

AN UPDATE ON THE BUSH ADMINISTRATION'S
COMPETITIVE SOURCING INITIATIVE

TESTIMONY BEFORE THE U.S. SENATE SUBCOMMITTEE ON OVERSIGHT OF
GOVERNMENT MANAGEMENT, THE FEDERAL WORKFORCE AND THE DISTRICT
OF COLUMBIA

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Thank you for inviting me to testify today regarding the Bush Administration's competitive sourcing initiative, which promises to subject at least 50 percent of the Federal Activities Inventory Reform Act (FAIR Act) not-inherently governmental jobs to competition by some as-yet-to-be-determined date. As you know, the Office of Management and Budget has given some ground on the competition quotas—the 50 percent goal is still a bit fuzzy, but is embedded in the criteria governing the red-to-green ratings in the president's management agenda.

As I have argued before, the competitive sourcing initiative is part of a long-standing effort to keep the total headcount of government as low as possible, whether through hiring freezes, personnel ceilings, or outsourcing initiatives. This is certainly the history of the FAIR Act, which is driving the current sourcing initiative.

Congress and the president have long understood that the federal government could not fulfill its mission without outside help. From the very beginning of the space and nuclear programs, for example, government has relied on contractors and consultants to conduct the essential research *and* manage the programs.

Where Does Government End?

To this day, no one has made a more determined effort at establishing a bright line between public and private than David Bell, the Kennedy Administration's first Budget Director. Acting at the president's request, Bell led a senior task force composed of NASA Administrator James Webb, White House Science Adviser Jerome Weisner, Defense Secretary Robert McNamara, and the chairmen of the Atomic Energy Commission, the Civil Service Commission, and the National Science Foundation. The Bell report began with a sweeping assessment of what it called government's "increasing reliance" on private contractors to do the research and development work of government.

Those contractors were hardly selfless giants, the report argued. Rather, they had come to depend for their existence and growth "not on the open competitive market of traditional economic theory, but on sales only to the United States Government. And, moreover, companies in these industries have the strongest incentives to seek contracts for research and development work, which will give them both the know-how and the preferred position to seek later follow-on production contracts." Because the profit incentive would lead contractors to expand their markets even to the detriment of agency capacity, the Bell Task Force set two criteria for casting the choice to contract out: (1) Getting the job done effectively and efficiently, with due regard to the long-term strength of the Nation's scientific and technical resources, and (2) Avoiding assignments of work, which would create inherent conflicts of interest.

The Bell Task Force argued that it is "axiomatic that policy decisions respecting the Government's research and development programs—decisions concerning the types of work to be undertaken, by whom, and at what cost—must be made by full-time Government officials

clearly responsible to the President and to the Congress. There are primary functions of management which cannot be transferred to any contractor if we are to have proper accountability for the performance of public functions and for the use of public funds.”

The task force clearly understood that the distinction was easier stated than applied, however. To maintain in-house control, government would need enough technical capacity in-house to know when and if contractors were doing the job. It would also need to be “particularly sensitive to the cumulative effects of contracting out Government work. A series of actions to contract out important activities, each wholly justified when considered on its own merits, may when taken together, begin to erode the Government's ability to manage its research and development programs.” In short, government could push so much of its work down and out that it would eventually atrophy as a source of control. NASA needs to know how to build satellites, not just acquire them; EPA needs to know how to build waste water treatment plants, not just grant them; the Department of Energy needs to know how to run a nuclear reactor, not just oversee a contractor that knows.

The task force clearly believed that there were times when contracting out was perfectly appropriate and times when it weakened the government’s core capacity to perform its mission. Although the Bell Task Force expressed support for both goals, it reserved its strongest concern for protecting government from the private sector, not vice versa. As the final report warned, “the Government’s ability to perform essential management functions has diminished because of an increasing dependence on contractors to determine policies of a technical nature and to exercise the type of management functions which Government itself should perform,” that a new generation of nonprofit contractors “are intruding on traditional functions performed by competitive industry,” that “universities are undertaking research and development programs of a nature and size which may interfere with their traditional educational functions,” and that government itself was “relying so heavily on contractors to perform research and development work as simply a device for circumventing civil service rules and regulations.”

Most important, the task force warned that the growing contract workforce was eroding the distinction between public and private. Its warning is well worth reading in its whole: “A number of profound questions affecting the structure of our society are raised by our inability to apply the classical distinctions between what is public and what is private. For example, should a corporation created to provide services to Government and receiving 100 percent of its financial support from Government be considered a ‘public’ or a ‘private’ agency? In what sense is a business corporation doing nearly 100 percent of its business with the Government engaged in ‘free enterprise?’

Paying attention to such issues would require a far broader instrument than Budget Circular A-76, of course. But the point is well taken: competitive sourcing should ask not just how to protect the private sector from government, but how to protect civil society from the private sector. According to my estimates, roughly 40 percent of all U.S. households contain at least one wage-earner who works for the federal, state, or local government, or for a contractor or grantee.

Defining Terms

The Bell Task Force clearly struggled to find useful applications of what have become two of the most confusing phrases in government: “commercial activities” and “inherently governmental functions.” On the surface, each term makes sense. It is in the application that confusion appears to reign.

Commercial Activities

Start with commercial activities, arguably the simpler of the two terms at issue. The Office of Management and Budget’s Circular No. A-76, which governs commercial activities, could not provide a clearer definition: “A commercial activity is the process resulting in a product of service that is or could be obtained from a private sector source.” It is a definition that has remained similar to the one used in 1955 when the Eisenhower Administration prohibited federal departments and agencies from starting or carrying on “any commercial activity to provide a service or product for its own use if such a product or service can be procured from private enterprise through ordinary business channels.”

Almost three decades later, the Reagan Administration restated the principle in a 1983 revision: “In the process of governing, the Government should not compete with its citizens. The competitive enterprise system, characterized by individual freedom and initiative, is the primary source of national economic strength. In recognition of this principle, it has been and continues to be the general policy of the government to rely on commercial sources to supply the products and services the Government needs.” Thirteen years later still, the Clinton Administration restated the principle once again, releasing an *A-76 Revised Supplemental Handbook* with a rather different rationale:

Americans want to “get their money’s worth” and want a Government that is more businesslike and better managed....Circular A-76 is not designed to simply contract out. Rather, it is designed to: (1) balance the interests of the parties to make or buy cost comparison, (2) provide a level playing field between public and private competitors, and (3) encourage competition and choice in the management and performance of commercial activities. It is designed “to empower Federal managers to make sound and justifiable business decisions.”

In contrast to the Eisenhower and Reagan Administrations, the Clinton Administration viewed the A-76 process less as a device for protecting the private sector from government and much more as a tool for stimulating greater efficiency inside government.

Even if the overall purpose of the cost comparisons between government and private delivery was clear, the actual process for testing the respective strength of the two sectors is both cumbersome and confusing. The federal government is allowed to engage in commercial activities for an assortment of reasons, some that are objective—including national defense or intelligence security, patient care, temporary emergencies, and functions for which there is no commercial source available or involving 10 or fewer employees—and some that are entirely

subjective, including the need to maintain core capability, engage in research and development, or meet or exceed a recognized industry performance or cost standard.

There are two broad exemptions from the A-76 requirements. The first involves inherently governmental activities, which are exempt from A-76 entirely. The second involves a lower government cost, which can only be proven through a three-step cost comparison study: (1) development of a work statement for a specific commercial activity, (2) completion of a management study of the organization, staffing, and operation of what would be the government's most efficient organization (MEO) for producing the good or service, and (3) a request for bids from private sources to assess the relative cost of private sector versus MEO delivery. A private source can only win the competition with a bid that is at least 10 percent lower than the MEO price. Even if government wins the competition by meeting or beating the private bid, however, it must still build the MEO, meaning that taxpayers should benefit regardless of the outcome.

Taxpayers cannot benefit, of course, unless the A-76 studies occur. Whether because departments and agencies are somehow convinced that they have become MEOs through a decade of downsizing, or because they either do not have the staff resources to conduct the studies or believe everything they do is inherently governmental, the number of A-76 studies has declined dramatically since the mid-1980s. According to the General Accounting Office, there were exactly zero non-Defense positions studied in 1997, and at least three departments, Education, Housing and Urban Development, and Justice, had not studied a single position since 1988.

There are two patterns worth noting here. First, administrations vary significantly in their general commitment to A-76. The federal government studied an average of over 16,000 positions a year under Reagan (1983-1988), 5,200 per year under Bush (1989-1992), and 7,000 under Clinton (1993-1997). Second, the Department of Defense is by far the most experienced at competition—remove Defense from the A-76 totals, and activity tumbles from 4,100 non-Defense positions a year under Reagan to less than 1,500 under Bush, and exactly 84 under Clinton.

In this regard, it is useful to note that even experts such as DoD can make big mistakes, as witnessed in the recent Defense Finance and Accounting Service competition involving 650 jobs in Cleveland and Denver. Anyone can fall into this trap, of course, but this one shows the potential weaknesses as the Bush Administration puts greater pressure on agencies that have not done A-76 competitions in years, even decades.

The point here is not to endorse greater A-76 activity. To the contrary, it is to suggest the limited utility of using A-76 as the primary sorting device for managing federal headcount. Even with the fullest presidential commitment possible in the mid-1980s, A-76 covered barely two percent of the full-time permanent civil service. The definition of commercial activity may be clear in the abstract, but the utility of the term as a method for shifting jobs from government to the shadow and back is limited at best. Without assaying the value of A-76 as a disciplining tool,

it seems reasonable to argue that it can never be more than a minor lever in allocating headcount constraints more systematically.

Inherently Governmental Functions

As noted above, departments and agencies can exempt themselves from A-76 by declaring a given commercial activity an inherently governmental function. Like commercial activities, the term seems easy to define. According to the Office of Federal Procurement Policy (OFPP), which was created in 1974 to strengthen federal oversight of an increasingly complicated procurement system, the term encompasses “a function that is so intimately related to the public interest as to mandate performance by Government employees.” That includes activities that “require either the exercise of discretion” or “the casting of value judgments in casting decisions for the Government.”

Defined formally in 1992, an inherently governmental function is nothing less than the faithful execution of the laws, which OFPP defines as any action to: “(a) bind the United States to take or not take some action by contract, policy, regulation, authorization, order, or otherwise; (b) determine, protect, and advance its economic, political, territorial, property, or other interests by military or diplomatic action, civil or criminal judicial proceedings, contract management, or otherwise; (c) significantly affect the life, liberty, or property of private persons; (d) commission, appoint, direct, or control offices of employees of the United States; or (e) exert ultimate control over the acquisition, use, or disposition of the property, real or personal, tangible or intangible, of the United States, including the collection, control, or disbursement of appropriated and other Federal funds.”

Much as one can admire OFPP’s effort to define a bright line, its policy letter mixed in just enough exemption to leave the reader wondering whether such a bright line could ever exist. “While inherently governmental functions necessarily involve the exercise of substantial discretion,” OFPP stated on page three of its letter, “not every exercise of discretion is evidence that such a function is involved. Rather, the use of discretion must have the effect of committing the Federal Government to a course of action when two or more alternative courses of action exist.”

“Determining whether a function is an inherently governmental function often is difficult and depends upon an analysis of the factors of the case,” OFPP continued on page 4. “Such analysis involves consideration of a number of actors, and the presence or absence of any one is not in itself determinative of the issue. Nor will the same emphasis necessarily be placed on any factor at different times, due to the changing nature of the Government’s requirements.” As if to acknowledge its own difficulties finding the bright line, OFPP added two appendices giving examples of activities likely to be declared inherently or not inherently governmental functions.

There are two problems with the list. First, as noted above, the policy letter was heavily caveated with “could be” and “might be” legalese. Try as it might to define terms and set boundaries, OFPP left plenty of room for reinterpretation, not the least of which was its statement that “This policy letter is not intended to provide a constitutional or statutory

interpretation of any kind, and should not be construed, to create any right or benefit, substantive or procedural, enforceable at law by a party against the United States, its agencies, its officers, or any person.” As such, the letter could not be used to create a basis on which to challenge an agency action. Notwithstanding the value of such boilerplate, agencies could rightly conclude that practically anything goes.

Second, the policy letter left the final interpretation to agencies alone. Although OFPP did reserve the right to review a particular decision, agencies had to follow their own interpretation. If the Department of Energy decided that having contractors write congressional testimony for the secretary was not an inherently governmental function, which it did in the early 1990s, so be it. “The extent of reliance on service contractors is not by itself a cause of concern,” the OFPP letter writers argued. “Agencies must, however, have a sufficient number of trained and experienced staff to manage Government programs properly. The greater the degree of reliance on contractors the greater the need for oversight by agencies. What number of Government officials is needed to oversee a particular contract is a management decision to be made after analysis of a number of factors.”

The Definitional Intersection

Despite the relative difficulties in defining commercial activities and inherently governmental functions separately, the two terms interact to form separate zones for pure privatization, contracts, grants, and mandates, and full government involvement. Presumably, government should never privatize a non-commercial activity that is an inherently governmental function, and should never retain a commercial activity that is not an inherently governmental function. It is not enough to examine the two terms separately. One must ask whether an activity is commercial and inherently governmental simultaneously.

The definitional tangle comes from the fact that the answer is rarely definitive. Doing laundry for the Navy can be a purely commercial activity in home ports such as Norfolk, Virginia, but can be an inherently governmental function in the Persian Gulf. Testing ordinance equipment can be a commercial activity in testing ammunition for an M-16 rifle, but an inherently governmental function when calibrating a laser for a missile defense system. Building a communications satellite or rocket motor can be an entirely commercial activity unless building that satellite or rocket motor is top secret or essential to government’s ability to oversee contracts for the commercial activity.

Where one sets the boundaries for each zone depends on more than just context, however. It also involves politics. Witness the decision to allow government agencies to bid against private firms to perform commercial activities for other government agencies. The Reagan Administration almost certainly would not have allowed the Agriculture Department’s National Information Technology Center in Kansas City to best IBM and Computer Sciences Corporation in a competition to build a \$250 million Federal Aviation Administration data center, as was done in 1997. Nor would it have allowed the Treasury Department to create a Center for Applied Financial Management that would compete with private firms in providing \$11 million in administrative support to other government agencies in 1997, or the Interior Department’s

Administrative Support Center in Denver to win a contract from the Social Security Administration to provide payroll services in 1998. Not only did the Clinton Administration allow all three departments to bid and win, it openly encouraged government to take on the private sector through the creation of “franchise funds” that allow departments and agencies to carry over earnings from year to year. Congress approved a five-year experiment with the franchise funds as part of the Government Performance and Results Act of 1993.

A Brief History of FAIR

Passage of the Federal Activities Inventory Reform Act (FAIR) in 1998 provided a tool for measuring at least one dimension of the federal workforce—that is, the degree to which it engages in inherently governmental activities. The final bill was a fair distance from the original proposal, which was titled “The Freedom from Government Competition Act.” That bill, which was authored by Senator Craig Thomas (R-WY), began with a sweeping indictment of the traditional sorting process: (1) “government competition with the private sector of the economy is at an unacceptably high level, both in scope and in dollar volume” and (2) “current laws and policies have failed to address adequately the problem of government competition.”

In its initial form, the act would have prohibited agencies from beginning or carrying out “any activity to provide any products or services that can be provided by the private sector,” or from obtaining any goods or services from any other governmental entity, meaning the franchise funds described above. It also would have created an Office of Management and Budget (OMB) entity called the Center for Commercial Activities to promote maximum conversion of government activities to private sector sources.

Facing intense opposition, sponsors eventually accepted the much more modest proposal embedded in FAIR. Under the final proposal, which basically codified the A-76 process, federal departments and agencies are required to identify and publish comprehensive lists of all activities deemed not inherently governmental. Once published, every activity on the list is theoretically subject to competition at the department or agency head’s discretion. Despite its earlier criticism of the A-76 sorting process, the Freedom from Government Competition Act accepted the Office of Federal Procurement Policy’s definition of inherently governmental functions word for word as a complete exemption from conversion, as did FAIR as a complete protection against listing.

What distinguished FAIR from A-76 was the annual listing requirement and an entirely new appeal process. Under the act, an interested party can challenge the omission of an activity from the list within 30 days of its publication, to which the agency must respond within 28 days, to which the interested party may appeal within ten days, to which the agency must respond a final time within ten days. However, just because an activity reaches the list of not inherently governmental functions does not mean it will never be subject to competition. Again, it is up to the agency head to decide what stays or goes. Because there is no judicial review under the act, all agency decisions are final. (At least one earlier version of FAIR had provided for judicial review by the United States Court of Federal Claims to render judgment on omissions from the inventories.)

Obviously, supporters of the bill envisioned a much larger zone for private delivery of public services. Noting that the bill was supported by the Clinton Administration and over 1,000 organizations, John Duncan, Jr., (R-TN), heralded FAIR as a way to get federal agencies “out of private industry and stick to performing those functions that only government can do well. At the same time it will allow our great private enterprise system to do those things it does best, providing commercial goods and services in a competitive environment.” Pete Sessions (R-TX) put it more succinctly by cribbing from the original version of A-76: “The government should not be in the business of competition with private business.”

Interestingly, as Stephen Horn (R-CA) noted in chairing subcommittee hearings on FAIR, the debate was “eerily familiar” to the controversy surrounding passage of H.R. 9835 in 1954. That bill, which passed the House only to die in the end-of-session rush in the Senate, provoked intense opposition, too, raising the ire of a junior member named Thomas P. O’Neill, Jr., who pleaded on behalf of a Navy rope plant in Massachusetts. “Others discussed the Federal operations making coffee roasters, dentures, sleeping bags, and even iron and steel plants. Most of these operations are now defunct, and we have contracted with private vendors to make dentures, and the coffee to stain them, with specialized firms that have those functions as their core missions.”

Why Outsource?

Given the definitional discretion embedded in the current sorting systems, it should come as no surprise that some contracting is for the right reasons and other contracting is driven by less-noble instincts. A department that wishes to insulate a particular activity from A-76 can do so, if not with complete impunity, at least with significant delaying power; an agency that wishes to push an inherently governmental function out to a contractor can also do so, arguably with even greater impunity.

But whether the decision is to protect or push, headcount constraints assure that the decisions have unintended consequences both within each department or agency and across the rest of government. The decision to protect a unit in Commerce may force contracting out at HUD, the decision to mandate out in Health and Human Services may create capacity for civil service expansion in Justice. Even if OMB never puts the decisions together in any kind of systematic analysis, headcount constraints eventually reshape government. Whether the result is a sculpting or demolition, depends largely on whether the shadows of government are used to hide weakness or build strength.

Poor Excuses

There are clearly times when contracting out is used not as a source of strength, but as a way to get a job done in the face of apparent incompetence. Although this contracting out may make perfect sense in the short-run, it eventually weakens government by excusing systemic problems or outright negligence.

1. Evading Headcounts.

The first excuse for contracting out is to evade headcount pressures. Given a choice between inflicting pain and contracting out, the federal government will almost always contract out.

This is not to suggest that government backfills downsized positions through some deliberate process. Bluntly put, most departments and agencies do not have the workforce planning systems to engage in such deliberate shell games. Although downsized employees occasionally do return to their agencies as contract workers, as National Institutes of Health radiologists did in the late 1980s, most agencies simply cannot play such games. To do so would mean linking an agency's human resource office, which is responsible for downsizing, with its acquisition office, which is responsible for contracting. The two barely talk to each other, let alone acknowledge the potential benefits of working together. The fact is that the federal government simply does not have a workforce planning system to shift jobs deliberately.

2. Evading Bureaucracy.

Departments and agencies also use contracts, grants, and mandates to evade the antiquated administrative systems that plague the federal government, a case that was effectively articulated by the first of Vice President Al Gore's reinventing reports.

Vice President Gore was hardly the first to make the case against over-control, however. Program managers have felt besieged by internal red tape for decades. The National Academy of Public Administration (NAPA) weighed in with its own call for reinventing government a full decade before Gore put pen to paper: "What is bitterly ironic is the fact that Federal managers, both political and career, typically regard themselves as captives of a series of cumbersome internal management 'systems' which they do not control." Describing the systems as "so rigid, stultifying, and burdened with red tape" that they undermine government's capacity to serve the public on "a responsive and low-cost basis," NAPA offered an all-too-familiar complaint:

"Many of the restraints and regulatory requirements which now make it so difficult for Federal managers to function have their origin in commendable efforts to prevent or control waste, abuse of authority, or corruption....Unfortunately, the cumulative impact of an ever increasing number of procedures, findings, appeals, and notifications is to jeopardize the effective execution of [government]. Moreover, regulatory requirements, once adopted, tend to be retained long after they have ceased to make any constructive contribution to program management." To reinforce its point, NAPA put a drawing of Gulliver bound by the Lilliputians on the cover.

What neither NAPA nor Gore ever wrote about is the role of such constraints in driving managers to create shadows. Much as federal managers might complain publicly about the contracting out of high impact jobs, many attest privately that they have greater control over the

work done as a result. There is no need to go through endless appeals to fire poorly performing employees nor any need to wait to add new staff.

Over time, the convenience of contracting can lead even the most dutiful federal manager to take the easy route. The federal manager can pay prevailing wages for high demand positions, while giving their contract employees the breathing room to do their jobs unencumbered by pesky overseers and what they see as needless paperwork. Herbert Hoover promised a government that works better and costs less in 1949, as did Johnson, Nixon, Carter (a government as good as the people, too), Reagan, and Clinton/Gore. Although the Gore effort appears to have penetrated more deeply than its predecessors, shadow casting may be the only way to make the numbers add up to performance.

3. Evading Poor Performance.

Contracts, grants, and mandates can also be used to hide poor performance within government's own workforce. When departments and agencies want the job done right, they sometimes look outside.

There are two ways to prevent what might be called "defensive" outsourcing. The first is to provide the pay and training to make the government workforce evenly effective. The second way is to hold government accountable for results, not compliance. Unfortunately, even the effort to shift accountability from rules to results can involve a plethora of rules.

4. Evading Blame.

Outsourcing clearly weakens government when it is used to avoid blame. There are times, although rare, when having a contractor in charge of a dangerous or risky program is the most comfortable position for government politically. In 1985, for example, just a year or so before the Shuttle Challenger tragedy, NASA asked NAPA to examine the feasibility of privatizing the entire program. From a perfectly appropriate perspective, the privatization study was merely good business planning. NASA was clearly concerned about the long-term burdens of running what it hoped would soon become a relatively routine cargo program. From a much more troublesome perspective, senior NASA officials also expressed worries about the potential for another "204 incident," a term used to identify the fire that took the lives of three Apollo astronauts in 1967. Privatizing the shuttle would give the agency some protection in the event of another catastrophe by shifting blame to the contractor.

The Challenger investigation obviously proved otherwise. Although the contractor, Morton Thiokol, was harshly criticized for suppressing internal objections to the launch of Flight 51-L, NASA's decision casting process was clearly identified as the contributing cause of the accident. NASA's middle-level contract managers not only knew that the O-rings used to seal the solid rocket motor joints would be compromised at low temperatures, they made no effort to relay the intensely-felt Thiokol worries upward on the night before launch. To the contrary, NASA contractor managers clearly pressured Thiokol to reverse what had been its original recommendation not to launch until temperatures went up. "My God, Thiokol," one NASA

manager asked, “when do you want me to launch, next April?” It was as if, one Thiokol engineer later testified, the contractor had to prove beyond a shadow of a doubt that it was unsafe to fly instead of proving just the opposite.

As the presidential commission appointed to investigate the accident concluded, “The decision to launch the Challenger was flawed. Those who made that decision were unaware of the recent history of problems concerning the O-rings and the joints and were unaware of the initial written recommendation of the contractor advising against the launch at temperatures below 53 degrees Fahrenheit and the continuing opposition of the engineers at Thiokol after the management reversed its position....If the decisionmakers had known all of the facts, it is highly unlikely that they would have decided to launch 51-L on January 28, 1968.”

5. Meeting Quotas.

I can think of few more destructive reasons for outsourcing than meeting arbitrary quotas of one kind or another. Such quotas send the signal that outsourcing is nothing more than a “body count” exercise, in which agencies are encouraged to push as much out the door as possible with little or no planning. Without top-to-bottom review, the outsourcing merely replaces one set of bureaucracy with another, and disconnects the workforce planning process embedded in the Government Performance and Results Act with a manic contest to see which jobs can be moved out the fastest. The result can only be a perpetuation of middle- and top-heavy government—if only because it is the middle and top of government that makes the decisions on meeting the quotas.

Good Reasons

If there is one word to separate the outsourcing that hides weakness from outsourcing that builds strength, it is “deliberative.” Outsourcing that builds strength involves hard choices about where government begins and ends, who should do what work, and how to deliver the goods in time. “It’s time to lower the level of rhetoric of outsourcing and contracting out,” former OFPP administrator Steven Kelman remarked in 1998 as Congress began debating a stack of bills requiring agencies to hold public/private competitions for any activities not deemed inherently governmental functions. “It’s not a question of big government/small government, nor is it a question of do you or don’t you like the federal workforce. It is a good management principle to stick to your core competency.”

1. Acquiring Skills.

This is arguably the best reason for outsourcing. Simply stated, the federal government must be able to acquire skills that it cannot develop or maintain on its own civil service workforce. Having chosen to run the nation’s nuclear weapons plants with contractors, for example, the Department of Energy never developed an internal capacity to clean up nuclear waste. Thus, when it came time to start closing the facilities at Savannah River, Fernald, or Rocky Flats, the department had little choice but to acquire clean-up specialists from the private sector.

The question is why outsourcing under such circumstances is any more acceptable than using a contract to evade pay limits on positions already within the civil service. The answer lies in the inability to build the internal capacity at a reasonable cost. If the federal government is not paying enough to recruit the auditors, computer programmers, and program analysts to deliver public goods effectively, Congress and the president should raise the rates or create a special pay system such as the one used by the Federal Reserve Board. But if it has never had the capacity to begin with or allowed the capacity to slowly leak away through headcounts, the federal government may eventually have no choice but to use a shadow workforce to get the job done. Thus, does the inappropriate use of contracts to evade pay ceilings eventually force the appropriate use of contracts to buy back the institutional memory (if it ever existed) from the private firms that now own it.

In a similar vein, the federal government has reasonable cause to use contracts to address crises such as the Y2K computer glitch, particularly when the need is clearly limited to the crisis. As noted earlier, it makes no sense to rebuild the federal government's COBOL competencies for a one-time event. Such one-time events hardly need be restricted to a year or two. At NASA in the 1960s, for example, the Apollo program created a surge in contractor involvement that peaked five years into the program, falling back as the program reached its goal in 1969.

2. Acquiring Flexibility.

Outsourcing also allows agencies to acquire needed flexibility to manage uneven work flows. NASA remains the premier example. Its workforce, both civil service and contract-created, was designed to rise and fall with mission demands from the very beginning. Although there were clearly places where the Whitten Amendment forced the agency to contract out activities that it would have preferred to create and maintain in-house, NASA's success depended on acquiring expertise already available on the outside. The surge-tank model also happened to fit NASA's political circumstances.

Despite President Kennedy's embrace, it is not clear that NASA's mission was broad enough to assure public support for a massive new bureaucracy. Even with its limited civil service workforce, NASA faced more than its share of controversy as America launched a war on poverty in the midst of a war in Vietnam. As the pressures to do more with less increased as both wars heated up, NASA pushed more and more of its work into the shadow, prompting calls for a rebalancing of in-house and out-of-house capacity. Nevertheless, as NASA historian Arnold Levine writes, "The case for service contracts rested on one powerful argument that was never adequately refuted: An agency with such urgent and unique assignments could have done the job with its in-house staff alone....Faced with ambiguous guidelines, NASA officials believed that resorting to the private sector was inevitable and that the question of whether a task was covered in-house or by contract was less important than the knowledge that the capability would be there when needed."

More recently, many federal agencies have been using contracts and temporary appointments to create what some have called a blended workforce composed of permanent civil servants, more or less permanent contractor employees, and outside consultants and easily

severable part-timers and temporaries, all theoretically working side-by-side toward the public good. The only difference is that the permanent employees will stay at the end of the surge, while the temporaries will go. At the Department of Energy, for example, temporaries are carrying an enormous burden in the clean-up of aging nuclear weapons plants.

Although blending most certainly reflects headcount pressure, making a virtue out of stark reality, it also addresses the difficulties the federal government faces in recruiting young Americans to public service. The old notion of spending a lifetime in the civil service is just that, old. Young Americans expect to change jobs much more frequently than their parents and are much more reluctant to make work the centerpiece of their lives.

3. Acquiring Savings.

The final reason for outsourcing, or at least competing, federal jobs is to save money. Let me start by noting that there is absolutely nothing wrong with saving money on tasks that are not inherently governmental, the problem again being how to define the term with enough precision. Democrats and Republicans have long agreed that government should never pay more than it has to in purchasing any good or service. It should be a “smart buyer” at all times, demanding the highest value for the money.

They have also long agreed that government should protect the private sector whenever possible. As noted above, the challenge is not to issue bright lines such as A-76, but to make them meaningful to the sorting of responsibilities. Although Democrats and Republicans alike believe in the efficiency-producing effects of competition, the question is how best to protect the private and public sectors from each other. Much as the Reagan Administration pushed government to conduct A-76 cost comparisons, even to the point of issuing a 1987 executive order requiring individual agencies to review at least 3 percent of all agency jobs annually until all commercial activities had been exposed, there is little evidence that the effort produced more than frustration.

There is at least some reason to believe that competition has a salutary impact on the price of goods and services. According to RAND, a Santa Monica-based think tank, Defense Department job-outsourcing competitions have saved from 30 to 60 percent regardless of whether government or the private sector wins. The source of the savings is almost always a net reduction in the number of people needed to do the job. The study shows that neither government nor private firms enjoy a particular advantage in reducing personnel costs—they both do it the same way, by using fewer people and pushing resources downward. The question, of course, is whether A-76 or competitive sourcing is the most efficient way to get these results. Why not ask agencies to reduce personnel costs through a more deliberate method?

The Problem of Price

As this discussion suggests, there are many more reasons for in-sourcing or outsourcing than just the price of a good or service. However, the current criteria for making the outsourcing decision is price. There is little room for considering other issues.

The problem is that price is a poor measure of other factors the government might value. Price reveals little about potential performance, for example. Although there is limited evidence that competition may produce greater customer satisfaction, the data on objective performance is poor at best. Morton Thiokol won the space shuttle solid-rocket contract based on price, for example, but the price was based on a design that put the burden on two thin O-rings to protect shuttle astronauts from harm. Mellon Bank won an Internal Revenue Service tax-return processing contract also based on price, but the price was based on employee piece-rates that fell to shreds when rush-hour hit.

Price also reveals little about public trust, innovation, helpfulness, or fairness. At least according to national surveys by the Center for Public Service, which I direct, the nonprofit sector has an edge over the federal government and private firms on virtually every measure of a healthy workplace imaginable. Nonprofit employees are more likely than federal or private employees to see their co-workers as helpful, committed, and open to new ideas, and more likely to describe their organizations and sector as the best place to go for innovation. Asked which sector is the best for helping people, even federal and private employees agree: It is the nonprofit sector. As for spending money wisely, even private employees split their votes almost evenly between the private sector and nonprofits.

Finally, price also reveals little about employee motivation. Asked why they come to work in the morning, almost half of the private employees interviewed in 2001 said they show up for the compensation, compared to less than a third of federal employees and less than a fifth of their nonprofit peers. According to advanced statistical analysis, private employees are motivated more by the compensation than either federal government or nonprofit employees. Satisfaction with salary is the number one predictor of job satisfaction among private employees, followed by pride in the organization and the sense that the work they do is interesting. In contrast, the opportunity to accomplish something worthwhile is the number one predictor of job satisfaction for federal employees, followed by the sense that they are given a chance to do the things they do best, and a belief that the work they do is interesting. Salary makes no difference in predicting job satisfaction among federal employees.

To the extent the federal government wants employees to put salary at the top of their list of concerns, going private makes greater sense. Moreover, as noted above, there are areas where salaries are so much higher in the private sector that the federal government cannot get the talent in-house. However, to the extent that the federal government wants a different set of motivations in play, it might consider nonprofits or federal employees.

The point here, of course, is where one gets labor depends in part on what one wants the labor to produce. If competition is the key to all of this, we all ought to figure out a way to put

greater competitive pressure on employees—for example, through pay for performance that really works. In this regard, passage of the Senate’s version of the Defense Department personnel reforms might be a far better way to assure more cost-effective production inside government than further investments in A-76 competition. One could easily argue, for example, that the money spent on A-76 would be better spent on a bonus pool that truly rewards high performance.

One could also argue that the money should be allocated to alternative methods that would allow government units to compete against each other for business. Why not let Denver and Cleveland compete against each other for the DFAS business, for example? No one has ever argued that competition between federal units and private firms is the key to cost savings. Rather, it is competition alone that provides the salutary effect. The competition can involve federal agencies competing against each other, or, in the recent case of the Transportation Security Administration’s human resource contracting, it could be private firms competing against quasi-government firms. (The winner of the \$554 million TSA new contract for recruiting and hiring passenger and baggage screeners was won by CPS Human Resource Services, a partnership between the California State Personnel Board and several local governments in and outside California.)

The ultimate challenge, therefore, is to move away from blunt instruments such as A-76, and the temptation to set targets, and toward performance-sensitive systems that allow federal agencies to achieve the effects of competition more naturally. If competition is, in fact, a good thing for government employees, and I believe that it is, the question is how to make it felt throughout government at a relatively low cost.