better, level of service; the same, if not better, wages, and to still do it efficiently and profitably, because of the increased productivity. The need to be profitable is what drives the productivity, particularly in small businesses, and particularly in businesses where the employees are the owners of the business. They are the stockholders. They benefit from the efficiency and productivity of their work.

Mr. KUCINICH. Yes, I'm sure that in some discrete areas a case could be made that there is productivity offered by the private sector. I'm also very certain, based on information that's been presented to this committee on another occasion, that there are areas where contracting out has been a disaster. HUD comes to mind.

So, I think that—I'd like to just conclude some—and thank you for engaging in this discussion because I think it is helpful to try to get an idea of how people view the world. The overall concern that I have about all privatization is that it inevitably reduces government to being just another unit of market participation, and that if we're going to maintain democratic values, I don't know that we can go to the marketplace to assure those democratic values are always going to be upheld. Because the marketplace is about seeking after profit, which is fine in and of itself, but it's not about upholding values or democratic traditions. Sometimes certain types of conduct can be anything but that, the marketplace. I think that's that dynamic tension that we are going to continue to see expressed in these great debates that take place over outsourcing, contracting out, privatization, whatever you want to call it.

The question is, can we have an accountable government? Can we have a maintenance of democratic values if, in fact, we are permitting broad areas of public service to be contracted out? What are the implications? We have to face this: that there are implications for the government. It's not just a financial issue. It is a financial issue. We always have to look at ways of making government work more efficiently, but there are also issues that relate to democratic control and accountability.

So I thank Mr. Sessions and Mr. Horn, and all the other committee members, for taking part in this discussion. This is where we started a few weeks ago when we finally came to an agreement. It would be good to have some give-and-take on this, and I appreciate you doing that. I appreciate Mr. Sawicky and Mr. Sclar and Mr. Engebretson being here as well.

Mr. PALATIELLO. Mr. Kucinich, may I make two comments? I actually agree with the statement you just made, and I think that's why this legislation is so important. I really appreciate all the effort that all the Members in the House and Senate have put into crafting it.

First of all, one of the difficulties that we've had—you said that there are instances where contracting out perhaps is advantageous and desirable, and others where it has not worked. Our experience is that the current policy and the current process of the Federal Government is not working in terms of making the determination of where contracting can work and where it cannot work.

I think the mapping community is a perfect example of that. We haven't been able to get agencies to do A–76 reviews of mapping to make a determination as to whether more of it can and should be done in the private sector or not. This legislation at least creates a framework to make those determinations.

The second point that I would make is that there are things that government should do, and there are things that only the government should and can do. But I honestly believe that we're at a point in the Federal Government today where the government is trying to do too many things, and trying to be all things to all people, and the consequence is government isn't being the right things to the people who generally need some assistance, and the government is not doing a lot of the things that it should be doing well. This legislation can help define the appropriate roles of government, so that we can start moving resources to those things that you and I believe the government should do.

Mr. KUCINICH. Just a question: Do you believe in privatization of Social Security?

Mr. PALATIELLO. Theoretically, yes.

Mr. KUCINICH. How about privatization of Medicare?

Mr. PALATIELLO. No. I think there are some States that are doing some good work with the management, but I think the provision of Medicare is an inherently governmental function.

Back to Social Security, I haven't been convinced that it can be privatized, but I think there is healthy debate going on as to whether or not——

Mr. KUCINICH. I think it's probably going on the last few days with the market dropping hundreds of points.

Mr. PALATIELLO. I can tell you my private IRA dropped a little bit over the last few days——

Mr. KUCINICH. I'm sure it did, and I have a great deal of sympathy for all my constituents who are similarly afflicted.

OK. Again, I think it's useful to have these discussions. I want to thank—I've had the chance to review the testimony of the gentlemen. Thank you. I will remain quite skeptical about efforts at privatization.

When I was mayor of Cleveland, I saw that privatization of computer contracts, prior to my administration, had cost the city of Cleveland over $10 million. People said, well, the city shouldn't be doing computers. Well, we went outside and the city got skinned. They had various types of outsourcing—if you want to call it that—which, unfortunately, turned out that it was done for less than altruistic purposes, shall we say. So, I always like to ascribe the best intentions to people who are looking to do business with government at all levels. I always like to do that. Sometimes I'm disappointed.

OK, thank you.

Mr. SESSIONS. Thank you, Mr. Kucinich. I think the dialog that we have heard today is one that is healthy. I think it's good for each one of us. I have engaged Mr. Kucinich several times in these philosophical debates. I will tell you that change is difficult. Change is hard for everybody.

On a philosophic basis, I will tell you that, while I believe Mr. Kucinich has talked about several things that he had on his mind, I have one on my mind, and it's probably a rambling dialog rather than a question, but it's an application of one that I had thought about many times. It's one that the military is in, militaries all around the world, in hundreds of countries around the world. They perform many manual functions—functions that wear out men, women, and machines, ones that cause a good number of fractures of bones and bodies.

In particular, working with the VA in the military, I became aware that they have trouble recruiting radiologists. Radiologists are among the highest paid physicians in the business, the medical community. They had trouble getting a good radiologist all around the globe, wherever military installations are. But because they were given the opportunity to manage their business properly, they have made a decision that they want to utilize distribution channels through FedEx, UPS, DHL—those types of overnight carriers. They now take pictures of fractures of bones and overnight express them to one or two locations in the United States. And they have a team of radiologists, and instead of having radiologists all around, multiplied in every installation, they can overnight express it somewhere, have a team of radiologists look at all these things, get two and three evaluations, render an immediate opinion to a surgeon, and perform a function.

I think this has to do a lot with what Dr. Sclar talked about when he talked about the central part of a mission, the frequency and highly specific assets. I think that it is philosophic, but I hope that what we have done in the compromise and attempting to craft this bill is to take into account what Mr. Kucinich talks about, but also to take into account that marvelous thing called change and wisdom; that a manager and workers of a business could see how change could evolve and make it better for everybody.

As I said, mine was more rambling dialog than philosophy, but it's another application of a way that I think relates directly to what we have had.

I will now defer to my colleague and my chairman, Mr. Horn, for such time as he may consume.

Mr. HORN. I thank the chairman, and I congratulate you on having this very good hearing. I'm sorry we had a few votes on the floor that disrupted your lives out there, and thank you for sticking with us.

One question I usually ask in these hearings is, is there anything any of your colleagues of the four of you said that you'd like to either disagree with, or support? And give you each a chance before you leave because I'd be interested in any new ideas that you've heard out of the three colleagues that are with each of you. I think we'll start at this end, because you're going to need throat spray for easing your brain connecting with the tongue. You were doing very well, and the ranking member would make an outstanding professor, as you can see. He put the students right to the wall. It's know as the Socratic dialog.

Mr. Sawicky.

Mr. SAWICKY. Sawicky, yes. Thank you. Well, one thing I need to respond to is what my friend at the other end of the table said, which is, he thinks government in the United States is trying to do everything for everybody. I'd like to remind people that, when compared to other industrial countries, the United States public sector, Federal, State, and local, taken together, are the smallest typically, maybe with one or two exceptions like Turkey or Japan. So, we begin in the United States with a lean public sector in terms size relative to the size of our economy.

At the Federal level, we begin with a public sector whose primary activity is really sending checks to people under social insurance, antipoverty programs, interest payments on our debts. The minority of our activity, you know, is actually providing services directly. We're giving payments to State and local governments, et cetera. So, the scope for reform in this area is very limited relative to the size of the Federal Government as a whole.

In that context, as I said in my testimony, there's ample opportunity to improve delivery services by moving things in either direction, either things that are public now that ought to be privately provided, or vice versa.

In terms of this amendment, I would emphasize that we try to get symmetry in this respect. We treat defense the same as nondefense; we treat things that are now public the same as things that are now private; we allow for movement in all directions, and most of what we get, beyond classification, to the actual evaluation and judgment of the efficacy of different approaches. Agencies and committees like this should—and do to some extent—continuously review what things cost under different possible methods of provisions.

In the State and local sector, although there's lots of talk about contracting, again, there's a great gap between that talk and the activity, which would tell you whether contracting or not contracting is the economic thing to do. I would just encourage the committee to focus on that, and it could turn out that we should do more mapping outsource and we should do other things by other means. I would stress that it's that evaluation which doesn't lend itself to basic principles by what's government and what isn't.

Mr. HORN. On that ploy, if I might interrupt, mapping rings bells in my head because I have the largest flood plain problem in the

country, in Los Angeles, with three rivers and 500,000 people of low income living in the flood plain—not rich people, low-income people, $20,000 a year, $30,000 a year, $35,000 a year. One city had the bright idea, let's not accept FEMA, the Federal Emergency Management Agency's maps. Let's go redo those. They did them in the normal way and they got hundreds of people out of the flood plain because the Federal maps were inaccurate. We brought to them the possibility of a New York firm where they would have satellite maps, and presumably they could come within 1 inch of accuracy, which is very important if you're going to be putting stilts on your house or jacking it up, or whatever crazy thing that happens in some other part of the country.

I think that sometimes it is that government either hasn't been given the funds by the legislative body, State or national, but they don't keep up on the latest technology in many of these things. That's certainly one place where you wouldn't want in-house people still drafting; you'd want people you could have available for a particular job, and that's certainly the ones with computerized architecture that we've had for the last 15 years where you can draw those plans. You're a professor of architecture. I'm sure you've seen a revolution in that. Well, you're in a school of architecture.

Mr. SCLAR. Yes, I hang around with those guys, yes. [Laughter.]

Mr. HORN. Yes, but you know what we're talking about. You hang around with them and you no longer have to sit there all day long doing a column. I mean, they can pop up like that now and you see the whole dimensions, three dimensions, all that.

Anyhow, you triggered a few thoughts that——

Mr. SAWICKY. Well, you triggered a thought, too. The capitalization of the public sector is referred to by your remark. The way we look at our budget is implicitly biased against capital or investment. We count a dollar that is going to be useful many years into the future, but it buys capital the same as the dollar that goes out the window tomorrow. So we have an artificial constraint on the ability of public agencies to tool up in the manner you're referring to, which puts them at an implicit disadvantage relative to private operators that can raise capital by various means. So again, it goes to the complexity of making fair comparisons between public and private. It usually doesn't reduce to a principle that you can use to categorize functions.

There's one exception, which is things that are inherently functions of a sovereign government, which has been eluded to: military, law enforcement, judiciary, legislative, prisons, corrections. There are things where the way things are done are so important, not the least because they can bring legal liability to taxpayers in the form of civil suits, that those argue much more forthrightly and a priori terms for being inherently governmental. Beyond that, I think there's very broad precepts and really a large task of all three branches of government to try to look at cases and judge them separately on their merits.

In the context of this legislation, one of the things that's bothersome is that there seems to be a blurring of boundaries between the legislature and executive. We seem to be opening doors for the Congress and the judiciary to be sitting next to people trying to make executive decisions, looking over their shoulders and other-

wise encumbering them. Sometimes they may need to be encumbered.

But my recommendation in that context is, I guess, more in the spirit of the reinventing government thing, which is to allow flexibility. But also to have consequences—good ones for good output, bad ones for bad output—that apply to the people making the decisions, the managers in the executive agencies, rather than trying to have bureaucrats watching bureaucrats.

Mr. HORN. I don't want to belabor this because I want to go down the line here.

Professor Sclar, what did you hear from some of your colleagues that you didn't particularly think much of, and what did you like about what you heard?

Mr. SCLAR. Well, actually, it was a very educational hearing because the breaks actually worked out well. I got to speak to my other colleagues on the panel whom I'd never met. And, too, you came with a different set of interests than I came to talk about.

I tell all of my graduate students to begin the answer to every question by saying, "It depends. . . ." Certainly, in the exchange that just took place, one of the things that's been clear to me, looking at public service now for a long number of years, is that there's a large gray area in which you can make a case, very often either way, for how things get done. What's more efficient? There's nothing automatically more efficient about the public or the private sector in getting certain things done. If we were in Scottsdale, AZ, our fire protection would be provided by a for-profit fire company. Other cities have tried this and they found that it doesn't work very well, and it hasn't gone very far. But certainly people in Scottsdale are satisfied with it.

This question of trash collection, it's one that certainly can go either way. The village I live in, we're very happy with our public collection. They come up in my driveway twice a week and empty the cans. I have no complaints with the way that works.

The region which I live in, we have a lot of problems with our private party collections. They seem to be called before committees all the time, in courts, for price-fixing, and organized crime. I don't know if that's a Northeast problem, but it's certainly one that happens.

So it's not—this question of, "if it depends," it's one you really have to look at. So what I'm concerned with is, how do we begin to get public organizations, public agencies, to be more innovative?

I worked for the VA. I was hired there once as the Chief of Economic Research and Health Plan. I was very impressed, and now I found out it was the lowest title they could come up with for me, but I stayed on. There were a lot of things that were very frustrating about public work and what I was able to do. But, it's very clear that public agencies have to find ways to be inventive, to provide incentives, to be responsive. There have to be upside and downside risks.

So, one of the things I was concerned about is this question of allowing outside parties to challenge these decisions. I understand from the discussion I had with my colleagues what the frustrations are that lead them to say they need this in the legislation. But my concern is not with the good guys who go with this in a modest

way. My concern is that, once you put something into place, how do you avoid the law of unintended consequences? My concern is, let's say something is put in—let's say the Pinkerton Co. doesn't like the notion—they could protect the President. Why do we need the Secret Service? They don't agree. The Treasury Department gives them a very rational answer, and we would probably all agree with the Treasury, but nowhere in the legislation then prohibits them from going to court and have this adjudicated. Nor does it prevent them to begin to lobby in Congress to try and change these things.

What I envisioned is another bureaucracy grows up in OMB that does nothing but oversee the way in which a decision is made to, one, protect against those things happening, to when those things happen, to be there to deal with them. Then the question of accountability moves down one level. So whereas the intention here is to make something more efficient, one of the fears I have, looking at this, is there's a law of unattended consequences, and how do you begin to preclude some of these very normal, human reactions that go on with this (a). And then (b), how do you begin to inject more organization into the public agencies? That was why, in my remarks, I talked about the need to bring—it's not just the question of unions bidding on the work. I don't really think it's not that unions shouldn't bid. I think it really is a question of employees and managers getting together and saying, we think we could do the job better; this is how we could do it.

It seems to me there are interesting things that could be done. In Indianapolis, where they didn't contract out their motor vehicle maintenance, one of the most shining examples, that you have a real reduction in cost, the employees of the Indianapolis Fleet Services, they receive a portion of what they save over what's budgeted for their department. They are also penalized when they don't turn vehicles around on time. They're docked for that. When I went out and interviewed them, I remember going to the body shop and there were four employees. They used to have, the ratio of a foreman, I think there was one foreman for every three or four employees before they started innovating themselves. We don't have the foreman, and we do about 25 percent of all the bodywork in Indianapolis. And my question to them was, why aren't you doing 100 percent? Their answer to me was, we figured out that it cost us $33 an hour, and we do it in-house. We can send this work out for $25 and we won't take the work back in-house until we get our costs better in line.

So it seems to me that what I fear in moving forward without thinking these things through is that we preclude the opportunity of bringing some innovation of flexibility into the public sector. Ironically, here's a case where, by bringing it in, you got more contracting out, whereas if these employees didn't have responsibility, they would have been fighting the contracting out of the bodywork. And now, here they were making the decisions. That's one of the concerns I would share with you, is my concern that this does not subject to this law of unintended consequences.

Mr. HORN. It's hard to protect anything we do from that law, by the way.

Mr. Engebretson.

Mr. ENGEBRETSON. Mr. Chairman, thank you. My remarks will be brief because John did a great job in explaining some of the problems that we have within our industries. Second, of course, his overview of what he thinks government should do and should not do, but there were some areas that were not covered, and there was a statement that I have a little concern of.

First of all, I think the amendment is going to do wonders. It will open up and study positions that have in the past not been studied. They will come, then, to be before the leadership, and they'll say, yes, this can be contracted out or no this cannot. This is the first time in my 11 years of CSA, and since the Eisenhower administration, that this specific thing is going to happen. I remember, during the Reagan era, they tried to get the agencies to do a 3 percent review every year, and that failed. Nothing happened; there was nothing there to push it. So I think this will be good.

The competition is going to be fantastic. This is where the savings will come in. As the Congressman from Ohio was pointing out, where do they really save the dollar? The competition is fierce in this industry. I know of companies that are operating on a 1 and 2 percent margin. That means it forces them to be very competitive. That means that they use the latest techniques to manage the projects and to manage people. They look for those things that they can save dollars and so they can do their work well. They do provide excellent services, and the government does have oversight, and they can force the companies to do the projects. That doesn't mean there isn't a bad apple in the barrel; there are some bad contractors; we know that. But the savings will be tremendous. We're looking at a 30 percent savings, as both of you commented earlier, and we will see that happen.

But here's the thing that bothers me. They say that our industry, when the people come from the public sector to work for the private sector, that we cut wages; we cut benefits; we don't provide benefits. This is an absolute false statement. We are under the Service Contract Act. We are under the Davis-Bacon Act. We are under the Fair Labor Standards Act. We are under the Walsh-Healy Act. All of them tell us what we must pay as the prevailing wage for our employees. We do have benefit packages that we are told that we must pay, and those requirements are there, and it's a part of the bidding process. So I do want that to go on the record that we must pay what the government tells us to pay. And the government and the contractors, as they put these proposals together—whether it's the most efficient organization or the company themselves—many dollars are spent in putting these together to try to get that savings for our taxpayers. And we will, and I think that this can work. And we thank you, again, for the opportunity to be here today.

Mr. HORN. Well, we thank all three of you, and we'll end with the last person whose got quite a record here on philosophy. I enjoyed it. You came up with a lot of answers that I, as a former professor, wouldn't think of, and you're right. You did well.

Mr. PALATIELLO. Well, thank you, Mr. Chairman. I'm sorry that Mr. Kucinich left because I wanted to tell him that I enjoyed it as well.

Three very quick comments. The question you asked was if there was anything that we heard that we'd like to agree with.

Mr. HORN. Or disagree with.

Mr. PALATIELLO. Well, I don't mean to be gratuitous, but I agree with your statement that you just made about mapping. I'll start with that. [Laughter.]

The second point I would make is to underscore what my friend, Mr. Engebretson, has said that—one thing that he admitted—it is in the regulations under the Service Contract Act that the Labor Department, when determining that prevailing wage, must consider what would be paid to government employees if the activity was performed in-house. That's in the regulations.

Mr. HORN. In the Walsh-Healy or Service?

Mr. PALATIELLO. Service Contract.

Mr. HORN. What's the difference between Walsh-Healy and Service Contract?

Mr. PALATIELLO. Walsh-Healy is for government acquisition of manufactured products and goods. Service Contract Act covers service contracts. Davis-Bacon covers construction contracts.

Mr. HORN. And Walsh-Healy doesn't cover services at all.

Mr. PALATIELLO. No. Three separate laws.

Mr. HORN. I hadn't thought of it in 30 years. I was Assistant to the Secretary of Labor under Eisenhower, and I knew Davis-Bacon very well, and we have that up here, of course, those arguments, all the time. But I just hadn't heard anybody even mention Walsh-Healy; that it's still on the books?

Mr. PALATIELLO. Yes, sir.

Mr. HORN. Learn something every day.

Mr. PALATIELLO. The third, very quick, and final comment that I would make is I really do tend to agree with Mr. Sclar and Mr. Sawicky on one point. I think, again, this is a very important distinction to make, and that is they're at a disadvantage, and Dr. Sclar and I spoke during the break. I have been involved in working with the Congress on this legislation for quite some period of time. And when you look at this particular proposal, Mr. Sessions' amendment, in a vacuum, you have one entirely different perspective as opposed to looking at it chronologically in terms of where we've been with this legislation.

The legislation that Senator Thomas and Congressman Duncan had in past Congresses was much more philosophical and ideological. It basically said, if it's commercial, it gets contracted. Well, we've had negotiations and deliberations that you all have engaged in on this legislation. We've come to the point where we are today, where it says we're going to inventory of activities and then go through a methodology to determine what's best for the taxpayer in terms of who delivers the service or who provides the product.

So, this legislation is not a Draconian, knee-jerk, all-or-nothing-at-all proposition. It is a much more methodological—methodical—way of making a determination as to whether something should be contracted or not. This doesn't say all contracts are good, and all government employees are bad. This legislation says, let's take a look and see how we can get the best bang for the buck for the taxpayer. Let's determine where contracting is appropriate, and let's determine where contracting is not appropriate.

So I think when you understand the progression of the legislation and the development of this legislation, you might look at it

in a little different context. Dr. Sclar, in particular, as we chatted, is at a little bit of a disadvantage because he wasn't aware of that legislative history too well.

Mr. HORN. Well, on that optimistic note, I'll pass it back to the presiding officer. If he wishes to adjourn the meeting, none of us are going to cry about it. [Laughter.]

We've enjoyed it.

Mr. SESSIONS. Yes, sir. Thank you, Mr. Chairman. I want to thank each of the panelists who have been here before us today. I agreed to hold this hearing in the spirit of trying to make sure we provided one more hearing. I think we've had three on this subject. But I felt like it was important for us to tee up a little bit higher those expectations to hear from people about the opportunities that will be before us. I want you to know that I believe that not only Mr. Horn and myself, but Mr. Kucinich, have engaged ourselves, and thrown ourselves at this issue. I have great respect for each of you who have taken time to be with us today.

As always, we have a team of people who have made this hearing successful. There are people who have contacted you and worked with you on your delivery today, and I would like to thank a few of those people. J. Russell George, who is staff director and chief counsel for Government Management, Information, and Technology; my adult supervision today, Mark Brasher, who is the senior policy director; Matthew Ebert, who is a clerk; Mason Alinger; Frank Cruz—now watch this one—Mark Urciuolo—there you go—Solomon Bartel, those three were interns; Julie Moses, who is with Mr. Kucinich's staff; Faith Weiss and Earley Green, who is also with the minority staff, and Anne Paine West, who is the court reporter.

On behalf of each one of us, I want to thank you for being here today. This concludes our hearing.

[Whereupon, at 5:05 p.m., the subcommittee proceeded to other business.]

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