CONTRACTING OUT: CURRENT ISSUES

HEARING

BEFORE THE

SUBCOMMITTEE ON
CIVIL SERVICE

OF THE

COMMITTEE ON GOVERNMENT REFORM AND OVERSIGHT HOUSE OF REPRESENTATIVES

ONE HUNDRED FOURTH CONGRESS

FIRST SESSION

APRIL 5, 1995

Printed for the use of the Committee on Government Reform and Oversight

U.S. GOVERNMENT PRINTING OFFICE

94-072 CC WASHINGTON : 1995

For sale by the U.S. Government Printing Office
Superintendent of Documents, Congressional Sales Office, Washington, DC 20402
ISBN 0-16-047747-6

COMMITTEE ON GOVERNMENT REFORM AND OVERSIGHT

WILLIAM F. CLINGER, JR., Pennsylvania, *Chairman*

BENJAMIN A. GILMAN, New York
DAN BURTON, Indiana
CONSTANCE A. MORELLA, Maryland
CHRISTOPHER SHAYS, Connecticut
STEVEN SCHIFF, New Mexico
ILEANA ROS-LEHTINEN, Florida
WILLIAM H. ZELIFF, JR., New Hampshire
JOHN M. McHUGH, New York
STEPHEN HORN, California
JOHN L. MICA, Florida
PETER BLUTE, Massachusetts
THOMAS M. DAVIS, Virginia
DAVID M. McINTOSH, Indiana
JON D. FOX, Pennsylvania
RANDY TATE, Washington
DICK CHRYSLER, Michigan
GIL GUTKNECHT, Minnesota
MARK E. SOUDER, Indiana
WILLIAM J. MARTINI, New Jersey
JOE SCARBOROUGH, Florida
JOHN B. SHADEGG, Arizona
MICHAEL PATRICK FLANAGAN, Illinois
CHARLES F. BASS, New Hampshire
STEVEN C. LaTOURETTE, Ohio
MARSHALL "MARK" SANFORD, South Carolina
ROBERT L. EHRLICH, JR., Maryland
CARDISS COLLINS, Illinois
HENRY A. WAXMAN, California
TOM LANTOS, California
ROBERT E. WISE, JR., West Virginia
MAJOR R. OWENS, New York
EDOLPHUS TOWNS, New York
JOHN M. SPRATT, JR., South Carolina
LOUISE McINTOSH SLAUGHTER, New York
PAUL E. KANJORSKI, Pennsylvania
GARY A. CONDIT, California
COLLIN C. PETERSON, Minnesota
KAREN L. THURMAN, Florida
CAROLYN B. MALONEY, New York
THOMAS M. BARRETT, Wisconsin
GENE TAYLOR, Mississippi
BARBARA-ROSE COLLINS, Michigan
ELEANOR HOLMES NORTON, District of Columbia
JAMES P. MORAN, Virginia
GENE GREEN, Texas
CARRIE P. MEEK, Florida
FRANK MASCARA, Pennsylvania
CHAKA FATTAH, Pennsylvania

BERNARD SANDERS, Vermont (Independent)

JAMES L. CLARKE, *Staff Director*
KEVIN SABO, *General Counsel*
JUDITH McCOY, *Chief Clerk*
BUD MYERS, *Minority Staff Director*

SUBCOMMITTEE ON CIVIL SERVICE

JOHN L. MICA, Florida, *Chairman*

CHARLES F. BASS, New Hampshire
BENJAMIN A. GILMAN, New York
DAN BURTON, Indiana
CONSTANCE A. MORELLA, Maryland
JAMES P. MORAN, Virginia
BERNARD SANDERS, Vermont (Ind.)
FRANK MASCARA, Pennsylvania

EX OFFICIO

WILLIAM F. CLINGER, JR., Pennsylvania
CARDISS COLLINS, Illinois

GEORGE NESTERCZUK, *Staff Director*
NED LYNCH, *Professional Staff Member*
CAROLINE FIEL, *Clerk*

CONTENTS

CONTRACTING OUT: CURRENT ISSUES

WEDNESDAY, APRIL 5, 1995

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON CIVIL SERVICE,
COMMITTEE ON GOVERNMENT REFORM AND OVERSIGHT,
Washington, DC.

The subcommittee met, pursuant to notice, at 1:55 p.m., in room 311, Cannon House Office Building, the Honorable John Mica (chairman of the subcommittee) presiding.

Present: Representatives Mica, Bass, Morella, and Moran.

Staff present: George Nesterczuk, staff director; Daniel Moll, senior policy director; Garry Ewing, counsel; Ned Lynch, professional staff; and Caroline Fiel, clerk.

Mr. MICA. If I could have your attention, I'll call the meeting of the Subcommittee on Civil Service to order. We have delayed a few minutes as our ranking member was making remarks on the floor. Several of our other Members are engaged in the debate on the floor at this time and several committee markups are going on this afternoon. But welcome to our guests and witnesses to this subcommittee hearing.

I'll start with some opening remarks. Today, we resume deliberations that we began last week when we heard from the General Accounting Office and the Office of Management and Budget. It's obvious from that initial hearing that a significant number of government employees are engaged in functions that could be cost-effectively performed in the commercial marketplace.

Government agencies must concentrate their resources on core policy and authoritative functions. Wherever possible, Federal agencies should utilize the competition afforded by the private sector, and try to utilize that competition in support of commercial and administrative activities. While that principle served as a standard for the executive branch for 40 years, practice and principle do not always coincide, as we've seen.

I was encouraged that the Office of Management and Budget reaffirmed support for the principle I just spoke about, and I hope we can work with them and other agencies to make contracting out a more substantial part of our efforts to achieve genuine reform in government. However, the apparent foot-dragging in the contracting out process—where major agencies take many years to complete routine management studies—serves neither government agencies nor the public interest.

I'm concerned about the lack of reliable data to evaluate contracting policies that have been in place for 40 years. I'm also disappointed that the Office of Personnel Management appears to

have no record, or not an adequate record that we've seen, of assisting the Federal employees it's directed to aid under the OMB Circular A–76. This function of OPM must be improved or better defined, possibly by future legislation.

Our witnesses this afternoon provide a variety of perspectives on the potential that contracting out may strengthen the partnership between commercial organizations and activities, and our Federal Government agencies. Mr. Wendell Cox, director of State legislation and policy for American Legislative Exchange Council, will provide, first, an overview of the success achieved by State and local governments who have opted to shift functions to the private sector.

We shall also hear from Mr. Bert Concklin, who's president of the Professional Services Council; Mr. Gary Engebretson, president of the Contract Services Association; and Mr. Robert Tobias, president of the National Treasury Employees' Union. It's my hope that our witnesses today can provide additional insights into the Federal Government's activities related to contracting that we've seen over the recent years.

We welcome their participation, and look forward to their suggestions for improvements. We're going to hear from Ms. Eleanor Holmes Norton, Delegate from the District of Columbia, who has expressed a desire to present brief testimony and remarks before our subcommittee at some point this afternoon, when she can get over to the hearing. And with those brief opening statements, I would like to now defer—and I'm pleased to see, having arrived fresh from the floor and heated debate over the pending rule—the distinguished gentleman and my colleague and working companion on the subcommittee, Mr. Moran. Do you have an opening statement, sir?

[The prepared statement of Hon. John L. Mica follows:]

PREPARED STATEMENT OF HON. JOHN L. MICA, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF FLORIDA

Today we resume deliberations that we began last Wednesday when we heard from the General Accounting Office and the Office of Management and Budget. It is obvious from that hearing that a significant number of government employees are engaged in functions that could be cost-effectively performed in the commercial marketplace.

Government agencies must concentrate their resources on core policy and authoritative functions. Wherever possible, Federal agencies should utilize competition of the private sector for commercial and administrative support. While that principle served as a standard for the executive branch for forty years, practice and principle do not always coincide. I was encouraged that the Office of Management and Budget reaffirmed support for the principle, and hope that we can work with them to make contracting out a more substantial part of efforts to achieve genuine reform in government.

However, the apparent foot-dragging in the contracting-out process, where major agencies take many years to complete routine management studies, serves neither government agencies nor the public interest. I am concerned about the lack of reliable data to evaluate contracting policies that have been in place for forty years. I am also disappointed that the Office of Personnel Management appears to have no record of assisting the Federal employees it is directed to aid under OMB Circular A–76. This function of OPM must be improved or better defined by legislation.

Our witnesses today provide a variety of perspectives on the potential that contracting may provide to strengthen the partnership between commercial organizations and government agencies. Mr. Wendell Cox, Director of State Legislation and Policy will provide an overview of the success achieved by State and local governments who opted to shift functions to the private sector.

We shall also hear from Mr. Bert Concklin, president of the Professional Services Council, Mr. Gary Engebretson, president of the Contract Services Association, and Mr. Robert Tobias, president of the National Treasury Employees Union. It is my hope that our witnesses today can provide additional insights into the Federal Government's activities related to contracting in recent years. We welcome their participation and look forward to their suggestions for improvements.

Mr. MORAN. I'll figure out something to say, Mr. Chairman. I'm glad that you made mention of the rule. I trust you're going to be voting against that thing. But that's where we came from, and there is clearly——

Mr. MICA. Between now and the vote, I'll consider your suggestion.

Mr. MORAN. With every due consideration, that's what we tell some of our constituents when they raise issues that we know we are not going to be able to address in the way they want. Mr. Chairman, this is a terribly important area—the issue of contracting out. As you know, I have been very much opposed to setting arbitrary workforce reduction goals. I don't think that's the way to do it.

I think what we should be doing is, carefully analyzing what functions the Federal Government does not need to be performing because they can be performed more effectively and efficiently by lower levels of government, or even by the private sector. And when we determine what functions don't need to be carried out at the Federal level, and which positions thus become expendable, we can then determine what workforce reduction goals would be responsible to make, and how much savings we can achieve.

That's not the way we have gone about this exercise. And so many people are being put in the position of having to do much more with far less resources at the Federal level. I was interested to see an article, just within the last week, that showed that we have actually increased, in my congressional district, the employment base. It's gone up by about three employees for each Federal position that has been reduced.

I don't think that we should be reducing the workforce at the rate that we are. But my most important goal is to ensure that people who have the skills and the education, and particularly the dedication, to perform the work that makes this country so prosperous, peaceful, stable, progressive, that those people's talents be available for the benefit of this country.

You know, there is no Federal workforce that is more effective and efficient and less corrupted in the world than the American civil service. And despite all the problems that we find with what some people would call bureaucrats in a derisive way, the reality is that the American people are better served by the Federal workforce than any population in the world is served by its national public workforce.

But having said that, I want to make sure that we don't impede the ability of the government to be able to contract with those personnel and with those organizations that can provide the services that are necessary. And that, in fact, since we are required now to pay for the crime bill, pay for deficit reduction, pay for unemployment compensation, everything else that we funded by offsetting it against this $20 billion we were going to save by reducing the Federal workforce, since that is inevitable that it will be done, it be-

comes particularly important that we have the flexibility to be able to contract with professional services, with organizations, with people that can provide the services that we need; and that we achieve the kind of fair and responsible balance between the Federal workforce and the private sector that is necessary to ensure the efficient use of taxpayers money and the most effective use of the resources that we provide to the Federal Government.

So I'm glad we're having these hearings. They're important hearings. I think they are going to show us that we have good people, both in the private contracting sector as well as, certainly, within the Federal workforce. And it is up to us to do what we can to make sure that their talents are fully available and appreciated and used by both the Executive and legislative branches.

So I appreciate the hearing, Mr. Chairman. I appreciate the opportunity to participate in it, and look forward to the testimony of our witnesses.

Mr. MICA. Well, I thank the gentleman both for his opening comments and for his sincerity in trying to do the best job possible to address some of these issues. This morning we met with the Vice President—myself and Mr. Moran, several other Members, Mr. Clinger, and Miss Collins. The administration, the Vice President, has expressed a similar willingness to work together when we face downsizing, when we face civil service reform, and some of the other issues that are going to hit us.

Again, I thank you for your comments and your willingness to work with me on those issues. And I'll yield now to the vice chairman, Mr. Bass.

Mr. BASS. Thank you, Mr. Chairman. And I want to apologize initially for failing to be present at this morning's hearing. As you can probably tell, I am suffering from laryngitis, which, in this line of business, is a serious disability. I'm very pleased that we're having these hearings today, and I want to commend you for calling them.

As has been said by both you and Mr. Moran, as we look at alternatives to the traditional structure of government that we have today, I think it's important that we consider contracting out of services to be a priority, but only so long as that priority makes government work better, more efficiently, and smarter.

So I will be interested, in the course of these hearings today, to hear what our witnesses have to say about this process in that light. So with that, Mr. Chairman, I thank you very much, and yield back.

[The prepared statement of Hon. Charles F. Bass follows:]

PREPARED STATEMENT OF HON. CHARLES F. BASS, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF NEW HAMPSHIRE

Mr. Chairman, I would like to thank today's witnesses for taking the time to appear before this Committee. We will be continuing a very important discussion today and building on last week's hearing on the same topic. At issue is federal policy regarding the contracting out of services.

It is appropriate that we are holding these hearings at a time when we are re-evaluating the scope and role of the federal government. In the future, I expect that we will turn more and more toward the private sector to perform activities currently performed by the government. This will require clear guidelines on systematic cost comparisons and a thorough understanding of the potential pitfalls we may encounter.

I look forward to today's testimony, and hope to gain from the experience of our witnesses. I thank the Chairman.

Mr. MICA. I thank the gentleman. I also have an opening statement from the chairman of the full committee, Mr. Clinger, and without objection, will make that part of the record; and also a copy of formal statements by the ranking member. We'll make that also part of the record, without objection.

[The prepared statement of Hon. William F. Clinger, Jr., follows:]

PREPARED STATEMENT OF HON. WILLIAM F. CLINGER, JR., A REPRESENTATIVE IN CONGRESS FROM THE STATE OF PENNSYLVANIA

Mr. Chairman, I am pleased to be here today to participate in your second hearing on the Federal government's commercial activities and contracting policies. I wanted to be here for your first hearing but was unable to break away from other Committee business.

But as you know, Federal government reform is a priority issue for the Committee on Government Reform and Oversight. Last year, we were successful in enacting comprehensive legislation to streamline and simplify the Federal procurement system. In February, the Committee held its first oversight hearing on that new law.

This Congress, we have an opportunity to continue the efforts begun last Congress on procurement reform and other Federal government reforms. I have introduced a bill, (H.R. 1038), along with Chairman Spence of the National Security Committee and Chairman Gilman of the International Relations Committee, which will be the foundation for the Committee's procurement reform initiative.

I want to thank you, Mr. Chairman, for holding these hearings and focusing on an important aspect of how the government goes about acquiring needed goods and services. An important characteristic of the American model of government is that the government, in carrying out its responsibilities, should rely on the tax-paying private sector before it uses or expands governmental resources. Certainly now, as we review the appropriate role that government ought to play, we must consider and promote reliance on the private sector wherever and whenever possible.

Perhaps we can consider a general policy statement regarding the government's reliance on the private sector when we proceed with our next round of procurement reform legislation. Certainly the current administrative policy, reflected in OMB Circular A–76, affirms 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."

I hope these hearings will identify key issues which we can consider as we move forward with our efforts to further reform the Federal government.

Mr. MICA. Now, if I may, I'd like to call on our first witness this afternoon, Mr. Wendell Cox. Mr. Cox, if you'd come up. Mr. Cox is the director of State legislation and policy, the American Legislative Exchange Council. If you wouldn't mind standing for a moment, it's the custom and practice of our subcommittee to swear in our witnesses.

[Witness sworn.]

Mr. MICA. With that, we welcome you and apologize for the delay. We may have a vote or two here, but we look forward to your testimony; and again, welcome to our panel.

STATEMENT OF WENDELL COX, DIRECTOR OF STATE LEGISLATION AND POLICY, AMERICAN LEGISLATIVE COUNCIL

Mr. COX. Thank you, Mr. Chairman and members of the subcommittee. I am Wendell Cox, director of State legislation and policy for the American Legislative Exchange Council, or ALEC. ALEC is a group of State legislators. We have about 3,000 State legislator members, both Democrats and Republicans. We're dedicated to the Jeffersonian ideals of limited government, individual liberty and the free market.

Coincidentally, I also served three terms on the Los Angeles County Transportation Commission, as an appointee of Mayor Tom Bradley; and out of that, became a consultant, and have spent a number of years working in issues of privatization and competitive contracting around the world, largely in public transit.

Some of what I'm going to say to you this afternoon you may not have heard before. It may sound rather unusual to you, but I want to go through it anyway because I think there's some issues that you may not have heard before with respect to contracting and why it is that government costs are always higher—are often higher than they need to be. And I would also suggest that the comments that I make as regards government employment are not meant in any way to criticize employees.

To the extent that the government employment system in the State and Federal levels results in higher costs than are necessary, it is a systemic problem, not a problem that can be traced to the employees themselves. But as you are aware, there is considerable cost around the country in the States, localities, and in the Federal Government with respect to the cost of government.

In the private sector, you get ahead, you succeed, you make profits by paying no more than necessary for the factors of production, whether those factors are labor, materials, capital, supplies, or whatever. In government, however, it doesn't work that way because the market generally does not operate in government, except to the extent that government uses competitive bidding for some things like consultant contracts and supplies and that kind of thing.

It certainly doesn't work that way with respect to labor. The Nobel Laureate, Frederich Hayek said, "The competitive price cannot be known until there is competition." And that, I would suggest, Mr. Chairman, is the problem in government employment and in government services at the moment. There is no competition. The Economist, the British news weekly, one time put it this way, that the role of government should be to "spend each dollar to the best effect. Individuals do that day after day, so do companies. They succeed, more or less, because they face choices as customers and competition as producers. The minimum duty of a State should be to replicate such choice and competition in its own affairs, so that the billions it raises in taxes achieve the high-sounding aims it sets for itself."

I would suggest, Mr. Chairman, and members of the subcommittee, that government ought to be seeking to pay no more than necessary for those services that it provides. That is the public purpose of government employment; it is the public purpose of government spending. Let me digress a little bit, though, into the area of government employee compensation. We at the American Legislative Exchange Council have done a good deal of research on this issue.

And largely, as you know, the employment is a major cost of government services in the State and local government level. Government employee compensation represents about 60 percent of the operating costs of government. You've all heard how private sector workers have seen their wages and benefits stagnate over the last

20 years. From 1980 to 1991, private employee wages and benefits went up about 3 percent on average in the United States.

State and local government employment wages and benefits went up $4.78 for each average $1 increase in private employee pay. At the Federal level, it was about $4.56. In fact, at this point, the average Federal employee makes about 45 percent more than the average private employee, and about 30 percent more than the average State government employee.

Now you have all seen, over the years, the various reports that come out of the Federal Government that try to suggest or have suggested that Federal Government employee compensation is below that of the market. I would suggest to you that what we've seen of those studies suggests that they are incomplete and, in fact, that their results are outrageous.

Those studies do not include fringe benefits. They do not include the fact that government employees—Federal government employees have defined benefit retirement programs that are very expensive. They do not take into account the more liberal paid time off that is available to Federal employees. And most importantly, they don't deal with the security issue.

The fact is, Federal Government employment is secure. The U.S. Government is not going to merge with Canada and lay off half the staff. But private employees see that happening all the time. We have done an analysis, which we would be happy to provide the committee, to suggest that, if you take two employees starting off at age 25 and assume that they work for 40 years, and you start them at the same wage rate in the private sector and in the Federal Government, you will see the Federal employee make about 50 percent more in value, when you consider the value of security and the value of the extra time off and that kind of thing—on average, about $600,000 over a career.

Now, back to competitive contracting and privatization. The genius of competitive contracting is that the government, the public agency, retains full control. It is not that the private sector is better than the public sector, it is that competition produces better results than monopoly. Around the country, State and local governments have been competitively contracting for years; cost savings ranging generally from 15 to 50 percent, some cases of 75 percent.

Surveys of public administrators have said that cost savings occur in 98 percent of the cases. And we would argue, it should be 100 percent, because if you're not going to save money, you shouldn't privatize. Second, the competitive market puts competitive incentives into government itself. And you see the cost curve of government going up less when government does more competition—sort of the ripple effect on the rest of government services.

And finally, something that a lot of people never consider, is that the private contractors pay taxes, which public agencies do not pay, which reduces costs even more. It is important, though, as you consider privatization and contracting out, that you do it in such a way that you achieve good public results. And I would suggest that there are two primary principles of competitive contracting.

The first is that the public agency, or the Federal Government in this case, should remain in full policy control. It should decide what services are being contracted out; what are the provisions

with respect to quantity of service, the quality provisions, those kinds of things. And second, the second principle is that you must foster a competitive market. A private monopoly is no better than a public monopoly.

That means you want broad information out to the entire market; you want to limit the length of time that contracts are given for; you want to limit the size of contracts so that there's a maximum amount of competition; you want to allow no price negotiation after the contract is let. That way you have no such things as the rightly concerned low-balling concern. And if the public agency or Federal workforce is competing, they need to compete on the same basis that the private contractors compete.

At the State and local government levels, more than 100 services are now being contracted out. There is much more to go. I suspect that less than 10 percent of the services at the State and local government level are contracted out at this point. Probably, it's even less than that. There is considerable potential for contracting out and saving more money at the State and local government level. And there certainly is potential at the Federal level as well.

As I conclude, let me also quickly digress and raise a concern about the kinds of requirements that you at the congressional and Federal level put on State and local governments to preclude contracting out at the State and local government level. Perhaps one of the most egregious Federal requirements is Section 13(c) of the Urban Mass Transportation Act, or the Federal Transit Act, which requires public transit agencies that lay off people for efficiencies in economies to give them 6 years' severance pay, which is more than the average American receives—6 years at the most.

These requirements have, through the Department of Labor, systematically kept agencies from contracting out for service. But even more than that, and more destructively, they have stopped minority entrepreneurs from starting services to improve the mobility in our inner cities. I suggest to you, Mr. Chairman, that in apartheid South Africa, minority—actually majority there—black entrepreneurs were able to start services wherever they want and make money and become entrepreneurs—something we deny our people through a provision that I would consider one of the largest Federal unfunded mandates in the country—Section 13(c) of the Federal Transit Act.

The basic problem in government with respect to services is that the costs are not determined in the marketplace, and they cannot be determined in the marketplace without the application of competition. The analysis I gave you a few minutes ago that suggested Federal employees may be as much as 50 percent overpaid, should be scrutinized with as much as question as any other analysis. The fact is, administratively, we cannot determine market prices.

In the final analysis, it is why the Soviet Union died. And I would suggest, the real answer, in the long run, is to move all of government—as much of government as we can—to the market so we can guarantee the taxpayers that we are paying no more than market rates for what it is we are getting. Bringing government to market will be just as difficult, I believe, as bringing the market to the Soviet Union and to the communist bloc—not an easy process, but a process for the taxpayers that we must do.

I would suggest that the role of government, again with respect to employment and respect to spending, is to spend no more to provide government services than is necessary. Thank you very much.

[The prepared statement of Mr. Cox follows:]

PREPARED STATEMENT OF WENDELL COX, DIRECTOR, STATE LEGISLATION AND POLICY, AMERICAN LEGISLATIVE EXCHANGE COUNCIL

My name is Wendell Cox. I am Director of State Legislation and Policy for the American Legislative Exchange Council (ALEC). I was appointed to three terms on the Los Angeles County Transportation Commission by Mayor Tom Bradley, serving from 1977 to 1985. I have consulted in the United States, Canada, Australia, New Zealand and Europe on competitive contracting.

ALEC is a bipartisan organization of state legislators, with over 3,000 state legislator members. ALEC is dedicated to the Jeffersonian values of individual liberty, limited government and the free market.

BACKGROUND ON COMPETITION

In recent decades there has been increasing concern about the cost of government, and at every level of government, there have been serious budget difficulties. The problem is not fundamentally a revenue problem—it is a cost problem. Government revenues have risen substantially—and so have the unit costs of government

In the private sector, people and commercial enterprises succeed by paying no more than necessary for what they buy. Businesses pay the market rate—it pays no more than necessary—for labor, supplies and capital. The competitive market works to minimize factor costs. In government, however, the situation is different. While government uses the competitive market to obtain various goods and services, the competitive market is not applied to the factors of public service production. The result is higher than necessary costs. And government costs that are higher than necessary is government waste.

The problem is lack of competition. Government costs are determined in a non-competitive environment. As Nobel Laureate economist Frederik Hayek put it,

> The market price cannot be known until there is competition.

And government has a special obligation to exercise stewardship over the resources it compels from people. This is not so in other sectors of the economy. People are not forced to purchase specific goods and services in the market. They are able to exercise personal choice. No such choice exists with respect to taxation. Government's financial obligation to the people, is

> . . . to spend each (dollar) to the best effect. Individuals do that, day after day. So do companies. They succeed, more or less, because they face choices as consumers and competition as producers. The minimum duty of a state should be to replicate such choice and competition in its own affairs, so that the billions it raises in taxes achieve the high-sounding aims it sets for itself.[1]

The public purpose (or objective), then, of government spending is to provide for government services at a cost that is no higher than necessary. The imperative to spend no more than necessary is intensified by the federal budget deficit, which threatens the living standards of future generations.

Around the world, governments are using competitive contracting to apply market forces to government services, and with overwhelmingly positive results.

THE EXCESS COST OF GOVERNMENT EMPLOYMENT

However, before providing an overview of competitive contracting, it is appropriate to review an important root cause of higher than necessary government services costs—excessive public employee compensation. Government employee compensation is the largest component of state and local government budgets—representing 60 percent of operating costs.

ALEC's America's Protected Class series shows that, while private employee compensation has stagnated, government employee compensation has risen steadily.

> Average state and local government compensation increased 16.0 percent from 1980 to 1991 (inflation adjusted)—$4.78 for each $1.00 received by the average private sector workers. State and local government employees are now paid, on average, 10.3 percent more than private employees.
>
> The average federal civilian worker has received $4.56 for each $1.00 in compensation increase for the average private sector worker between 1980 and

[1] "Britain's Underclass," The Economist, May 23, 1987.

1991. Federal civilian employees are now paid, on average, 45 percent more than private employees.

Federal workers are compensated, on average, at least 30 percent more than above state and local government workers. If federal employees were compensated at the same average rate as state government employees, nearly $25 billion would be saved annually.

Inside the beltway, there is the perception that federal workers are less well paid than private sector employees doing similar work. This is based upon federal surveys that are frankly incomplete, misleading and outrageous in their results. The federal surveys are limited to wages—as if the more expensive federal fringe benefits have no value—as if the extra paid time off has no value—as if superior federal security has no value.

American Legislative Exchange Council research indicates that, where federal government and private employee wages start out equal, inherent federal employment advantages create 50 percent greater value over a career for government employees. This amounts to a nearly $600,000 advantage for government workers who start at the same rate of pay as private workers.

And then there is productivity. The lack of competitive incentives allows government staffs to become larger than necessary. ALEC has identified substantial variation in productivity among state governments.

ALEC estimates that, when all advantages of government employment are considered, including sub-market productivity, it is possible that government employment costs exceed market rates by nearly 75 percent.

In the competitive market, customers determine employee compensation. Private companies do not have the freedom to artificially raise employee compensation. In the private sector, the prices that customers are willing to pay for goods and services constrain how much will be available for employee compensation, investment and distribution of earnings to stockholders (including employee pension plans). A company that raises employee compensation above levels that customers are willing to pay will lose market share and eventually close, taking with it the jobs of employees and the investment of owners.

COMPETITIVE CONTRACTING

The realization that government employee compensation often exceeds market rates has led to an increasing use of competitive contracting.

Competitive contracting is the provision of a public service through a competitively awarded contract. It has been used for decades by private and public organizations to ensure that goods and services of a defined quantity and quality are produced for the lowest possible cost.

The public agency seeks competitive bids to provide a particular public service. The public agency establishes quality and quantity specifications. The competitive market responds to the invitation of the public agency, and one or more producer is selected to provide a specific service for a period of time. The public sector retains policy control over the service, while the competitive market produces the service under public scrutiny.

There are five basic steps in the process:

1. The public agency seeks competitive proposals to deliver a specific quality and quantity of service for a defined period of time.
2. The public agency may submit its own cost proposal, capturing all attributable costs, and subject to the same terms and conditions that apply to private proposals.
3. A contract is awarded to the lowest responsible and responsive public or private proposer who demonstrates an ability to provide the same quality and quantity of public service at a cost lower than that of the public agency.
4. Contractors, public or private, that fail to provide the service as specified are financially penalized or replaced.
5. New competitive proposals are sought in sufficient time to award a new contract for service commencing at the expiration of the contract. New competitive proposals are sought regardless of whether the incumbent contractor is a private company or the public agency itself.

Competitive contracting does not necessarily result in private operation of public services. It merely requires that the public service be provided according to the specifications of the public agency for the lowest possible cost. Competitive contracting removes the present bias toward in-house public service provision and replaces it with a results-oriented approach in which the lowest cost qualifying proposer, public or private, operates the service.

Competitive contracting reduces public costs in three ways:

1. Lower costs through provision of service at no more than the competitive rate (the "going" rate). Cost savings of 15 to 50 percent are frequent, with occasional savings of up to 75 percent. Touche Ross reports cost savings in 98 percent of cases.

2. Lower direct public service costs as public agencies improve their cost performance in response to the competitive environment. Competitive contracting not only results in lower costs for the public services competitively contracted, it also induces improved internal public cost performance. This "ripple effect" has been identified in various public services, including solid waste collection, public transit, fire protection, and other services. Public employee unions have negotiated competitive wage and benefit packages in response to competitive contracting.

3. Lower net costs as a result of tax revenues paid by private contractors on the public services they operate.

There are two fundamental principles of competitive contracting of public services:

1. The public agency should retain full policy control, determining which services are purchased, establishing quality and safety standards, administering contracts, and monitoring service performance.

2. The public agency should foster a competitive market. The maintenance of a competitive market is crucial to the success of competitive contracting. Private monopoly should not be tolerated any more than public monopoly. Fostering a competitive market requires:

a. Wide participation and full disclosure of information, so that all potential interested proposers have sufficient information to submit a proposal if they desire.

b. Limitation of contract duration (usually no more than five years including renewal options).

c. Limitation of contract size, so that smaller companies have an opportunity to participate.

d. Cost control through a requirement for fixed price proposals, and prohibition of price negotiation after contract execution.

e. No public agency specification of labor arrangements except compliance with applicable state and federal law.

f. The public agency should compete in the process under the same terms as the private proposers and should include all attributable costs.

Competitive contracting saves money not because the private sector is superior to the public sector; competitive contracting saves money because competition induces lower costs than monopoly. Services provided by private contractors are no less public than the same services that are provided by public agencies themselves, because the public agency remains in complete control.

At the state level, more than 100 services have been competitively contracted. But even so, there remains substantial opportunity to increase competitive contracting and reduce the costs of government.

Unfortunately, the federal government itself sometimes puts barriers in the way of state and local governments that seek to implement more cost effective service delivery mechanisms. A particularly egregious example is the special labor mandates in the Federal Transit Act (Section 13c). The US Department of Labor has repeatedly withheld federal grants pending the capitulation of transit agencies to union demands. The perniciousness of these labor provisions is illustrated by the six year severance payment obligation for transit employees dismissed because of efficiency measures. This mandate has been used to prohibit competitively contracted transit service and unsubsidized transit services. This has retarded transit job creation. Particularly onerous is the fact that minority entrepreneurs have been systematically denied the opportunity to initiate services and that residents in low income communities have been denied the improved mobility that such services would have provided. all as a result of this egregious federal mandate.

CONCLUSION

The administrative mechanisms for controlling the costs of government have failed, and are beyond repair. The answer is not better administrative systems, it is direct application of market forces, especially through competitive contracting. All governments, state, local and federal need to be brought to the market.

The transition of government to the market will be, in many ways, as difficult as the transition from statist monopoly economies to market economies in eastern Europe and the former Soviet Union. But the transition from costly monopolistic government service provision to competitive service provision is necessary.

April 10, 1995

Representative John L. Mica,
Chairman, Committee on Government Reform and Oversight
United States House of Representatives
2157 Rayburn House Office Building
Washington, DC 20515–6143

DEAR CHAIRMAN MICA:

Thank you for the opportunity to share our views with the Committee on Government Reform and Oversight Subcommittee on Civil Service on April 5.

As you may recall, our testimony that federal workers are better paid than private workers raised interest among the members of the subcommittee. Enclosed is a copy of our report America's Protected Class: The Excess Value of Public Employment.

Based upon the questions that were asked, we would like to emphasize the following points:

The system for determining federal pay comparability is unreliable. Admittedly it is difficult, if not impossible to administratively establish market rates (whether wages or prices). But, worse, the federal system falls far short of even the minimum that should be required of an administrative compensation determination system. Employer paid fringe benefits are not included, despite the fact that federal employer paid benefits are considerably above those of private employees and those of state and local government. Other advantages of federal employment, such as superior security and extra paid time off are not a part of the pay determination. The federal pay determination system is a disservice to both Congress and America's taxpayers.

Various research reports have estimated substantially different results with respect to federal employee wages than are produced by the federal pay determination system (these are noted in America's Protected Class: The Excess Value of Public Employment).

Even if the federal pay methodology were unquestioned with respect to wage determination, the inherent advantages of federal employment would still produce a substantial monetary advantage for federal employees.

We would be pleased to provide you with any additional information.

Sincerely,

WENDELL COX
Director, State Legislation and Policy

P.S. For your information, I have enclosed an "op-ed" from the April 7 Wall Street Journal, which raises additional concerns about the value taxpayers are receiving from federal employment.

[NOTE.—To reduce publication costs, the subcommittee has omitted from the record a report entitled, "America's Protected Class: The Excess Value of Public Employment." A copy of the report may be found in the subcommittee files.]

Mr. MICA. Thank you for your testimony and for the interesting statistics you gave us today. And I might, if I may, just ask a couple of questions about some of the statistics. Now, you said that the average Federal worker earns 45 percent more than the private sector, and then 35 percent more than the average worker in State and local government. Is that correct?

Mr. COX. It was 30 percent more than the State. I'm sorry if I said 35, I erred.

Mr. MICA. Thirty percent more?

Mr. COX. Yes.

Mr. MICA. And is this a cast in all Federal workers, or is it some category?

Mr. COX. No, it is all. It would include everyone from minimum wage workers to people that are making millions of dollars as CEOs of big companies.

Mr. MICA. Did your study break that down? I mean, are we paying certain levels a disproportionate amount?

Mr. COX. No.

Mr. MICA. Are the managers, administrators, and supervisors getting the bulk of this, or is there some differential?

Mr. COX. Well, the studies that have done—and we have not done this. Obviously, this would be a very expensive study, and nobody has really done a good comprehensive study including all the benefits and so on beyond the wages that are received by public and private employees. Simply nobody has done that.

But the general view is that, in the lower levels of government, the difference—you tend to have government employees paid more than private sector employees. And obviously, as you go further up, you get to a position where, in fact, private employees are paid more than public employees. The President is paid $200,000 and Lee Iacocca was paid $20 million.

Mr. MICA. How recent is your information?

Mr. COX. This is 1991 information. The 1994 information—and this is out of the Department of Commerce and Department of Labor, these data—shows approximately the same relationship.

Mr. MICA. So, the latest information confirms this?

Mr. COX. Generally speaking.

Mr. MICA. You gave another statistic. And again, if you could elaborate on it—you said public employees, Federal public employees, and you talked about 50 percent more. Is that adding in benefits?

Mr. COX. Yes. What we did—well, first of all, all of my testimony includes the employer cost of the fringe benefits. I don't deal with wages alone, and I think that is the fatal flaw in the program that the United States——

Mr. MICA. These first figures you gave include——

Mr. COX. Employer paid benefits as well.

Mr. MICA. OK. And then you jump to 50 percent. What was the difference, then, between the 50 percent? Is that over the term of employment?

Mr. COX. No, what it is—first of all, one has to be careful just basically saying, OK, let's compare the entire private sector, the entire public sector, because you don't know the job descriptions and the way that the various categories fall out. That was just given to give you a focus in terms of understanding of how much better paid Federal workers are, or State workers are, than the people that are paying the taxes.

The second figure, the 50 percent figure, is an attempt to get at the comparability issue by basically setting up a strawman kind of situation, where you say, OK, let's start two workers at the average private wage at age 25; let's apply the Federal benefits rate and the private benefits rate; let's apply a security percentage; let's apply the average rate of increase; and let's apply the differences in terms of time off.

In order to try to get an idea of a situation where, if you had two workers doing the same jobs—one public, one private—what would the difference be at age 65? And the difference is that the Federal worker would come out about 50 percent ahead as a result of the inherent advantages of public employment, even though the wage rate would have been the same in the beginning.

Mr. MICA. Then you used a figure of, over the total time of employment, an average——

Mr. COX. $600,000.
Mr. MICA. $600,000?
Mr. COX. Almost $600,000, that's right.
Mr. MICA. For every employee?
Mr. COX. That would be for this prototypical employee, starting out at age 25 at the average private wage.
Mr. MICA. And they would end up with $600,000 more in the full package?
Mr. COX. That's right.
Ms. MORELLA. Will the chairman yield?
Mr. MICA. Yes.
Ms. MORELLA. Mr. Cox, I respectfully have some concerns with your statistics. Would you supply this committee with that report?
Mr. COX. I'd be very happy to.
Ms. MORELLA. Because we're in an area where we have locality pay to the very contrary to what you say, because there is that 30 percent gap between the public and private sector. I would appreciate it, thank you.
Mr. COX. If I might, Mr. Chairman, and I appreciate that—we will be most happy to supply that. One of my basic points is, though, that the problem with the whole locality pay thing is that it is based upon wages only. It does not take into consideration a number of inherent benefits of Federal employment.
I mean, better fringe benefits are a monetary advantage. Better security is a monetary advantage. More paid time off is a monetary advantage. But anyway, we'll provide that, and would be most interested in any criticism you might have.
Ms. MORELLA. Thank you, Mr. Chairman.
Mr. MICA. Well, it looks like we have a vote. If you wouldn't mind, we will probably recess for about 20 minutes. We'll come back about quarter of, because you presented some testimony here that I think the ranking member and other Members would like to question further.
We will recess until about quarter of, and then reconvene.
Mr. COX. Fine.
Mr. MICA. And I thank you for your patience.
[Recess.]
Mr. MICA. If we can, I would like to reconvene here. And I apologize, we had not one vote, but two votes. And part of the mission that we're seeking to accomplish is done, and now there will be about 4 hours of debate. We've got plenty of time, Mr. Cox, if you're available for the next 4 hours here.
Mr. COX. It would be a pleasure.
Mr. MICA. I'm expecting the ranking member to return momentarily, and several of the other Members. In the meantime, if I may, I'd like to continue on the line of questioning that we started about some of the statistics that you brought before the subcommittee today. One of the items we were talking about was the amount of compensation over the tenure of employment.
And I think you said, on average, $600,000 more for Federal. Did you have any statistics—well, first of all, is that against the private sector, or is that against State and local?
Mr. COX. If I might, Mr. Chairman, let me make sure it's completely understood. What we did was a strawman analysis. We

said, let us take a private worker doing the same work as a Federal worker, starting at the same pay at age 25, and let's go through a 40-year period. Now, what we do not know is what, truly, is our Federal worker's pay in wages relative to the private sector.

You've got the pay agents report that says, on average, that private workers are paid 23 percent less. You've got a CBO report that says 12 or 13 percent. You've got other academic research that says Federal worker wages are 3 percent less than the private sector; others, as much as 40 percent more. So what we did is we said, let us take—we're not making a statement with respect to the average, because I would argue that the present mechanisms for trying to determine Federal pay are really very flawed, and nobody truly knows what they are.

So we said, if we could assume they are the same, what would the difference be? We're not making a charge or making an allegation that on average it's $600,000 more. We're saying that if we had two workers starting and running through a career, starting at the same wage rate, the Federal employee would have $600,000 worth of value additional over a career.

Mr. MICA. Now, you also—and again, I don't want to take any words out of your mouth, but maybe you could explain for the subcommittee—you said the comparison of compensation, and then you also said that's more, and then you said the benefits are more. Is that correct? I think your term was more liberal benefits in the Federal sector.

Mr. COX. Right.

Mr. MICA. And how does that compare with the private sector? And then the liberal benefits you spoke of and compensation, how does that compare in State and local governments, as far as your study?

Mr. COX. OK. When we talk about compensation, first of all, we mean the total monetary compensation, including wages and employer paid benefits. In the private sector, on average in the United States, the benefit load on top of wages is a little bit less than 20 percent. In State and local government, it's in the range of 22 to 23 percent, maybe 24 percent. And I'd have to calculate it. But the Federal number is over 30 percent.

For example, if you take a look at the total compensation for a Federal civilian employee in 1991, it was $46,100. The total wage was——

Mr. MICA. What was that again?

Mr. COX. $46,164. The total wage was $34,724; that's 30-some percent over the wage.

Mr. MICA. Thirty-six percent?

Mr. COX. Yes, very significant. I mean, it's not quite double, but it's significantly above the private and even above the State and local government rate.

Mr. MICA. You also referred to the State and local governments getting into more of the contracting out. I guess the local governments have had more of a history for this for municipal type services. And the State services are also being increased in this area. You said, I think, it was approaching 10 percent of the activities or functions. What are these numbers; can you elaborate on them?

And then, what kinds of services? And a third part of the question—are there any models for this, as far as State governments?

Mr. COX. Well, first of all, the 10 percent is really conjecture. There have been estimates of anywhere from 5 to 10 percent that have been made. But there are arguments about how you would calculate that. The area that I'm most familiar with, which is about a third of State function and two-thirds local function, is public transit service, where the number is, in fact, just a little bit over 10 percent at the moment.

So there's plenty of room to go. You'll find some services where a large percentage of services are contracted out and some where very little is. But I mean, we've got welfare administration being contracted out in some places. We would argue that you can competitively contract virtually everything but the legislation function and contract management.

We would not propose contracting out Congress. Now, with respect to models—I hope that I won a friend——

Mr. MICA. We don't want to put that to a vote.

Mr. COX. No, no. I guess with the new Congress, it may be a different issue. In terms of models, there are some proposed models around that have not been implemented yet in the United States. One is a process which we call petition of interest process, whereby you would, rather than mandating a percentage of contracting out—because one of the problems as you look at government is, how does a legislative body determine what should be contracted out; it's very difficult.

So what you do instead, through the petition of interest process—a bill that got through both houses in Arizona, but was vetoed by Governor Mofford a few years ago, and is being considered now in a couple of States—a petition of interest process would have you basically say to the private sector, challenge us on specific services; private sector, if you think you can do the service better, send us a petition of interest saying we would like to provide your janitorial service, your welfare administration, whatever.

Send that in, and then a board would take a look at that; see whether or not the company was a valid company that had the financial capability and the technical capability to do it. And once that was established in the affirmative, if it were, then you would go out to competitive bidding for the process. Now, there are some other models that are being used around the world.

As you may or may not know, the Local Government Act of 1988 in the United Kingdom required the contracting out of six specific county government and municipal government services. The results out of that have been very, very good. And indeed, one of the things that happens in contracting out is, the public service becomes much more competitive, too, and it lowers its cost. And in a lot of cases, you have public agencies, their own workforces winning the contracts.

In New Zealand, Socialist Finance Minister Roger Douglas moved the country, in the 1980's, strongly toward markets. And what they did through—I can't remember the name of the act now, but it was an act having to do with local government. Essentially what they did is, they required local government units to, what

they called, corporatize into direct service organizations and compete in the market.

So they would compete against private companies for contracts. In the long run, they might even compete in the market. And actually what they did there, in a somewhat unique approach, is, they actually made them taxable as well, because they recognized that when you provide services to public agencies, you're actually foregoing tax revenues. So there is that model, as well, that has been developed outside the United States.

Mr. MICA. One of the problems we've had at the Federal level is that we have operated with—I guess you're familiar with the A–76 circular. And we see that you have some opportunities, sort of, to lead the horse to water; but they're not drinking very often. And one of the things that we may consider is some legislation in this area. Do you think that you need legislation and then, say, a combination of rules to implement this? What would be your recommendation from the models you've seen?

Mr. COX. Well, in fact, there's a third model that is sort of coming up in a lot of services in Europe and Australia and New Zealand at this point—something I would refer to as the policy-only body kind of approach. It's something that the Advisory Commission on Intergovernmental Relations recommended a few years ago, but nothing has happened with.

A basic approach whereby you would essentially take away—you would basically set up agencies or tell your agencies that you may do only policy, you may do only administration; and require them to virtually purchase all of their service—whether from a public organization or a private organization. And what this has done—especially in transit in Europe—is create a situation where you've got administrative bureaucracies who now have an incentive to save the public's money.

Because your problem, you see—why the A–76 process doesn't work very well, and why there's been such resistance to contracting in public agencies at the State and local government level—is, here you are, you say to a public manager, we are going to reward you based upon the size of your budget and the size of your staff. Well, no rational public manager is going to come in and tell his boss that he can provide the service less with a private contractor.

It's a prescription for disaster, with respect to your career. So what you do is, you create a situation—and it's very theoretical, I know, at this point—but you create a situation where you basically limit the scope of your agencies to policy and administration, and force them to go outside for virtually everything they do, which will create more of a mentality that gives the taxpayers a chance, with respect to these organizations.

Mr. MICA. We've talked a bit about contracting out, but what about providing opportunities for employee groups or unions or other representative bodies to bid on this work?

Mr. COX. Oh, they should, Mr. Chairman. Indeed, they ought to be allowed to do that. The English example and a lot of the European models and New Zealand and Australia—that is a part of the process. One of the people—I don't know if you've had Ron Jensen from Phoenix talk to you yet, but you may want to listen to him. He administers a bunch of work the city of Phoenix does. And

they've developed, rather carefully, a public-private competition model. The basic idea being to recognize we're not saying that public employees are less efficient than private employees. We're only saying that world records, for example—if I can use an example of track; I'm an old track man. The fact is that the 4-minute mile would never have occurred without competition.

And so, competition makes us all better, whether we're in the private sector or the public sector. And this model of public-private sector—something that comes out, by the way, very strongly in Vice President Gore's National Performance Review Reinventing Government—is a very valid thing. And obviously, public unions, public employee work groups ought to be allowed to compete, ought to be encouraged to compete.

In the long run, one would hope that you would create a situation whereby you would be able to corporatize these organizations and sell them to the public employees, which has been done in a lot of countries.

Mr. MICA. Another problem that we had show up in our last panel with OMB is that OMB has a responsibility to oversee and prescribe some of the parameters for these functions being privatized. And one of the problems that we found is that they weren't able to create any models to quantify the task, or qualify the task, and then, also, to evaluate performance.

Is there any way we can judge once—you get into this what you want to get in, what you want done; and then when it's performed, to review it and analyze and see if the performances measure up and if you're getting your dollar's worth.

Mr. COX. Well, yes, that's a real problem. Because I would suggest, if one cannot do that in specifying the contract for private suppliers to bid on, I would question whether government has the capability of evaluating its performance, with respect to public employees that it employs. And one of the most difficult problems, as you indicate, in privatization and contracting out of services, has been the difficulty of specifying the task.

And indeed, the privatization process has given government, in a lot of cases, the ability to, for the first time, really specify the task. But depending on the kind of task, you can have standards with respect to any number of kinds of performance issues. You ought to try to have the administration be as nonprescriptive as possible and flexible as possible.

With respect to those things you're very interested in, again, simple thing is, you go back to public transit. And I realize the world has more in it than public transit, but you're concerned about on-time performance; you're concerned about meeting schedules; you're concerned about the buses being clean—any number of things like that. And what you do is, you can set up processes whereby contractors pay penalties when they fail to perform up to those standards, which creates an additional financial incentive for them to provide better service.

And I mean, the experience has been really stunning in some places. In Los Angeles, Price Waterhouse, the accounting firm, has reported that the contracting out of a major bus system in the San Gabriel Valley section of Los Angeles has saved 60 percent. The service is better and the quality is better and the safety is better.

That is to say, the old public cost of operating the same service was 150 percent more than the private competitive cost.

Now, that obviously is the high end of the scale. But those are very legitimate concerns, and one has to be very careful to make sure that you understand, as you put this process forward, that it is public services you are trying to obtain. And you are trying to obtain the best in public services, and you just have to be careful about that.

Mr. MICA. Well, you talked about transportation, and I guess if you look back at public transit, most of it was really privatized and people were making a profit. Then it fell into the category where more people were taking automobiles and became less profitable, and has been steadily subsidized more and more by the public sector.

And then some of the standards which you spoke to, also have distorted the process. For example, I think you mentioned section 13(c). This is a tough one, because people are not willing to come forward and say, I'm willing to take less as far as compensation; I'm willing to take less as far as benefits; or I'm willing to throw overboard this 13(c) security and protection blanket that's been put in, which makes change extremely difficult.

Amtrak is an example where, we're into that category. We've got three-quarters of a billion dollars, I guess, subsidy, and we now find ourselves really mired down in trying to make changes. You have the employee groups and others really protesting any changes. So, is crises and complete failure and breakdown and bankruptcy the only way we're going to get this changed? Or is there any example, or is there any model you've seen that we can use to help bring this about in a reasonable fashion?

Mr. COX. Well, first of all, let me comment on your first point about how transit was privatized before. It wasn't; it was a regulated market, owned by—it was a utility. And one of the main reasons that the private transit operators failed was the unwillingness of regulatory agencies to provide inflationary rate increases. And I can tell you since public transit has become public, there is no such restraint.

And in fact, right now you have major suits going on with bus rider groups in Los Angeles, trying to overturn fare increases because they are so displeased with the ability of the public agencies to control the fares. And what happened, even with a monopolistic, regulated market in the private sector, the productivity was declining. It has declined at more than twice the rate since the public takeover. But you get to the point of, obviously nobody who has a privilege wants to give it up.

And I think one of the things, if we are serious about solving our budget deficit crisis—and I realize this is not a very political thing to say—but one must be prepared to start saying no to the people that have unfair privileges. This Congress is not guaranteeing, to the average wage earner out there, 6 years severance pay when they get laid off the job. So I would argue from a philosophical standpoint, we ought not to do that.

But in terms of models, there are some in addition. San Diego, for example, has, over the last 15 years, moved from a situation where it was contracting out virtually none of its transit service to

where it's contracting out about 40 percent of its service. Contracting out on average, about 3 or 4 percent, one could, over a longer period of time, use attrition to protect the albeit bloated and unfair benefits of current transit workers who make double the market rate for unionized workers in the same industry.

One could protect them by just converting to competitive contracting through the driver attrition rate—just don't hire new drivers at $16 and $18 an hour. Hire them at the competitive rate—unionized, nonunionized rate—and you could affect the economies over a 10-year period very easily. And what's happened in San Diego, where they have done this, their costs have actually gone down, relative to inflation, about 30 percent since 1979.

And at the same time, the public transit agency now has a deal with the amalgamated transit union whereby its new drivers, for contract services, it's able to hire at competitive rates. And it's now bidding successfully against private carriers. So there is a model out there. The problem is, I believe, with respect to that particular issue, the Congress needs to repeal 13(c) and take away the barriers to going further, with respect to that kind of a conversion.

Mr. MICA. All right. Thank you for responding to the questions that I had. I see our ranking member is back. Mr. Moran, we've had additional testimony while you were gone, relating to some of the statistics that Mr. Cox gave the subcommittee. And I note that you were concluding your business on the floor, but yield to you now for any questions you may have for the witness.

Mr. MORAN. Thank you, Mr. Chairman. Mr. Cox has put plenty of testimony in the record. If I were to ask questions, some of his responses are more than likely to be duplicative, and we have several witnesses after Mr. Cox. So I think at this point, in the interest of efficiency of these hearings, that I'll defer any questions.

Mr. MICA. I would like to thank you, Mr. Cox, and let me see if Mr. Bass has any questions.

Mr. BASS. No questions, Mr. Chairman.

Mr. MICA. Again, we thank you for your testimony. I know I questioned you at length, and appreciate your responses. We may have some additional questions from panel members who are not with us this afternoon. We'll leave the record open, and hopefully, you can respond.

Mr. COX. I'd be very happy to.

Mr. MICA. Thank you.

Mr. COX. Thank you.

Mr. MICA. We've had a request from a Member, and I always try to accommodate them. Our delegate from the District of Columbia, Eleanor Holmes Norton, has asked to testify before the committee. And I'd like to welcome her to the Civil Service Subcommittee; she serves on our full committee. Welcome, and we'll offer you this opportunity to comment now.

STATEMENT OF HON. ELEANOR HOLMES NORTON, A REPRESENTATIVE IN CONGRESS FROM THE DISTRICT OF COLUMBIA

Ms. NORTON. Thank you very much, Mr. Chairman. I very much appreciate your looking into the contracting area. As it turns out, it is the cost of government that has seen the least inspection, and,

in a real sense, least justification. By saying that, I don't mean to imply that contracting out is never justified. On the contrary, I think we all live in the real world, where State after State and city after city now contract out parts of what used to be a public mission.

I certainly recognize that, particularly in this day and age, our obligation is to get the best deal for the taxpayer, so long as we don't cut corners unfairly and so long as we are not unfair to our own workforce in some way. I have today dropped into the hopper four bills. They are bipartisan; Ms. Morella is my chief cosponsor. And those bills are aimed simply at helping us to understand what we need to know about contracting out, even as we have insisted on accountability from our own employees.

Mr. Chairman, I think you would be shocked at how little we do know about this extraordinary expense of the Federal Government. It caught my attention last year when I recognized that $105 billion of Federal Government money goes to contracting out for services alone, and nobody can tell you anything about it. It's a virtual shadow government that is out there working—whether poorly or well, I do not know; I'm not here to criticize them.

I'm only here to say I don't know enough about them, given the size of that amount. Now, I got interested in it first because we were, as is our custom, failing to give Federal employees their full raise. Now, I am the first to say I represent Federal employees. And so part of my job is, of course, to look out for Federal employees. They have a statutory raise that is due them, and they usually don't get the full amount.

But then I noticed that while virtually every—this was last year, last session—while virtually every sector was taking some sacrifice, this huge mission was taking no sacrifices; not $1 of sacrifice. It seemed strange to put off of the screen such a large amount. For example, between 1989 and 1992—and I will merely summarize my testimony, Mr. Chairman—between 1989 and 1992, the number of contractors doing business with the government rose from 62,819 to 82,472.

During the same period, the Federal workforce remained mostly constant and, of course, had begun to go down. During that same period, we did, in contracting out, $184 million in 1989 to $200 million by 1992. I mean, this is a fast-growing cost of the government. It's such a fast-growing cost that it would pique almost anyone's curiosity. This is government-created work. I'm talking now, service contracts.

So what we have here is what some have called a shadow government. These are folks who get their paycheck from the same place that civil servants get theirs. The difference is that we insist upon holding civil servants accountable. And while I see no reason why people in the private sector should be held accountable in precisely the same way as in government, we certainly ought to know more about this large amount of money and how it's used than we now know.

The Clinton administration, when it came in, said that they thought service contracts were out of control. It was something they didn't know anything about. And they have begun to do something; they have proposed new performance-based standards for ex-

isting service contracts. But very frankly, the President's budget also doesn't do anything about service contractors.

If you say to Federal workers, you will not get your full statutory pay increase, you might say to contractors, we want you to cut, let's say, 1 percent from what you have been charging us, and transfer that money to Federal workers and give them some greater percentage of their statutory pay cut. I guarantee you this: If you told service contractors, who are used to competing, to tighten your belt to the extent of 1 percent, they'd tighten it so fast to keep that contract that the government would save a lot of money in a very short period of time.

So I have introduced four bills. One, of course, does deal with the Federal pay raise. It would cut $2 billion in Federal agency funds for service contracts, and make the money available to pay Federal employees more of the paycheck that our statute says they are due. And may I say, Mr. Chairman, I don't think you can, year after year, say to a workforce, we're not going to give you what we say we're going to give you, without having a affect on that workforce that I don't think anybody wants to have.

In effect, it's a give-back. If you say you're due 2 percent a year and every year you say, but I'm only going to give you 1.1 percent, after a while, you demoralize that workforce. We ought to come up either with a better way of doing it, or we ought to give these people their pay raise. My second bill plugs a hole—and a large hole, I think—in our buyout legislation.

In that legislation, we say, I think quite appropriately, that civil servants who have been cashed out, bought out, cannot be replaced. And yet there's nothing in the existing law to keep an agency from replacing bought out employees with contracted out employees. If that's the case, then we have not downsized the Federal workforce. We have simply substituted one kind of an employee for another kind of employee. And I can only think of this as an oversight. I think it ought to be corrected.

My third bill would have agencies do what you would think they would already do as a matter of cost; and that is simply to cost out whether they save any money by contracting out. And in fact, this kind of costing out is not systematically done. We know that because of a 1994 GAO study. And this study looked at 9 or 10 agencies and found that work that they had contracted out was being done for more than that work could have been done in the agency.

And that means somebody has just gotten in the habit of contracting out work. That's contracting out more of taxpayers' money than, in those cases that the GAO discovered, were necessary. And my final bill would have us do what surely is the beginning point of understanding this process—simply to find out how many folks are out there; what is the extent of this workforce?

In 1988, Congress passed a bill requiring the agencies to significantly cut service contracts. So the idea of cutting service contracts is not new. But then when Congress asked GAO to find out if they'd done it, GAO said that there was no way to know if the agencies had actually complied with the bill. So my fourth bill would require OMB to develop a governmentwide system for determining and reporting the number of non-Federal employees who are engaged in service contracts.

It seems to me that the other side of wanting to make sure that we are putting work where it can be done most efficiently and with the least cost, is insuring ourselves that that, in fact, will happen. We have no way of knowing that now. We have an unchecked, unmonitored contracting out system. I believe that the case for contracting out will be stronger and the morale of Federal workers would be better if, in fact, we could say, we know what we're doing; and when we contract out, we know we're getting the best deal; and we know a sufficient amount about contracted out employees so that no question of fairness can be raised. Thank you very much, Mr. Chairman.

[The prepared statement of Hon. Eleanor Holmes Norton follows:]

PREPARED STATEMENT OF HON. ELEANOR HOLMES NORTON, A REPRESENTATIVE IN CONGRESS FROM THE DISTRICT OF COLUMBIA

Today I am introducing four bills to bring some accountability and cast a search light on the elusive, stealth "shadow government." This government we cannot see is the proliferating and largely unmonitored private contract service sector and work force from which the federal government procures services. Although a huge $105 billion Goliath, this sector has emerged unscathed and uncut at a time when deficit reduction has spared few others.

In fact, service contracting constitutes the fastest growing area of federal procurement. In the 1980's, federal officials acted as if they wanted to contract out the entire government. From FY 1989 to FY 1992 alone, before the Clinton administration came into office, the number of contractors doing business with the government rose from 62,819 to 82,472. Over that same period, the amount of money shelled out to contractors of all kinds mushroomed from $184 billion to almost $200 billion. Service contracts alone account for $105 billion of the $200 billion spent each year on outside contracts.

This is a government-created and financed monster that the OMB itself concedes is out of control. How extraordinary, then, that in a budget which has left no visible stone unturned, this large federal expenditure has remained hidden in the shadows and has not contributed a single dollar of mandated cuts to deficit reduction, as federal agencies and employees have. How remarkable that, despite a government-wide effort to promote efficiency, we have not considered the inefficiency of guaranteeing contractors an invulnerable chunk of tax dollars.

The Clinton administration, to its credit, has worked hard to make service contractors more responsive—for example, by proposing new performance-based standards for existing service contracts. How surprising, then, that the budget the Congress is now considering proposes no cuts in funds allocated for service contracts—thus leaving untouched a huge source of potential savings—while demanding continued sacrifices from the career work force that makes up the "visible government." Thus far, the shadow government has not registered beneath the green eyeshades of budget cutters, including the Congress.

The time is long past due for overhauling contracting practices. With the four bills I am introducing today, I hope to help begin the process of re-inventing federal contracting just as the rest of our government is being re-invented.

FULL FEDERAL PAY RAISE

My first bill would cut $2 billion in federal agency funds for service contracts and make this money available for pay raises that are due federal employees next year. Federal employees are again being required to give up part of their statutory pay increases while, again, contract employees paid from the same federal budget remain untouched. The intent of my first bill is to eliminate the raw discrimination that allows the government to seek sacrifices from civil servants because they are where we can see them but to give immunity to contract employees because they are out of sight.

Beyond the discrimination against career employees who are denied modest increases promised by statute, current contracting practices are fundamentally bad business. According to a March 1994 GAO report, issuing service contracts and hiring consultants actually costs federal agencies more than using federal employees. In three of the nine cases analyzed by GAO, agencies could have saved over 50 percent by keeping the work in-house.

BUYOUTS

My second bill would plug a gaping hole in the landmark buyout legislation we have only just passed. Congress went to extraordinary lengths to ensure that civil servants who were bought out with cash could not be replaced and that the resulting 272,000 reductions in the federal work force would be permanent. However, as it stands now, the buyout law would allow untold numbers of contract employees to take the places of bought-out federal employees—substituting shadow government employees for career employees. My bill would amend the Federal Workforce Restructuring Act to prohibit agencies from contracting out work previously done by buyout recipients.

COST COMPARISONS

The reason most often touted for contracting out work is that it is cheaper. The March 1994 GAO study contradicts this assumption, and an OMB study released in January 1994 shows that the cost-saving assumption is often not even tested. Federal agencies do not compare the costs of contracting with the costs of doing work in-house. My third bill would require agencies to make these cost comparisons and would prohibit any agency from entering into an outside service contract if the services could be performed at a lower cost by agency employees.

SIZE OF CONTRACTING WORK FORCE

One of the chief obstacles to regulating the contracting work force has been the absence of information on the extent of that work force. In 1988, for example, Congress passed legislation requiring agencies to significantly cut service contracts. However, a subsequent GAO report found that there was no way to know if the agencies had actually complied with the legislation. My fourth bill requires OMB to develop a government-wide system for determining and reporting the number of non-federal employees engaged in service contracts.

All four of these bills would provide more systematic ways for monitoring and constraining the expenses associated with contracting out of services—just as we have insisted for federal agencies and employees. Efficiency and deficit reduction must not stop at the door of the federal agency. We need to bring the shadow government into the full light of the day so that the sacrifices demanded in the name of re-inventing government may be shared by all employees and by every area of government.

SUMMARIES OF SERVICE CONTRACTING BILLS INTRODUCED BY CONGRESSWOMAN ELEANOR HOLMES NORTON

1. The first bill cuts $2 billion in Federal agency funds for service contracts and makes this money available for pay raises that are due Federal employees next year. Federal employees are again being required to give up part of their statutory pay increases while, again, contract employees paid from the same Federal budget remain untouched. The intent of this bill is to eliminate this inexplicable discrimination.

2. The second bill amends section 5(g) of the Federal Workforce Restructuring Act of 1994, (Public Law 103–226) to prohibit an agency authorized to offer voluntary separation incentive payments under that Act from contracting out, in whole or in part, the duties previously performed by an employee who separated upon receiving such a payment. This is to ensure that no substitution of shadow government employees for career employees occurs.

3. The third bill prohibits any Executive Branch agency from entering into a service contract if the services to be procured under the contract can be performed at a lower cost by employees of the agency. It requires agencies to perform cost comparisons (contractor cost v. in-house cost) when deciding whether to contract for a service. The requirement applies to contracts entered into after the date of enactment.

4. The fourth bill requires the Director of the Office of Management and Budget (OMB) to develop a government-wide system for determining the number of persons employed by non-Federal Government entities providing services under service contracts awarded by agencies in the Executive Branch of the Federal Government. It also requires OMB to submit an annual report to the Congress indicating the number of such persons providing services and the number with jobs comparable to those of career Federal employees providing services to agencies.

Mr. MICA. We thank you for your interest and your comments. I have not had an opportunity to review in detail the contents of

the legislation you're proposing, along with my colleague, Ms. Morella. But there are several areas that we will be addressing. The buyouts is one area where we will be having a hearing in the future, and we welcome both your suggestions, your legislative recommendations and your participation in that process.

We're also concerned about giving employees the opportunity to compete, as you heard maybe at the end of the questioning of our last witnesses. Also, we're equally concerned that we don't have a good data base, or quantifying or qualifying base of what's going on right now, either from GAO or from OMB; and how to evaluate the service and value received for contracting out that is now occurring or proposed.

So we will be looking at some of these areas. We welcome your participation, your suggestions, and we'll look at the legislation. I thank you for coming, and I'll defer now to our ranking member, Mr. Moran.

Mr. MORAN. Thank you, Mr. Chairman. Ms. Morella, we agreed with the Vice President this morning, and I was not surprised. I know that your goal is the same as mine—to get the highest quality work done for the least cost, and to address what we believe to be this Nation's priorities in the most representative, responsible manner. But given the fact that 272,900 Federal employees are going to be cut from the workforce—and it's going to be done, we can't stop it—many of those will have an opportunity to find employment in this area by contracting with the Federal Government.

And I say that despite some policies which mitigate against that; in fact, some legislation that you, I understand, support that that should not be done. The reality is, it's going to be done because while we have cut the workforce, we haven't cut Federal activities, the responsibilities that the Federal Government still has to carry out various programs.

And it seems to me, since history shows that a pendulum swings back and forth, that it's probably in the long term health of this area for people to be able to contract with the Federal Government, particularly Federal civil servants who choose buyouts or who leave the Federal Government, but wish to be able to continue to make their expertise and experience and knowledge available to the programs that they were at one time part of, and still are committed to.

So I'm not as anxious to put up barriers to contracting out because I think our principal responsibility is to provide jobs and a healthy economy to our constituency. And while I have more confidence in the Federal Government and the Federal workforce than the majority of the House of Representatives today, I think that may change 1 day.

And in the meantime, I don't want for us to lose some of the best and brightest people that are currently Federal employees because there were no jobs available and, in fact, we set up barriers to their employment in the private sector within the Washington area and within the same kind of activity area where they have chosen their careers.

So I have misgivings about what appears to be the thrust of your legislation. Do you want to respond to some of that?

Ms. NORTON. Yes. I think you misunderstand. I have no problem—I think you're talking about my buyout bill. My buyout bill would not keep a Federal employee from going to work with a contractor. My buyout bill is aimed at the clear intention of Congress to downsize the Federal workforce. And all it would say is that you cannot buy out Federal employees—let us say you bought out 10 Federal employees, and you substituted 10 contracted out employees.

That would not be a downsizing of government. But it would not say that if, in fact, a Federal employee is bought out, that that employee couldn't shop around the Beltway to find other employment. I don't believe that we're at odds. My legislation would not bar any Federal employee from seeking——

Mr. MORAN. Good, I'm glad we've clarified that. And I think there may be some Federal managers who need that clarified as well; that that is not your intention. That is certainly appropriate and consistent with your intent that people who leave the Federal Government would be able to contract to the Federal Government.

Ms. NORTON. And remember what we said, we said you couldn't replace the people we had cashed out with new people. So if you can't replace them with new people coming into the civil service, you don't want to leave a loophole to replace them with bought out people.

Mr. MORAN. That's right.

Ms. NORTON. But the freedom of the individual to continue to earn a living in any way that person sees fit, I would fully endorse, as you indicate. And by the way, I think the previous witness—the chairman, I think, referred to this—as well talked about competition between Federal workers and workers on the outside. One of the things I'd like to see us do more of is something that the States and counties apparently are beginning to do more of. And that is, before they contract out, they essentially allow their own employees to bid as well, to compete with the private sector.

Now, that's one way to get people in the kind of competition that I think makes a lot of sense. And I do think that the lack of a bottom line in any bureaucracy, in any government, does make it harder to make it efficient. If in fact you say to government employees, look, we found we can do this cheaper on the outside; let's see what you have to say, I think you impart in a creative and, I think, legitimate way, some notion of competition that would make some sense.

And I think some experimentation of that kind in the Federal sector would be worth it.

Mr. MORAN. Thank you, Ms. Norton. Thank you, Mr. Chairman.

Mr. MICA. Again, I want to thank you for your testimony and your comments relating to the legislation you've introduced, and for your participation here today. We look forward to having you work with our subcommittee because we have some tough chores and tasks ahead, and you can be a valuable part of and contributor to that process. So thank you so much for being with us.

Ms. NORTON. Thank you, Mr. Chairman.

Mr. MICA. Now I would like to call our next panel forward. We have Gary Engebretson, who's president of Contract Services Association; Bert Concklin, president of Professional Services Council;

and Mr. Robert Tobias, the national president of the National Treasury Employees' Union. Gentlemen, if you wouldn't mind, it's the custom of the subcommittee to swear in our witnesses.

[Witnesses sworn.]

Mr. MICA. Welcome, I thank you for your patience. You've survived a rule vote, a very contentious previous question vote, and an unscheduled witness. And we look forward to your testimony before the subcommittee. I'm going to start with Gary Engebretson, president of Contract Services Association. Welcome, again.

STATEMENT OF GARY ENGEBRETSON, PRESIDENT, CONTRACT SERVICES ASSOCIATION; BERT CONCKLIN, PRESIDENT, PROFESSIONAL SERVICES COUNCIL; AND ROBERT TOBIAS, NATIONAL PRESIDENT, THE NATIONAL TREASURY EMPLOYEES' UNION

Mr. ENGEBRETSON. Mr. Chairman, thank you. Also I would like to say thank you to my Congressman, Congressman Moran. I live in his district, and so it's also interesting to be testifying before your own representative here at the committee. Mr. Chairman, members of the committee, my name is Gary Engebretson. I'm president of the Contract Service Association of America, the Nation's oldest association of government services contractors.

Our more than 200 member companies perform support services of all kinds, from basic maintenance to sophisticated technical operations, for most agencies of the Federal Government, as well as scores of State and local governments. Indeed, our industry is gratified that the issues surrounding privatization and contracting out are receiving such serious and close attention in the 104th Congress.

It is our hope that this attention and consideration will lead to the kind of assertive, forward-looking steps that will enable the government to fully realize the enormous benefits available through a well-run comprehensive program of contracting out government services. Let me first clarify the terms of this discussion. Indeed, the terms privatization and contracting out or outsourcing are often used as if they are synonymous; but they are not.

Privatization refers to the government divesting itself of basic control, and sometimes ownership, of an asset or a function. Contracting out, or outsourcing, is a relatively straightforward concept, whereby the government simply retains a private sector provider to perform the work, with all ownership and control remaining vested with the government.

Both of these concepts have been discussed with increasing frequency. But I'd like to limit my remarks today to the contracting out, since it is the more common. In discussing contracting out, three facts are clear: one, contracting out saves money. As the Wall Street Journal reported in April 1993, the government saves an average of 25 percent per year per contract. Two, the national interest is best served by an aggressive program of contracting out. Indeed, our entire economic system is built on the well-founded belief that a strong and dynamic private sector is the key to our Nation's economic vitality.

Thus, to the extent the government is performing commercial type services it is competing with the private sector in our Nation's

long-term best interests. Three, contracting out is a valuable management tool that plays an integral role in helping the government downsize and rightsize, without eliminating important services.

Thanks to the efforts of people like yourself, Mr. Chairman, and Congressmen John Duncan and Scott Klug and others, Congress appears to be ready to get serious about this issue. And we stand ready, of course, to work with you. I would like to offer a few specific and, we think, important recommendations that we hope will be included in any legislative initiatives you might pursue.

First, we recommend that a high-level commission be formed to review all Federal statutes and regulations to identify any obstacles to contracting out that may exist. The commission should also be charged with surveying the vast array of functions and services now performed by the government, and identifying those that are truly commercial in nature and should thus be contracted out. The potential savings are very significant.

Depending on which analysis one chooses to use, those savings could be anywhere from $12 billion to $36 billion over 5 years. Clearly, with savings of that magnitude, we can ill afford to be complacent. Second, Congress must repeal Section 5(g) of the Federal Workforce Restructuring Act of 1994. 5(g) requires that a cost comparison be conducted if the positions to be contracted will be counted toward the agency's share of the 272,000 FTE reduction mandated by the act.

The requirement is impractical, ill-conceived and outrageously costly. The manpower to comply with it simply doesn't exist, and the budget could never support compliance. This brings me to our third recommendation. It is time to recognize that the whole system of public-private cost comparisons is in need of substantial repair. Under OMB Circular A–76, a cost comparison process is established for use whenever a government entity contemplates converting to contract a function with more than 10 FTEs.

While the A–76 was designed as a means of protecting the interests of the Federal workers by providing them an opportunity to essentially bid against private contractors, the cost comparison process simply does not work. Government accounting systems do not allow the full accounting of all overhead and other indirect costs in a manner as comprehensive as required of the private sector. As such, the playing field is far from level, and it must be fixed.

To achieve that, we recommend that a complete independent analysis of current cost comparison methodologies be conducted. The goal will be to determine how those processes can be streamlined, adjusted to the account for real government costs, and utilized more fairly. Fourth, we must take steps to prevent the arbitrary refederalization of contracted work.

Not a day goes by, Mr. Chairman, that I do not get a call from a concerned company that has been informed by a customer that some of their contracted positions are being brought back in house. Under A–76, such refederalization is supposed to be preceded by a comprehensive cost comparison. But often, no such comparison is conducted. More importantly, if a contract is not performing adequately and an agency feels it could achieve greater savings than are currently being realized, that contract should be recompeted.

Let the marketplace, which in our industry is enormously competitive, do what it does best. Fifth, we must do more to assist Federal employees whose positions are affected by the decision to contract. All too often, we are told that contracting out leads to massive job loss, when the data simply doesn't support this myth. Talk to any one of our member companies, and they will tell you that they prefer to hire incumbent workforces because it saves training and relocation time and money.

As well, effective government employees have the right of first refusal on all positions available under a contract for work that is being converted. But some percentage of the workforce will be negatively affected. And they, frankly, deserve more retraining and replacement support from their agency than is currently available. Finally, let me offer a thought on the questions of the so-called dueling reports.

I'm often asked by Members of Congress why there seem to be so many reports offering so many disparate conclusions as to the effectiveness of contracting out. My answer is simple: the vast bulk of reports reach strikingly similar conclusions—contracting out works well, particularly where there is effective oversight and management of the contract by the government.

In many cases, the reports most often cited by opponents of contracting actually bolster our contention that the record is far better than the rhetoric. For instance, in 1990, the Department of Defense inspector general report was much heralded because it seemed to conclude that contracting out was costing the government more than it was saving. But a closer reading of the report made it clear that 90 percent of the contracts studied were successfully saving the government money—a remarkable rate of success for any government program.

And of those few that were not achieving cost savings, the reasons were mostly due to changes in the scope of work; the advent of new regulatory requirements; increases in the wage determinations; or other factors unrelated to contractor performance. This is precisely the same conclusion reached by the DOD inspector general in a report on cost growth commercial contracts, which was released just last week. And by the way, I have a copy Mr. Chairman, if you'd like to have it.

Likewise, the OMB SWAT team report of a couple of years ago focused on the need of better government management of its contracts and more consistent application of cost rules. The report specifically found no evidence of widespread contractor fraud or abuse. In short, the report identified weaknesses, but was hardly a chilling indictment of contracting. Simply put, as elsewhere in life, one must always read the fine print and not rely solely on the stated conclusions or sensational headlines.

Mr. Chairman, we have an extraordinary opportunity before us. In the spirit of change that today so predominates not only on Capitol Hill, but across the Nation, I urge you to push forward and not let this opportunity pass. My thanks for your time and attention, and I will be happy to have any questions that you may have.

[The prepared statement of Mr. Engebretson follows:]

PREPARED STATEMENT OF GARY D. ENGEBRETSON, PRESIDENT, CONTRACT SERVICES ASSOCIATION OF AMERICA

Mr. Chairman, Members of the Committee. My name is Gary Engebretson and I am the President of the Contract Services Association of America, the nation's oldest association of government service contractors. Our more than 200 member companies perform support services of all kinds—from basic maintenance to sophisticated technical functions—for virtually every agency of the federal government as well as scores of state and local government entities.

I am pleased to be here and greatly appreciate the committee's interest in contracting-out. Indeed, as an industry we are gratified that the issue is receiving such serious attention in the 104th Congress, and we are hopeful that this Congress will take the kind of positive and assertive steps forward that will enable the government to reap the many rewards available through a well run, comprehensive program of contracting government services.

DEFINITIONS

Let me start by clarifying some of the terms of discussion and debate. The terms privatization and contracting-out or outsourcing are being used more frequently now than ever before, sometimes as if they are synonymous . . . but they are not.

When we speak of outsourcing or contracting-out, we are speaking of a procedure whereby the government contracts with a private entity to provide services that would otherwise be performed by government personnel. In such cases, all control and ownership remains with the government.

When we speak of privatization, we are typically speaking of a process by which the government divests itself of basic control—and sometimes ownership—of an asset or function, effectively turning that asset over to the private sector through any one of a number of methods.

I know there is much discussion in the Congress today of privatizing some government functions—the FAA, Postal Service, and more. I, however, would like to focus my comments on contracting-out, since it is the more common of the two.

CONTRACTING-OUT

In discussing contracting out, or outsourcing, three facts stand out:

One, contracting out saves money. As the Wall Street Journal reported in 1993, despite all the overblown reports alleging malfeasance and scandal, the reality is that the government saves an average of 25% per contract over the cost of in-house performance.

Does that mean that all contracts save money? Of course not. As in any business venture, there are failures. But by and large, when all is said and done, the government's contracting out program saves real money.

Two, the nation is best served by an aggressive program of contracting out. Indeed, our entire economic system is built on the well-founded belief that a strong and dynamic private sector is the key to our nation's economic vitality. Thus, to the extent the government is performing commercial-type services, for which there is a competitive, private marketplace, it is competing with the private sector and, even more significantly, with our nation's best interests.

Three, contracting-out should not be viewed as a necessary evil, but, rather, as a valuable and positive management tool that plays an integral role in helping the government downsize and rightsize in the most reasonable and efficient manner . . . and without eliminating important services.

Without contracting as an option, current budgetary and FTE pressures would undoubtedly be worse. I think we all recognize the importance of bringing the size and cost of government under control, as painful as it may be. And contracting-out is vital to our ability to do so.

This is not a simple issue. It has many dimensions. But in November, the American people expressed quite clearly their distress with the system as it now exists. And polls continue to show that the real reinvention of government is a high priority with the American people and an issue with real resonance beyond the beltway.

This is a message that state and local governments have received and are taking seriously. Today, the state and local government service contracting market can be measured in tens of billions of dollars; most experts predict that within ten years it will be measured in the trillions.

It is a message that corporate America has also received and taken seriously. All across the nation, companies are looking carefully at what they do, and what they need to do, and outsourcing an ever increasing amount of their support functions. The most innovative and successful companies have made a decision to stay out of

functional areas that are not vital for the company to perform, and to concentrate instead on those things that are genuinely central to the company's business.

Now it also appears that Congress is taking seriously that same message. Thanks to the efforts of people like yourself Mr. Chairman, Congressman John Duncan, author of HR 28, and Congressman Scott Klug, this issue is achieving a prominence that just a year ago was unthinkable.

RECOMMENDATIONS

In order to ensure that we don't miss the opportunity before us, I would like to make a few specific recommendations that we hope will be included in any legislative initiatives that might emerge from these hearings.

First, we recommend that the Congress create a high-level, independent commission to conduct a full and comprehensive review of all federal statutes and regulations that could be standing in the way of progress on the contracting-out front. Such obstacles would include the obvious—such as statutory prohibitions on contracting for firefighting and guard services—and the less obvious, such as FTE floors, unfair or unworkable competitive requirements, etc. Such an audit, if properly conducted, would go a long way toward identifying additional specific steps the Congress needs to take to enable the kind of management changes and innovations that are necessary.

Today, the government contracts for a substantial amount of services; but we have only scratched the surface. For example, the Office of Management and Budget estimates that there are some 250,000 FTE that could be considered for possible contract. At an average annual savings of $10,000 per position—also an OMB figure—that means the potential exists for $2.5 billion in savings per year . . . or more than $12 billion over five years. It should be noted, however, that other comprehensive reports, including the Grace Commission, placed the number of FTE that should be contracted at nearly 750,000, meaning the savings could be as high as $30 billion or more over five years.

Clearly, where savings of that magnitude are concerned, we cannot afford to be complacent. As such, the commission should also be charged with surveying the vast array of functions and services now performed by the government and identifying, perhaps by general category, those that are truly commercial in nature and should thus be contracted out.

Second, Congress must repeal Section 5(g) of the Federal Workforce Restructuring Act of 1994. Section 5 (g) requires that whenever a government manager wants to consider contracting out an existing government function, a cost comparison study must be conducted. Section 5(g) was conceived and passed as a means of preventing additional contracting out. It represents a wholly impractical, outrageously costly, and totally ineffective approach to efficient management and must be removed.

Third, it is time to recognize that our whole system of public-private competition is in need of substantial repair. As many of you know, the contracting of recurring government services is principally covered by OMB Circular A–76, which establishes a process of cost comparisons and management studies designed to justify—or not—the conversion of existing functions to contract.

A–76 was designed specifically to enhance the rights and opportunities available to existing federal workers. Indeed, the system established under A–76 allows the existing workforce an opportunity to propose a new, maximally efficient approach to its functions—known as the Most Efficient Organization, or MEO—which, in the end, effectively serves as the government's bid, if proposals are eventually solicited from the private sector. In such cases, the winning private sector offeror must beat the government's bid by 10%.

Unlike proposals from the private sector, MEOs are not subjected to any of the past performance or other subjective, historical data that are considered so vital in the evaluation of private sector bids. Moreover, the costs included in the MEOs are based on a government accounting system that is functionally incapable of accounting for all costs, particularly indirect costs such as management salaries, capital and overhead. On the other hand, private sector bids must include all such direct and indirect costs.

The playing field, in short, is wildly tilted away from the private sector. In the past there has been little interest in leveling it—primarily because the private sector still wins close to half of all A–76 competitions. That apparently fair balance has served to dilute any interest in making the kind of changes that will at least improve the playing field. We think that attitude must change.

Furthermore, in those instances where the decision is made to retain the work in-house, there is rarely, if ever, a follow-up audit to ensure that the government is managing to the MEO. Considering that the average MEO study recommends a

personnel reduction of roughly 15%, the failure of the government to manage to the MEO represents an extraordinary cost to the taxpayer.

With all that in mind, we believe the time has come to revisit the whole question of cost comparisons and public-private competitions. We recognize that such competitions will not be entirely eliminated, but believe they should be strictly limited to those few functions that fall into a gray area in that they are not entirely commercial but nor are they "inherently governmental." In no other cases are such public-private competitions justified, particularly in light of the inherent flaws in the current cost comparison processes.

Additionally, we recommend that a credible, high-level outside resource, either the commission I spoke of earlier or a major business school, be tapped by Congress to study the broad issue of public private cost comparisons, and develop a system that will create a streamlined cost comparison process and make the appropriate adjustments to government cost estimates to make them fairer and more accurate.

Fourth, it is time to stop allowing agencies to refederalize contracted work without any justification for doing so. Mr. Chairman, not a day goes by that I do not get a call from a member company informing me of yet another case in which the company has been informed that the contracting activity is terminating some or all of the positions covered by a contract, and bringing the work done by those positions back in-house.

Under the A–76 process, all refederalization decisions are supposed to be accompanied by a cost comparison, to justify removing work from the private sector—the backbone of our economy—and returning it to the public sector—the size of which we all agree needs to be reduced. But A–76 is only a circular, it does not have the power of law, and it must be specifically enforced by OMB whenever such cases arise. Therefore, we ask that if you develop legislation dealing with the broad question of contracting-out, you include in it provisions to guard against such arbitrary actions.

Fifth, we believe more needs to be done to assist federal workers who might be affected by a decision to contract. All too often we hear the refrain that contracting-out is the cause of massive job loss. Yet the evidence is quite to the contrary. According to figures offered by OMB over the years, less than 5% of the workers affected by a decision to contract end up involuntarily unemployed. Most go to work for the contractor, while most others take other positions in the government, opt for private sector opportunities, or retire.

Yet despite the reality, the federal employee unions have done a very effective job of convincing many people that contracting-out is a jobs issue.

It is not.

Let's be honest about it. All federal workers whose positions are converted to contract have the right of first refusal for all jobs with the contractor. As well, most contractors want to hire qualified members of the existing workforce because it would be senseless to go to the trouble of training and bringing in a whole new workforce. Moreover, despite the sensational allegations that contractors pay unfairly low wages and no benefits, the fact remains that on most service contracts the Department of Labor, using prevailing, local wage data, tells contractors how much they must pay for each position, what benefits must be offered and so forth.

Nonetheless, it is not a painless process. Some existing employees are adversely affected by a decision to contract. To help those employees, we recommend that the government develop a more aggressive and effective retraining and re-placement service. The costs of such a program pale in comparison to both the savings available from contracting and what might be the costs associated with an individual receiving public assistance. As a matter of fact, it might make sense to fund such an effort out of the anticipated savings from contracting—the amount, as I said, would be miniscule, compared to the savings, if the government were to take the kind of serious steps we recommend.

Bringing government under control, reducing its cost and size, and enhancing its efficiency will, unavoidably result in reductions in personnel. That is, of course, already happening.

But as we seek to continue that process, and make further, important progress, we can and we must also preserve the rights, and address the needs, of the hard working federal employees who, through no fault of their own, happen to be caught in a system that simply doesn't work.

Finally, let me close with a comment or two on the ever-present issue of "dueling reports". Many Members of Congress have asked me why there seem to be so many conflicting reports in government about the success of contracting out . . . with some singing its praises and others purporting to show contracting doesn't work.

The short answer is that there are not actually that many conflicting reports. While most reports cited by the opponents of contracting may identify weaknesses

or problems in the system, the reports often bear little resemblance to the rhetoric that is used to describe them.

For example, in 1990, the Department of Defense Inspector General released a report which, according to opponents of contracting out, proved that contracting was costing the government more than it was saving.

However, a close reading of the report revealed two critical, and unassailable facts: over 90% of the contracts studied were saving money—an extraordinary success rate for any government program; and where money was not being saved, the reasons almost always had to do with changes in the scope of work, changes in the Department of Labor wage determinations, new regulations, particularly in the environmental arena, and more—none of which were related to contractor performance and almost all of which would have had a virtually identical impact were the work being performed in-house.

In another case, the Office of Management and Budget released what it called its SWAT Team report on service contracting. Opponents of contracting were quick to jump on the report as further evidence of the insidious nature of contracting. But what, in the final analysis, were the key findings of the report?

The oversight and management of some service contracts was inadequate; the rules governing allowable costs were unclear and often inconsistently applied; and there is no evidence of widespread fraud and abuse by contractors.

Certainly, the SWAT Team report identified problem areas that must be addressed—primarily, it must be pointed out, on the government side of the table. But it was hardly what one might call a chilling indictment of service contracting.

In addition, we must remember that GAO reports are routinely misrepresented by opponents of contracting. For instance, last year's report on advisory and assistance contracting, a small discreet segment of overall government service contracting, was hailed as a report on service contracting as a whole. GAO specifically stated that it did not draw any conclusions from its investigation, and even acknowledged that there are many instances in which such contracting is desirable—whether it is immediately cost effective or not. These facts were, unfortunately, largely lost.

Here, as in all aspects of life, a simple warning is warranted: read the fine print, because if you don't, you might be inappropriately swayed by the headlines which, all too often, offer less than the whole story.

CONCLUSION

Mr. Chairman, we have an extraordinary opportunity before us. It is an opportunity on which we can capitalize—much to the long term good of the nation's taxpayers, or one we can allow to pass without taking the aggressive and forward-looking action that is possible. In the spirit of change that today so predominates, not only on Capitol Hill but across the nation, I urge you to push forward and not let this opportunity pass.

My thanks for your attention and I will be happy to answer any questions you might have.

April 18, 1995

The Honorable John L. Mica, Chairman
Subcommittee on Civil Service
House Committee on Government Reform and Oversight
U.S. House of Representatives
336 Cannon House Office Building
Washington, D.C. 20515

DEAR CHAIRMAN MICA:

I first want to thank you on behalf of the members of the Contract Services Association of America (CSA) for the opportunity you provided me to testify before your subcommittee on April 5, 1995. I greatly appreciated the chance to outline for you and the other members of the subcommittee, the issues CSA, as the nation's oldest and largest association of government service contractors, have identified as those that will most impact our collective ability to enhance the efficiency—and reduce the cost—of providing government services.

I wanted also to take this opportunity to clarify and reiterate some of the key issues that were raised at the hearing. It is my hope that the hearing represented not an end, but a beginning, and that we, therefore, will have additional opportunities to discuss the many important aspects of the issue.

- Public/Private Competitions: Should government agencies compete with private contractors?

This is an issue that really has two, conflicting dimensions, both of which are important and fundamental to the discussion. As such it is important that both perspectives are understood, so that the most appropriate and workable solutions are found.

In short, there is the practical/political aspect to the question (to deny employees an opportunity to compete for the work could negatively impact employee morale, productivity and loyalty) and the sound policy aspect (whenever the government competes with the private sector, our broader national interest—the enhancement of a vibrant private, rather than public, sector is hurt). As you search for ways in which to address the issue in a manner that adequately deals with both points of view, I would like to offer a few observations:

1) When the unions talk about employees competing with the private sector, the implication is that if those employees lose the competition, or are denied the right to compete, they will lose their jobs. Yet the reality is that most contractors prefer to hire the existing workforce—be it government or that of the incumbent contractor—because doing so saves time and money that would have to be devoted to hiring and training a new workforce.

In addition, when a decision to contract a function is conducted via procedures established under OMB Circular A–76, the existing federal employees are given a right of first refusal for all available jobs with the contractor.

In other words, such competitions do not represent "win or lose" propositions for government employees—the system is designed in such a way as to protect their interests.

2) As I stated in my testimony, the current system of cost-comparisons is fundamentally flawed because the government accounting system is incapable of producing accurate cost estimates of in-house performance. The system simply does not allow for full accounting of all indirect costs—including capital and salaries. The net result is that the government is making "buy/no buy" decisions based on incomplete data, a problem which is clearly costing the taxpayers more than is warranted.

Thus, to the extent the government will continue to have cost comparison requirements, it is vital that we come to grips with the issue of how those comparisons can be improved and streamlined.

3) To the extent resources are being unnecessarily committed to "commercial activities" (i.e., those functions of government that are not "inherently governmental" and for which a competitive, private marketplace exists), the government's ability to more fully focus on its core responsibilities is affected. For instance, if, within the limited budgets available, the Border Patrol is doing work in-house (such as fleet maintenance, or information systems, or facilities management) that could be contracted to the private sector, there is less money (because we know that contracting saves an average of 25% per contract) available to put more officers to work patrolling borders.

- Removing Barriers to Efficient Management: Is legislation needed to encourage and incentivize additional contracting of government services?

CSA believes that the Congress can and should take the leadership role in removing all impediments to efficient and flexible management in the government, including removing all obstacles to contracting-out. This is not to say the Congress can or should pass legislation that would force a set amount of contracting to take place. Rather, it is to say that Congress can and should ensure that the system encourages and allows government managers to manage in the most efficient manner possible. This, unfortunately, is not the case today.

Specifically, CSA believes any effort to encourage the contracting of government services must include these elements:

1) Statutory limits on cost comparison studies (to the extent such comparisons are going to continue to be required or allowed) must be shortened from the current 24 months for a single function and 48 months for a multiple function, to 12 months and 24 months respectively. If such legislation is passed, and accompanied as well by a requirement that once studies are announced they proceed without interruption, we believe the process will become far more "user friendly".

As many GAO and other studies have indicated, a principal cause of the lack of aggressive conversion to contract of government services is the drawn out and costly study process. By limiting study times it will do a lot to improve the system and make it more acceptable to those government managers who must work within the process.

2) Address the cost comparison issue (as suggested above) through the authorization of a credible, independent resource (such as a major business school) to study the process and recommend 1) how a factoring or scoring formula might

be applied to government "bids" to make them more accurate and 2) how the process itself can be streamlined and made far more simple. This is a natural, and unavoidable, companion to the recommendation above (on limiting study times) and an issue that goes to the very heart of the whole debate.

3) Remove all direct and indirect barriers to contracting, including FTE floors, specifically special interest prohibitions (such as prohibiting the contracting of firefighting and guard services at DoD—services routinely contracted in other agencies).

4) Prohibit government agencies from competing with the private sector for work at other government agencies. As you may know, some government entities, such as arsenals, labs, military depots, etc., are allowed to compete with the private sector for similar workload at other agencies. Such policies are both unfair—since the government has a clear advantage competing against private providers—and contrary to the broad national interest.

Mr. Chairman, we are both appreciative and mindful of the leadership you are demonstrating on these important issues. I sincerely hope I, and my staff, will have additional opportunities to work with you and your staff, as the search continues for the most appropriate and effective means of achieving the goals we share.

My thanks once again for your time and attention and I will look forward to working with you to find ways to save the taxpayers dollars.

Sincerely,

GARY D. ENGEBRETSON.
President.

Mr. MICA. Mr. Engebretson, we thank you for your testimony. We'll turn now to Mr. Bert Concklin, president of the Professional Services Council.

Mr. CONCKLIN. Thank you very much, Mr. Chairman. And I want to mimic the preceding speaker, and also acknowledge my gratitude at being here in front of my Congressman, Congressman Moran. The Professional Services Council is a trade association which represents the high technology and professional services community and is, in fact, the second oldest trade association, to the preceding association, since we're in the business of denoting age today.

I am Bert Concklin. I'm the president of the association. And first of all, I'd like to commend the committee for your wisdom and courage in undertaking this most complex and controversial issue. And I mean that very, very sincerely. This is a decades-old issue which remains in a state of tension. Let me just say a word or two about professional services. Professional services are the fastest growing sector, many of the components in the two-digit growth range both in terms of sales and job creation, in the U.S. economy.

And it is, in fact, the dominant sector in generating a positive trade balance in a situation where we have a perennial net negative trade balance. Our assets are people. We do not manufacture physical things. We have people as our resources, and therefore we are, in many very fundamental respects, more sensitive to the development and the state of employment and everything else having to do with people as members of organizations who have very critical and challenging missions in today's competitive economy.

Our particular association represents approximately 300,000 people worldwide. The business constituted of that group of companies and employment is in the range of $23 to $25 billion annually. I want to speak very briefly to the value of contracting out. Contracting out has many attributes, but it has three key attributes which I think are noteworthy as you consider contracting out as a privatization strategy along with other potential strategies.

The first of these is expertise. The very nature of the competitive services economy today is one of constant churning, constant moving forward; particularly in the high technology areas such as information technology, environmental technology, health sciences and many other similar fundamental areas in the economy. In order to be successful in this most competitive business, all our firms have got to stay on the cutting edge so that they are practicing current technologies and current problem solving techniques that are world-class, in order to be competitive both in the national and in the international economic domains.

The second major attribute, which goes more to the heart of the tension between public and private sector balancing of responsibility, is flexibility. Contracting out offers close to 100 percent flexibility in the sense that you can hire a contractor; you can modulate the contractor's effort in terms of telling them to add people, reduce people or, in fact, discontinue effort because the mission or the function is no longer required.

I will not abuse you by conducting a lecture about the intractability of bureaucracies or public sector organizations. I've spent approximately 40 percent of my lifetime as a public sector employee. But it is very, very difficult, given the personnel rules as well as the organizational cultural aspects of big public sector organizations to match the kind of flexibility that is afforded by the private sector.

A third and final attribute is competition, which has been alluded to already in this hearing. And the answer there is very simple. Competition causes people to be efficient and effective; efficient in the sense of being economic and cost-effective because you have to do that in order to successfully compete for business, be it public sector or commercial or international; and effective in the sense of, if you don't do the work very well, your past performance is scored low and you simply don't continue to participate in that market.

I want to observe just in passing, having talked about those attributes, that we do not say that the private sector is perfect in every aspect. There have been instances where there have been problems with contracting out. My colleague alluded to the OMB study, the so-called SWAT team study. That was ostensibly, because there were problems with services contracting. But I want to echo what he said and repeat the notion that 90 or more percent of the printed findings and the associated activity focused on the government's contract management, not the behavior and conduct of the services contractors.

Shifting now to how to think about the contracting out issue in terms of the policy paradigm, or a strategic approach, we have not originated, but we have embraced what I think is the logical way to look at that equation. And it involves three steps, or three blocks, if you will. The first is, there is a range of activity that I think most intelligent people would agree is inherently governmental.

The OMB has published a policy document that very clearly sets out what is inherently governmental and, in fact, what is not inherently governmental, and some criteria in decision rules about how to navigate through that situation. The second part of that policy paradigm is poor capability.

There is no question that the government must have a minimum level of technical, management and administrative talent and skill in order to intelligently manage its affairs, including overseeing the range of external organizations—contracting out and nonprofits and all other players—in an effective way, given the government stewardship imperative that exists when you are a government manager.

Finally, the third piece of that paradigm is the contractors themselves. If you know what's inherently governmental; if you've taken prudent steps to make sure you have the core capability, then arguably everything else is subject or eligible for contracting out. And that is our basic thesis. We do not favor, at the Federal level, public-private competition.

We stay with first principles and say that the government should not be competing with the private sector. And in particular, the cost comparison methodology or cost comparison tool that's been used primarily in the A–76 world, is an analytically badly flawed tool that should not be used under any circumstances, even if the Congress and the executive branch decide to continue some form of public-private competition.

As with the preceding speaker, we would say that cost comparison methodology must be dramatically upgraded. It is simply not providing a level playing field in today's world. Specifically, it just does not faithfully recognize, other than very marginal elements of Federal Government overhead. So you can't get an apples-to-apples, valid, equitable comparison.

I'd like to suggest to you, or respectfully suggest that in looking at privatization as a public policy strategic issue, that you be cautious about forms of privatization other than direct contracting out, which has a proven track record and a high level of acceptability and satisfactory performance over time. We have seen emerge, within the administration and within certain quarters of the Congress, interest in government corporations; civil service; buyouts of organizations; schemes called franchising, and others.

Some of these may be appropriate to certain circumstances. Many are rather tenuous because they involve long-term underwriting or subsidization of markets for organizations like government corporations—the Amtrak type of situation—which incurs, for the government, long-term obligations and very uncertain situations, and never fixes the total responsibility and the liability for performance in a purely private sector organization.

Because government corporations, in particular, are half public and half private sector in their pathology, if you will. I don't want to overly repeat again what was said by previous speakers, but we are very concerned about the civil service workforce and the professional and morale aspects of how a privatization transition will impact them. We would urge you to consider prudent measures, of which there are many good candidates, to assure that that transition is humane, is professional, and is carefully managed.

And certainly one clear idea that has merit is to build concrete specific incentives into contracts that would award contractors who hire government employees and hire them in a reasonable way; and conversely, punish them if they are not forthcoming in that regard. The next issue is that of legislative impediments. I know

you've had submitted for the record and heard several already today. I won't overly digress into that, except to say that there are a number of them; they're perverse; they are narrow; and they're completely contrary to the freedom that a public sector policymaker and manager ought to have to manage their agency, irrespective to the degree to which they may ultimately privatize all or parts of that agency.

There is one aspect of government behavior that I want to allude to because, as was noted by a previous speaker, it's a disquieting development, and I think it needs to be dealt with. And that is that some government agencies are going the other way; that is, they are tending to in-source work or increase their Federal employee count by canceling ongoing and successful contracting out issues.

The best example of that is the Environmental Protection Agency, which has embarked on that in a very arbitrary and destructive way. They are in fact increasing their civil service population at the expense of long-term research and development contractors who have performed for them in distinguished fashion with no defensible rationale. And there are other manifestations which we can provide for you.

Finally, in terms of recommendations, we recommend three things. First of all, that the Congress pass an unequivocal law that affirms and endorses privatization as public policy which we want to take seriously and embark on and move down that path in a real way. Second, we recommend that either through a legislative impetus, or perhaps at the executive level, that there be created a self-perpetuating process, because the cultural resistance to privatization is more than obvious in the history of A–76 and similar enterprises.

And in thinking about such a self-perpetuating process, there are at least three ideas that we would commend to you. One is some variation, some careful variation, of what the Department of Defense has done with their Base Realignment and Closing Commission, which has a self-animating or self-perpetuating characteristic to it that has worked rather well. Second is, continued and judicious use of ceilings and reduction goals to provide stimulus to downsizing and right sizing.

And third is requiring all agencies—and this is only an example—but all agencies to include in their budget submission, and price in their budget submission each year, their top 10 privatization targets that they intend to effect in the next year or two or three. And finally, we would urge you to remove this cluster of statutory disincentives to privatization that's been well documented here today.

In summary, we think the Nation is on the threshold of a fundamental transformation in how we are thinking about and how we are acting on the balancing of responsibilities between the public and private sector, moving into a privatization era. The notion of limiting the doing functions of government to those things that are, in fact, inherently governmental we think is thoroughly sound and thoroughly feasible.

The ultimate result for all of us will be saving of money and improvement in performance. And we commend you for your thought-

ful examination of this issue, and thank you again for the chance to be here today.

[The prepared statement of Mr. Concklin follows:]

PREPARED STATEMENT OF BERT M. CONCKLIN, PRESIDENT, PROFESSIONAL SERVICES COUNCIL

On behalf of the Professional Services Council (PSC), I would like to express our appreciation for having the opportunity to testify today on the experiences of contracting out in the federal government. I am Bert Concklin, president of the Professional Services Council, a national trade association providing a policy voice for the technology services industry. Let me begin by commending this Committee's effort to seek a public policy which balances public and private sector resources. PSC's more than 135 companies and associations have direct interest in having continued opportunities to sell their expertise to the government. And in a global economy increasingly dominated by high technology and information systems, we believe the government has an equal interest in utilizing the evolving technology and expertise of the private sector for performing services to meet those challenges. We believe each sector has an important role and look forward to a more productive partnership, as those roles are understood better.

THE PROFESSIONAL SERVICES INDUSTRY

Let me take just a minute to describe the professional services industry. The industry can be described best by its employees, because in the services business, our people are our companies' assets. Our sector's products are ideas and problem-solving techniques, primarily in the form of specialized knowledge to assist customers in solving technical, management and operational problems. Professional services companies are made up of dedicated career professionals, who are proud to be working for practical solutions to government, commercial and international customers' problems. PSC members employ over 290,000 men and women across the country and around the world—computer scientists, research specialists, training professionals, physicists, engineers, quality control specialists, financial and accounting experts—specialists in their fields offering state-of-the-art solutions and innovative expertise to government and other customers.

Overall, the services industry has been one of few engines of growth and job creation throughout the 90s. Growing an estimated 10% per year, and employing over 6 million people. The services industry last year added a $4.9 billion surplus to the overall U.S. balance of trade, out performing goods by over $18 billion. Many of these export businesses started, and some continue, through contracting with the federal government.

ELEMENTS OF THE PSC TESTIMONY

1) Value of Contracting Out,
2) Outline of a Model for In-house Performance vs. Contracting Out,
3) Transitioning the Civil Service Workforce,
4) Legislative Impediments, and
5) Recommendations to Congress.

VALUE OF CONTRACTING OUT

Initiatives in rightsizing the federal workforce, deep cuts in agency budgets, National Performance Review and other reinventing government initiatives have created a need to explore alternate approaches in delivering federal government services. Now, the new Congress, through Subcommittees such as this one is taking an aggressive approach to bring about change to achieve more cost effective and efficient services for taxpayers dollars. PSC believes a balanced and well managed contracting out policy, which enables the government to capture the value of the country's services entrepreneurs, is essential.

The federal government has been engaged in successful contracting out throughout its history, with increased levels in recent decades. Early on the government understood the value of tapping into the resources at the private sector businesses, universities, and nonprofit organizations to supplement its own workforce. Let me outline the key features for success that make utilization of the private sector attractive. Among the many features, specialization and expertise, flexibility of workforce, and competition for contracts are the most distinctive.

Expertise. Services contractors provide specialization and expertise to government customers. Contractor skills are acquired typically through hands-on field experi-

ence, advanced academic preparation, and intensive on-the-job training. Areas such as systems management, operations research, engineering, training, and other business sciences are good examples of areas of specialization. Ongoing commercial as well as government projects enable a company to retain highly qualified personnel and state-of-the-art capabilities. These resources stand ready for the government to tap into as needed through contracting out.

Flexibillty. The government enjoys great flexibility by using services contractors. The government quickly can acquire or expand needed expertise, use it for a limited period of time, and then swiftly discontinue its use. The government only pays for the highly specialized service, while the service is needed. Instead of hiring a full-time workforce for tasks which may not be long term, contractor workers can supplement the workload peaks and when lulls occur, the contract can expire. This approach allows an agency to tailor workforce expenditures to their specific need, without carrying full-time cost burdens in times when there is less than full-time demand.

In the private sector, contracting out (commonly referred to as outsourcing) is a common practice which meets with great success. Whether calling upon accountants during a busy tax period or supplementing computer specialists as a network is being installed or adding help to support a major conference, the private sector adds to its efficiency with short-term help not carried on employee payrolls after projects are completed.

Utilization of the private sector also allows the government "technology flexibility." As technology focuses change, government managers cannot always redirect existing employees to focus on new technologies, due to civil service personnel rules and organizational rigidity. For example, if a DoE research scientist specializing in alternate fuel research is asked to make a minor change and transfer his focus to even another renewable energy technology, he cannot be required to make the shift. By contrast, it is commonplace for a contractor to respond instantaneously to the governments directive, shifting from one to another technology focus.

Competition. As the single most dominant factor in cost savings, competition brings market forces into play, where cost consciousness is rewarded and inefficiency punished. The federal procurement system is extremely competitive, demanding that services contractors compete against each other in order to win a contract. It is a rare occasion when a contractor is not in intense competition. As a result, competition provides cost containment pressures, allowing the government to obtain the best value for its dollars. Firms must be creative, value conscious, and cost competitive in order to win competitions in the federal marketplace.

Real-life examples of competition in today's market can yield millions of dollars in savings, as was the case recently in an army base operations and maintenance contract, when $1 million was saved through a recompetition. The incumbent company was forced to develop innovative approaches and lower cost solutions in order to win the contract again. The average profit margins for professional services are a low 2%–4%, illustrating the role of competition in maintaining low cost profiles to the taxpayer. In addition to cost savings, competition of ideas and solutions is occurring among professional services, allowing a government manager to choose from many ideas, not merely the ones developed inside the government.

In continuing value and success in the use of the private sector, PSC recognizes the importance of proper management and contract oversight. We sincerely believe that the majority of contracts are operating in a functional, value-added way. Occasional stories of abuse or mismanagement are heard, frequently resulting from inadequate contract management and lack of meaningful communication between the government and contractors, but they are the exception not the rule, and should be addressed appropriately.

BALANCED MODEL FOR CONTRACTING OUT

Despite the success found today in contracting out, there continues to be tension between the private sector and the government as to the amount of work and functions that should be performed in house by government employees or in the private sector by contractors.

Policy institutions, including The Procurement Roundtable, a nonprofit group of 40 former high-level acquisition officials, have advocated various conceptual approaches to the issue. The Procurement Roundtable argues that the very term "contracting out" is a misnomer, since it connotes or presumes that all functions "belong" to the government in the first place. The group maintains that such an assumption is inaccurate, and the "right" to performance should not be automatically accrued to the government. Therefore, they argue, the real issue is not whether a

function should be "contracted out," but whether the government can claim the issue to be inherently governmental.

In defining a model for contracting out, historically, PSC has taken the lead in promoting a framework involving a three-tiered approach for a meaningful public and private balance.

We believe the above model reflects the right solution to enhance the use of private companies and achieve the proper role of government. To date, the closest attempt to frame this public vs. private issue has been in OMB Circular A–76 and OFPP Policy Letter 92–1. Even with these existing regulatory policies, a well-executed contracting out plan is rarely undertaken at the top levels in government and maximum contracting out is not achieved. A Congressional mandate, to be used as a guideline for agencies and the private sector, is needed to display leadership and intent to an otherwise floundering policy.

[NOTE.—The model referred to can be found at end of statement.]

PUBLIC/PRIVATE COMPETITION

If the PSC model is applied, the issue of public/private competition is no longer a factor. Contracting out can be executed in a manner consistent with the views espoused by this Committee. Public/private competition is contrary to the first principle that the government should not compete against its taxpayers. This committee has rightfully asked the key question: if the public sector can compete for the work, is it an appropriate function for the government to be performing? We believe that the proper role for the government is not to compete against the private sector. Civil servants should be employed to carry out inherently governmental functions only.

Among the arguments for using the PSC model, inherent flaws in the government cost comparison methodology making public/private competition infeasible. One problem is in the governments ability to state its full costs, due to the "uniqueness" of their accounting system. In addition to not providing a level playing field, other problems exist in cost comparisons being used as the determinant in contracting out; they slow the process and ignore best value thrust. Many ask, how do we fix this problem and make it fair? For as long as I have followed this issue, this point has been raised, debated and brushed aside as too difficult. Only to have the issue raised again, debated again and dismissed again.

At this point in history, cost comparison studies have shown no serious professional credibility as a primary mechanism for determining whether or not to contract out. Rather, its use contributes to nonproductive political debate, and does nothing to stabilize and balance the public policy environment. PSC recommends refraining from conducting public/private competitions, instead adopt a framework for determining the appropriate role for government and optimal use of the private sector.

OTHER PRIVATIZATION SCHEMES

In moving to embrace the overall theme of privatization, of which contracting out is one option, we believe it is very important to keep foremost in our minds a series of qualifications. First, privatization is not a stand-alone solution. Alterations in government culture, infrastructure and tools are necessary to be successful. And second, contracting out is the most immediate high-payoff option in an effective privatization strategy. Other more exotic schemes such as public corporations, franchising, and civil service employee buyouts all entail significantly higher risks and greater degrees of continued government subsidization of markets and operating budgets, as illustrated by the Postal Service or Amtrak experiences.

TRANSITIONING THE CIVIL SERVICE WORKFORCE

Apprehensions within the civil service about contracting out are understandable. Companies are experiencing similar rightsizing, as they adjust to a new global economy. IBM is laying off tens of thousands employees and defense giant mergers have left thousands of scientists and technical professionals looking for jobs. Federal employees are not alone in facing the uncertainty about the future.

As in these cases and others, a similar transition can be expected in the civil service workforce. Many employees will find positions in the businesses taking over the functions previously performed in the government. While we do not have hard statistical data, PSC companies' workforces are made up of large percentages of civil servants, due to their knowledge of the federal marketplace. It is not unusual for the private sector to pick up 80%–100% of the workforce, when contracting out occurs. In one particular case, a services company took over mailroom functions, keeping 100% of the existing workforce, 80% of whom were minority employees.

According to GAO data, other federal employees will move to other agencies. Some may even start their own businesses, selling services to the government. Even with confidence that these natural transitions will occur, we believe government-wide mechanisms need to be developed in order to assure fairness and order as the workforce transitions.

In urging contractors to retain federal workers in areas where contractors will be used, PSC recommends that the government develop initiatives for offering contract incentives. For example, giving source selection points to the company with a plan for keeping existing employees or waiving regulatory requirements may provide positive incentives without producing disincentives that would result in effects contrary to those desired.

LEGISLATIVE IMPEDIMENTS TO CONTRACTING OUT

The committee asked that legislative barriers to contracting out be noted in this testimony, I have cited a few laws that have proven to cause negative effects on our PSC members.

The Federal Workforce Restructuring Act (P.L. 103–226), as you heard last week from GAO's witness, Steven Nye, can be cited as a contracting out prohibitor. The law prohibits an agency from using contractors to perform functions previously performed by a federal employee which was lost in personnel reductions.

The FY'95 DoD Authorization Act (P.L. 103–701, 10 USC 24101) requires a cost comparison be performed before entering into contracted advisory and assistance services (CAAS), if DoD has employees who can perform such work.

The so called 60–40 Rule applies to DoD Services Depots. Where Depots must perform 60% of their work with Depots employees, contracting out no more than 40% of total requirements to the private sector, as required in 10 USC 2466.

More than legislation prohibiting contracting out, the lack of statutory policy outlining the proper balance including a role for the private sector inhibits contracting out.

A growing phenomenon needs to mentioned as a deterrent to contracting out. As agencies have been budgeted less money for operating expenses, many companies have had fewer opportunities in the federal marketplace. Compounding the problem, companies have been experiencing a growth in competition from an "entrepreneurial" government. Frequently, agencies will market their services to other agencies, the same services done by tax-paying companies via competition. The transactions, which are frequently done by Interagency Agreements, has prevented private companies from proposing for new projects and even have forced them out of performing in traditional markets.

The Office of Personnel Management, for example, last year developed a brochure to outline the services they could provide to agencies for a fee including workforce restructuring services and labor management teambuilding consulting. In the Environmental Protection Agency, contractors were replaced by federal employees to maintain supplies in research labs and drive boats, not exactly functions inherently governmental in nature. The Department of Agriculture travels internationally at taxpayers' expense to seek work from international customers. This activity is in direct competition with a tax-paying U.S. small business, which pays for travel with company profits. DoD Depots are competing for maintenance and repair workloads of other agencies.

RECOMMENDATIONS

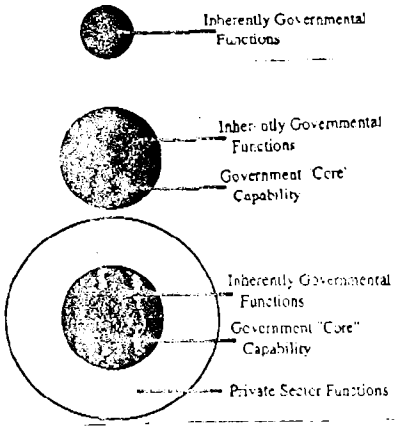
Statutory Policy—A statutory policy for contracting out with emphasis on using the private sector is needed. Without a law on the books and an emphasis for federal managers to use the private sector unless the services are inherently governmental, there is little incentive for the federal employees to make decisions to contracting out instead of performing in house. This is the single most critical factor for stimulating increased contracting out.

Self-Perpetuating Process—Three self-perpetuating processes for contracting out should be put into place: a privatization commission to recommend potential areas for private sector use, (2) continued federal personnel ceilings or reduction goals as a catalyst for more contracting out, and (3) a "top ten list" to be submitted to Congress annually identifying potential areas for contracting out.

Removal of legislative disincentives—The laws cited in this testimony and that of other witnesses should be repealed, so as to allow maximum flexibility in utilizing private sector resources.

SUMMARY OF THE CHALLENGE

In summary, we believe the nation is on the threshold of a fundamental transformation in how we think about and define the role of the federal government. Limiting governments "doing" functions to those which are truly inherently government, and systematically privatizing the rest, will yield profound benefits. The ultimate result: saving money and improving government performance. We urge you to get involved now by enacting into law an unequivocal commitment to privatization.



Inherently governmental function should be performed by government employees only.

As a subset of inherently governmental functions, the government must keep a "core capability." That is the technical, management, and administrative in house knowledge and skills to conceive, execute, and oversee contract activity.

All other functions should be contracted out to the private sector.

Mr. MICA. We thank you for your testimony, and at this time would like to call on a gentleman who is becoming a regular at our panel, Mr. Robert Tobias, president of the National Treasury Employees' Union. Welcome.

Mr. TOBIAS. Thank you, Mr. Chairman. I really appreciate your providing us with the opportunity to testify. I start with the proposition today that the public is entitled to full and fair competition between the employees of the Federal Government and the private sector, to determine who can produce the service at the least cost with the highest customer satisfaction.

Mr. MICA. You might want to pull the mic up just a little bit closer.

Mr. TOBIAS. Thank you. Maybe I'll repeat that, because I think it's important. I start with the proposition that the public is entitled to full and fair competition between the employees of the Federal Government and the private sector, to determine who can produce the service at the least cost with the highest customer satisfaction. I think it's the responsibility of Congress to create a comparison process between the private and government sector free of the erroneous predisposition that the private sector can do it better, faster, cheaper and so forth.

What we've been hearing today is, I think, kind of interesting so far—somehow that the national economy will benefit if we contract out work that's performed by Federal employees currently; or that the government ought enact a policy to eliminate Federal jobs and contract them out or privatize them.

But it seems to me that the issue for the public is not who performs it, but whether it's performed at the cheapest possible cost with the greatest customer satisfaction. So I believe that enacting a policy which contracts out jobs or eliminates services and gives them over to the private sector without knowing whether or not it would cost more would be very, very irresponsible. And especially in light of the reports that GAO has put out in the last 2 years, which reveal that the contracting out has cost the government significantly more than the work performed by Federal employees.

Second, it is the responsibility of Congress, I think, to require that a cost comparison is conducted every single time. Well over $12 billion—this is not nickels and dimes, but $12 billion in service contracts are not subjected to OMB Circular A–76; they're just done. They're gone; they're out there. We don't know whether they cost more, the same or less. There wasn't any competition there.

And finally, Congress must ensure that Federal agencies can bring work back in the Federal Government when the Federal Government can prove that it can do it cheaper. This is now very, very difficult because once the work goes out, the FTEs are lost and the work is performed outside no matter what the cost happens to be. It seems to me that Congress has to allow agencies to manage their resources and their products in a way that allows them to produce it at the least possible cost, rather than placing arbitrary caps on FTES, which often requires work to be performed no matter the cost.

The goal must be to shrink the government debt, not shrink the government. The idea that, in terms of rightsizing, we would eliminate 272,900 jobs and then substitute other private sector workers

to do that work, I think, is an inconsistent policy. We're not talking about small change in terms of what's contracted out. Mr. Koskinen testified last week that $108 billion was spent last year on contracted-for services.

Now, the average Federal employee pay and benefits are around $40,000 a year. Now, applying that to the $108 billion we pay to outside contractors, the government is supporting a 2.7 million workforce, or 700,000 more private sector employees than public sector employees. Rather than the predisposition to contract out, the available evidence indicates that the Federal employees are currently performing services at least at the same cost as the private sector, and probably cheaper.

I cite, for your information, a GAO report that came out in March 1994. And at page 23, I wish Mr. Cox was here so he could take a look at this, because what it does is to compare the contracted out work and the salaries that were paid to people who were performing that work and compared that to those who were doing the work before it was contracted out.

And for example, this was a DOE, Department of Energy report, and it showed a junior engineer being paid at $20.83, which included pay and benefits—$20.83 an hour—and the same person in the private sector was paid $48.44 an hour; and the senior engineer paid even more. So I think that there is ample evidence around that it is not automatically cheaper for work to be contracted out.

Now, after studying contracts over a period of years, GAO testified to this committee that "GAO cannot prove or disprove that the results of Federal agencies' A–76 decisions have been beneficial and cost-effective." Now, why would we willy nilly start contracting out when it can't be proved that it's going to be cheaper? And there's a great deal of evidence that the costs are not properly compared in advance; contracts are not adequately administered to monitor the costs or outcomes; and contractors arbitrarily increase costs in the out years of contracts because they know that the work cannot be taken back.

In report after report, GAO announces that the government pays too much to the private contractors. In the 1994 report I mentioned, GAO reviewed 9 contracts and found between 26 and 53 percent could have been saved, performing the same work using Federal employees. Now, we're not talking about marginal savings here, we're talking about real savings.

While it's true that the private sector has downsized and increased its efficiency in general, so has the Federal Government. I believe that if Congress requires fair cost comparisons when contracts are initially contemplated; requires those comparisons be done every time and at every renewal, you ensure that the public receives its product at the lowest possible cost. And I believe that the work will remain with the Federal workforce.

Thank you very much, Mr. Chairman.

[The prepared statement of Mr. Tobias follows:]

PREPARED STATEMENT OF ROBERT M. TOBIAS, NATIONAL PRESIDENT, NATIONAL TREASURY EMPLOYEES UNION

Mr. Chairman, Mr. Moran, Members of the Subcommittee, I am Robert Tobias, National President of the National Treasury Employees Union (NTEU). On behalf of the over 150,000 federal employees represented by NTEU, I appreciate the oppor-

tunity to present testimony today as the Subcommittee continues its examination of critical issues related to the Federal government's contracting-out practices.

Over the years there has been significant congressional inquiry into the federal government's contracting-out practices, as well as countless studies conducted by agency Inspector Generals, the Office of Management and Budget (OMB), the nonpartisan General Accounting Office (GAO) and others. Numerous reports continue to demonstrate that service contractor abuses can be found in virtually every federal agency that has been studied, sometimes resulting in massive cost overruns and inadequate performance. While the concept of the A–76 cost comparison analysis has been justifiably praised for imposing some needed safeguards, the process itself still holds some problems.

Mr. Chairman, this hearing is timely, and the issues being addressed here today are compelling. At the same time that agencies are being asked to downsize, the number of contractors doing business with the federal government and their costs are rising. A January 1994 OMB report entitled Summary Report of Agencies' Service Contracting Practices, reported that service contracts are the "fastest growing area of government procurement, accounting for $105 billion annually of the government's $200 billion FY 1992 procurement program." Moreover, the report states that from fiscal year 1989 to fiscal year 1992, the number of contractors doing business with the government rose from 62,819 to 82,472. In testimony before this Subcommittee last week, OMB Deputy Director for Management, John Koskinen, stated that in FY 1994 service contracts represented a total of approximately $108 billion. These statistics are especially alarming when one considers that some contracts may be initially awarded without any cost analysis. In its January 1994 report, OMB further stated that cost analyses and independent government cost estimates are not performed by many agencies prior to the renewal, extension, or even re-competition of existing contracts.

Mr. Chairman, federal employees and the methods by which they perform their work have undergone complete and thorough examinations in recent years as reinvention efforts attempt to bring the lessons of the private sector to public service. The loss of 272,900 jobs over the next five years represents only the most prominent of the "Reinventing Government" initiatives—federal employees have made numerous other sacrifices in order to meet deficit reduction goals, and they continue to adopt new ideas and techniques in pursuit of greater efficiency. Unfortunately, our contracting counterparts have yet to undergo such a thorough re-evaluation and the crisis in government contracting continues.

In order to alleviate this crisis and achieve the goal of a truly effective and efficient government, there must be an increased commitment by the federal government to make choices that best serve American taxpayers and service beneficiaries. By creating a level playing field that allows for genuine competition between contractors and federal employees, government can ensure that the best possible job is done and enhanced quality, economy, and productivity are achieved

As both the Congress and Administration explore ways to effectively streamline the functions and operations of Federal Agencies across the board, this important issue must be thoroughly examined and considered. As this process goes forward, federal employees on the front lines often know best how federal services are, or are not, delivered; and they are willing to work with Congress to ensure that agencies are required to make more fiscally-responsible decisions about service contracting. I am pleased to present to you today the views of NTEU's membership concerning the growing problems associated with service contracting and how they might be resolved through effective reform of the OMB Circular A–76 process.

OMB CIRCULAR NO. A–76: MAJOR ISSUES AND CRITICISMS

As you are aware, the Office of Management and Budget (OMB) Circular No. A–76 establishes the federal policy regarding the performance of commercial contracting activities. OMB defines a "commercial activity" as one which is operated by a federal executive agency and which provides a product or service which could be obtained from a commercial source. Performance of commercial government activities by outside contractors is subject to OMB Circular A–76, which requires a cost comparison of performing work in-house by government employees versus performing work by private contractors. The stated goal of the Circular is to "achieve economy and enhance productivity through competition." This is to be accomplished through comparing the costs of performing commercial activities in-house by Federal employees with the costs of obtaining the same services from private contractors, and selecting the most economical alternative. Before approving a conversion from in-house to contract performance on the basis of costs, OMB Circular No. A–76 has established cost margins which must be exceeded. The cost margin is equal to 10

percent of the government personnel-related costs and 25 percent of the acquisition of any new capital assets required to fulfill the task. Also, commercial activities of less than 10 Full Time Equivalents (FTE), research and development functions, and non-recurring activities are exempt from the cost comparison requirements of the circular.

In contrast, however, service contracts, including "advisory and assistance" (consulting) services which GAO estimates that the federal government spent almost $12 billion on in FY 1992[1], are subject to OMB Policy Letter No. 93–1 which provides detailed guidance on managing and controlling the use of service contracts including advisory and assistance contracts. Although the OMB Policy Letter No. 93–1 emphasizes cost-effectiveness and provides guidance on managing and controlling the use of service contracts, it does not specifically require agencies to develop a cost comparison between contractor and in-house performance.[2] GAO has reported that its analysis of studies by GAO, the Department of Energy and the Department of Defense suggest that cost comparisons can be a useful management tool for assisting government agencies in deciding how to acquire needed services in the most cost effective manner.[3] NTEU strongly believes that this sort of cost comparison and analysis is a critical element that should be explicitly indicated in the rules governing all service contracts.

While OMB Circular A–76 does in fact require agencies to conduct a cost analysis to determine the most cost effective approach for providing certain commercial services, agencies, unfortunately, often disregard this rule. In a January 1994 report entitled Summary Report of Agencies' Service Contracting Practices, OMB itself reported that cost analyses and independent government estimates are not performed by many agencies prior to renewal, extension, or recompetition of existing contracts. OMB further concedes that in far too many instances, cost estimates are not even prepared prior to entering into new contracts.

A common criticism of the A–76 program is that it is burdensome, time-consuming and complex. Depending on an agency's workload and financial accounting systems, the development of the historical data necessary to prepare a performance work statement may take considerable time and effort. At DOD the study time has nearly doubled to an average of more than four years since the late 1980's. During this process, employees do not know their future employment status and employee morale and productivity declines. In fact, the President's Council on Management Improvement reported that ". . . agencies believe that the A–76 savings do not compensate for the aggravation, loss of staff productivity, reduced staff morale and attrition that result from doing a study." The three step process requires a major investment of time and effort and relies heavily on the procurement process to complete. This presents the Subcommittee with yet another opportunity to improve on the current process.

Last month, the GAO released its latest report criticizing federal contracting out procedures. The February 1995 report entitled Defense Contract Management, aptly points out that contractors have a responsibility to support their shareholders by maximizing profits. GAO reports that "Serious DOD financial control weaknesses have resulted in large and numerous erroneous and in some cases, fraudulent payments to defense contractors. During a 6-month period in fiscal year 1993 defense contractors returned to the government $751 million, and in fiscal year 1994, they returned $975 million, most of which appears to have been overpayments that were detected by the contractors." The report further states that weaknesses in contractor procedures for identifying and excluding unallowable costs from overhead submissions have contributed to DOD inappropriately reimbursing contractors for unallowable overhead costs. During fiscal year 1991–1993, DOD auditors questioned about $3 billion in contractors' overhead charges.

It is clearly the responsibility of the Congress to properly protect the government's and taxpayers' interests, and this responsibility demands a thorough review by this Committee of the federal dollars spent on contracting out of federal services that can be accomplished at less expense by federal workers. The current emphasis on acquisition reform and the recently passed Federal Acquisition Streamlining Act of 1994 are positive steps toward strengthening the acquisition system. However, as the above referenced GAO report states, these actions can be successful only by ensuring the integrity and fairness of the procurement and contracting process.

Lax management and ineffective oversight of contracts also continues to plague many federal agencies. As a result, contractors are receiving bonuses for mediocre

[1] GAO, GOVERNMENT CONTRACTORS: Measuring Costs of Service Contractors Versus Federal Employees (GAO/GGD–94–95) (March 1994) p. 1.
[2] Ibid. p. 2.
[3] Ibid.

performance and are charging the federal government for millions of dollars in costs, such as employee parties, tickets to sporting events, and alcoholic beverages, that are either unallowable or questionable.[4] These and other federal contracting out costs represent a black hole that this body has an important obligation to review.

Contract oversight clearly represents another key area desperately in need of reform as efforts to streamline federal expenditures and eliminate instances of waste and fraud go forward in this Subcommittee. Concerns have continuously been raised about contract oversight, especially since once a function goes to contract there is little oversight on the contractor's performance or cost overruns. In testimony entitled "Federal Contracting—Cost-effective Contract Management Requires Sustained Commitment" (GAO/T–RCED–93–2), GAO concludes the following:

> With the budget deficit and other financial commitments that the federal government faces, it cannot afford to ignore the potential cost of poor contractor oversight. For many years federal agencies have increasingly relied on contractors to carry out needed activities. Unfortunately, in all too many instances, federal agencies have abdicated to their contractors the responsibility for ensuring that contractors perform quality work cost effectively.

Unfortunately, service contracting personnel continue to concentrate their efforts on the awarding of contracts and the obligation of funds, however the equally important oversight of contractor performance often becomes a peripheral concern. NTEU supports GAO's recommendation that senior agency managers must be made accountable for contract administration.[5] Contract administration becomes one of the costs of doing business with contractors, and it should therefore be included in any cost comparison analyses.

Furthermore, in the absence of healthy competition, the incentives necessary for a contractor to provide timely and effective service are greatly diminished. Having established a monopoly, the contractor is often able to demand a larger fee the second or third time around when a contract comes up for renewal. By then, however, the federal government's own bargaining power is greatly reduced since the employees who once performed that particular service have long since been separated or dispersed and their valuable expertise lost. Often, more efficient ways of delivering services can be developed over time. If a service contractor knows that his or her contract will be renewed without further review, the federal government loses the competitive edge and the incentive for that contractor to reduce or eliminate the unnecessary expenses he or she charges to the federal government. NTEU strongly believes that contracts should not be automatically renewed in this manner. In addition to improving contract management as I have suggested, agencies should also conscientiously audit the work of their contractors to ensure that the government pays no more than it should for the services it receives.

In the March 1994 GAO report entitled, Measuring Costs of Advisors and Assistance Service Contractors Versus Federal Employees, the GAO found that the federal government could save millions of dollars by performing functions directly rather than allowing them to be performed by private contractors. GAO reviewed nine previous studies comparing the cost of using contractors rather than federal employees to perform necessary government functions. The findings were alarming. For example, an audit of Air Force service contracts disclosed that the Air Force paid $4.7 million in additional costs for certain contractor work in fiscal year 1990, and could have saved up to $6.2 million if the work to be performed under the optional years of the contracts reviewed were performed in-house.[6] A Department Of Defense (DOD) Inspector General report on certain consulting services contracts estimated that DOD agencies could save about $26 million from fiscal years 1992 to 1996, by gradually reducing their service contracts by 60 percent. The report further estimated that contracting costs were between 21 and 40 percent higher than in-house performance.[7] Another study of 11 Department of Energy (DOE) service contracts estimated that that Department could have achieved savings ranging from 3.1 to 55.4 percent, with an average of 25.4 percent if the work were done in-house.[8]

---

[4] GAO, FEDERAL CONTRACTING: Cost-effective Contract Management Requires Sustained Commitment (GAO/T–RCED–93–2) (December 1992), p. 1.

[5] GAO, FEDERAL CONTRACTING: Cost-Effective Management Requires Sustained Commitment (GAO/T–RCED–93–2) (December 1992), p. 13. "The persistence of contract management problems and the inattention to contracting audits indicate a need for top agency managers to intervene, raise the level of concern throughout the agency and see issues through to resolution."

[6] GAO, GOVERNMENT CONTRACTORS: Measuring Costs of Service Contractors Versus Federal Employees (GAO/GGD–94–95) (March 1994) p. 26.

[7] Ibid. p. 25.

[8] Ibid. p. 24.

In these times of fiscal constraint, it is simply unconscionable for the government to waste money in this manner. This is more troubling when it becomes apparent that if service contracts were subject to the cost analyses in Circular A–76, this money would not have been wasted. The March 1994 GAO Report cited above recognized this point, and specifically recommended that OMB extend the A–76 cost comparison requirement to advisory and assistance services. NTEU supports this position.

NTEU strongly believes that subjecting service contracts to Circular A–76 would address a major shortcoming in the contracting process. However, some agencies report that even when they are able to demonstrate through studies that it would be less expensive to perform the work in-house rather than contract it out, they are not authorized to hire additional government personnel.[9] Apparently, although there is no room in their personnel budgets, there is plenty of room in procurement budgets to accomplish the work. "Agencies often assume that additional government personnel will not be authorized and, therefore, there is no alternative but to contract for needed services. Several agencies requested that they be given more flexibility with respect to determining whether work should be performed by agency or contractor staff. Examples were reported where the government (based on the agencies projections) could save several millions of dollars by performing functions directly rather than having them performed by contract."[10]

It is ironic to note that even tighter restrictions on hiring federal workers are in fact leading to what has been shown to be more expensive contracting out of services. Strict FTE caps should not be manipulated to justify increased contracting out of services. Under this scenario, reinvention would be limited to a ledger paper change—the procurement column having a far larger debit and the FTE column indicating a decrease in government employees.

OMB should review the cost effectiveness of bringing contracted work in-house when there aren't sufficient FTEs to perform the work. NTEU recommends that the Committee seriously consider the fact that more flexibility with the budget limitation on FTEs is necessary when it can be demonstrated through studies that it would be less expensive to perform the work in-house but government personnel ceilings prevent that decision. Only when it is clearly understood what work an agency is to perform can the appropriate level of staffing be realistically determined. Unfortunately, however, FTE downsizing requirements continue to be driven without this critical evaluation or an appropriate assessment of the types of employees and the appropriate number needed to provide essential services in an efficient and effective manner. NTEU strongly believes that agencies should be given the flexibility to use their budgetary resources so that funding for contracting-out purposes could be used to hire additional FTE if a cost analysis indicates that it would be more efficient to conduct a particular service in-house.

NTEU is also concerned that again because of agency personnel ceilings, once a function goes to a contractor it cannot be converted back to in-house because of FTE ceilings. In testimony last October before the Civil Service Subcommittee of the House Post Office and Civil Service Committee, GAO stated: "GAO believes that agencies should have the flexibility to accomplish their work in the best possible manner and should not be constrained by arbitrary personnel ceilings, which could be counter productive and inefficient in certain circumstances. Agencies should determine if contracting out for services or using government employees is more advantageous. To make the best decision for the government, agencies need information that permits managers to make meaningful decisions. Cost comparisons and consideration of non cost factors can provide such needed information."

As the government attempts to reinvent itself, it will become even more important that contracting out of government functions also be used only when truly shown to be more cost effective. As agencies attempt to downsize and offer employees incentives to leave federal service, they should not be allowed to then contract out the work of the former employee. Under current A–76 procedures, a cost comparison is required for functions of 10 or more FTE. However, Section 5(g) of the Federal Workforce Restructuring Act requires the President to take appropriate action to ensure that agencies do not convert the work of employees included in the proposed 272,900 FTE reduction target or of employees who accept buyouts to contract performance, unless a cost comparison demonstrates a financial advantage to the government. Therefore, if one FTE is identified for contracting out, a cost comparison must be conducted. This important provision should be maintained.

Without appropriate service contract reform, downsizing is likely to continue to lead to an increase, not a decrease in federal spending. In view of the current tide

[9] OMB, Summary Report of Agencies' Service Contracting Practices, (January 1994), p. V.
[10] Ibid.

of deregulation, NTEU is concerned that efforts may be made to amend section 5(g) to require performance of cost comparisons for functions of 50 or more FTEs. Agencies would be allowed to go directly to contract, avoiding a cost comparison, for functions of 49 or fewer FTE. This approach is contrary to the recommendations of NPR and the GAO, and would lead to widespread contracting to avoid personnel ceilings.

OMB Circular A–76 specifically prohibits the contracting out of "inherently governmental" services. Such services were subsequently defined as "those which are so intimately related to the public interest as to mandate performance by government employees." Concerns have been raised for many years about what constitutes an "inherently governmental" function. Senator David Pryor (D–AR), the former chairman of the Senate Subcommittee on Federal Services, Post Office and Civil Service, once questioned the use of contractors and consultants performing certain government functions and referred to them as "the Shadow Government." Senator Pryor cited instances where contractors/consultants have prepared Congressional testimony; drafted memos for the signature of top agency officials; researched Freedom of Information requests; drafted internal agreements; and written agency regulations.

In response to the Senator's request for a GAO investigation of this matter, the GAO found that some service contractors appear to be administering governmental functions. The report, entitled Government Contractors—Are Service Contractors Performing Inherently Governmental Functions? further stated that: "The major reasons contributing to agencies use of contractors to administer functions that may be governmental in nature are the lack of authorized federal positions for employees or the lack of federal employees with sufficient expertise to do the work."

OMB's Office of Federal Procurement Policy subsequently issued a policy letter in 1992 giving guidance on functions which must be performed by government officials and employees and what kinds of functions may be performed by private contractors. The letter indicated that OMB firmly believes that agencies need 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 the agencies." NTEU strongly supports this position.

NTEU also believes that non cost factors also need to be considered when deciding whether to contract out. The GAO report entitled Government Contractors—Measuring Costs of Service Contractors Versus Federal Employees (GAO/GGD–94–95) states the following:

> For a cost comparison of contracting out versus using federal employees to be a useful management tool for agency decision makers, OMB also needs to consider other non cost factors. These include the difference between the quality of services offered by federal versus contractor employees; the timeliness of services available; the availability of federal employees to do the work; the value of flexibility in responding to variable work requirements; and whether the services needed are short-term, nonrecurring in nature, or of a longer term.

NTEU supports this position.

If there is to be any true reinvention of the federal government through downsizing and other reorganization efforts, NTEU views reforms in the current contracting-out process as a necessary step toward achieving that goal. As federal employees continue to make sacrifices to bring about improvements in the effectiveness and efficiency of service delivery, the Congress ought to be fully aware of the exact nature of the "shadow government" of federal service contractors. It is only fair that they too follow the example of federal employees by shouldering their fair share of the burden of deficit reduction as well.

FEDERAL EMPLOYEE PROTECTIONS:

In the Subcommittee's March 29, 1995, letter of invitation, you specifically requested that my testimony include "a discussion of protections provided for federal employees displaced as a result of contracting decisions, including any guarantees related to wages, benefits and/or working conditions provided by law." In addition to those protections addressed earlier in my testimony, I wish to highlight the following:

The "Policy Implementation" supplement to OMB Circular No. A–76, Chapter 3, page I–18 states the following with regard to "Personnel Considerations":

1. Adversely affected Federal employees are employees identified for release from their competitive level by an agency in accordance with 5 CFR Part 351 and Chapter 35 of Title 5, United States Code, as a direct result of a decision to convert a Government commercial activity to contract performance.

2 Agencies shall exert maximum effort to find available positions for adversely affected employees including:

a. Giving them priority consideration for available positions within the agency;
b. Establishing a Reemployment Priority List and a Positive Placement Program;
c. Paying reasonable costs for training and relocation which contribute directly to placement;
d. Coordinating with:
(1) The Office of Personnel Management to ensure adversely affected employees have access to Government-wide placement programs, including the OPM-operated Displaced Employee Program (DEP) and the Interagency Placement Assistance Program (IPAP); and
(2) The Department of Labor on private sector job opportunities; and
e. Consistent with post employment restrictions, advising adversely affected employees that they have the right of first refusal for employment on the contract in positions for which they are qualified and assisting them in applying for such employment.
3. Agencies should notify affected employees as soon as possible of an impending cost comparison study and periodically keep them informed of its progress.
4. Guidance on employer-employee relationships and other personnel matters that affect Federal employees involved in contracting situations can be obtained from the Office of Personnel Management.

While the above mentioned "right of first refusal" is indeed a positive element included in the Circular, it still provides no real guarantees to federal employees likely to be displaced when an agency decides to contract out a particular government service. In testimony before this Subcommittee last week, GAO Director of Planning and Reporting, L. Nye Stevens states that although GAO had not done any recent work on the question of what happens to displaced federal workers under the A–76 program, several studies conducted in the 1980's may provide the following insight:

> "For example, in a 1985 report on the program's impact in DOD, we found that the majority of federal workers whose jobs had been contracted out obtained other federal employment, most often at the same installation. We found that of 2,535 DOD employees we sampled who worked in activities that were contracted out in fiscal year 1983, 74 percent had found other government jobs, most often at the same installation; 7 percent went to work for the contractor; 5 percent were involuntarily separated; and most of the remaining 14 percent resigned or retired. Of those who obtained other government positions, about 56 percent received lower grades, and about 44 percent received the same or higher grades."

Subsequent GAO follow-up with those employees who had been involuntarily separated or went to work with contractors revealed that over half were reemployed with the federal government; over half indicated that they had received unemployment compensation and/or public assistance; and 53 percent who went to work for contractors said that they received lower wages, with most reporting that contractor benefits were not as good as their government benefits.[11]

It is critical to note, as GAO does, that the current downsizing environment may not provide the same opportunities for displaced federal employees to find employment in another government job.[12] This point is further illustrated by GAO's review of OPM's interagency placement program established to assist separated employees. "According to OPM, between the program's inception in December 1993 and September 16, 1994, from an inventory of 2,018 registrants, agencies made 204 job offers. Among other things, OPM attributes the low number to the fact that agency downsizing has substantially reduced the number of vacancies.[13]

Under Circular A–76, federal employees also have a right to appeal to their agency within 15 days of the contract announcement. NTEU has long been concerned that 15 days is by no means sufficient time for a local union to use its limited resources to try to put together an adequate appeal package. The procedure does not authorize an appeal outside the agency or a judicial review.

Section 7(c)(6) of OMB Circular A–76 which functions as an additional safeguard against cost-inefficient service contracting decisions, also serves as an employee protection. The provision prohibits the conversion of in-house functions to contract, "solely to avoid personnel ceilings or salary limitations." In the past, unions have used collective bargaining grievance procedures to report such violations. However, a recent court decision held that a union could only raise Section 7(c)(6) violations

---

[11] GAO, GOVERNMENT CONTRACTORS: An Overview of the Federal Contracting-Out Program (GAO/T–GGD–95–131) (March 1995) p. 6.
[12] GAO, GOVERNMENT CONTRACTORS: An Overview of the Federal Contracting-Out Program, (GAO/T–GGD–95–131) (March 1995) p. 6.
[13] Ibid. p. 6–7.

in an agency's internal appeal system. Unfortunately, the agency internal appeal system often does little more than rubber-stamp management's decisions and there is, therefore, no longer an effective forum in which to report the failures of agencies to comply with this important federal acquisition regulation.

As the Subcommittee considers reforms to the Circular A–76 process, NTEU urges you to include a provision that would expressly allow unions to use a negotiated grievance procedure to resolve disputes over such issues as when an agency abuses its authority by contracting out services merely to avoid personnel ceilings. In addition to lengthening, possibly to 30 days, the period of time within which employees can appeal an agency's contracting-out decision, the Circular should also be expanded to permit employees to appeal such a decision outside the agency system and allow as well for a judicial review.

CONCLUSION:

Given the emphasis on labor-management partnerships and decentralized decision making in recent years, some might suggest that contracting out concerns might be better addressed at the respective agency levels. NTEU has attempted to work in partnership with various federal agencies where excessive contracting-out robs the American taxpayer of the best possible return on his or her tax dollar. One such example is the Federal Deposit Insurance Corporation (FDIC), where the Corporation's own internal studies have demonstrated in the past that FDIC employees not only outperform outside contractors by exceeding collection goals and bringing in more money, they also provided significant savings by performing these asset liquidation tasks in a less costly manner. NTEU continues to work with the FDIC to curb what we see as excessive contracting-out by the FDIC and the Resolution Trust Corporation, with moderate success. Clearly, however, the Congress and OMB working to implement a clear national standard of guidelines that apply to agencies across the board would significantly increase efficiency as well as the economic benefits that would accrue to the federal government as a whole.

In summary, NTEU proposes the following recommendations:

- Congressional Budgets and Appropriations Bills should indicate line-items for contracted services. Prominently displaying the staggering totals for service contractor expenses in this manner will do much to bring the crisis in contracting to the attention of policy-makers and taxpayers alike.
- NTEU concurs with the GAO recommendation that the A–76 cost comparison process should be used before contracting out any government service, including advisory and assistance services which can currently be contracted out without a cost comparison. Cost comparisons have been an effective tool for the government and afford some modicum of fairness to its employees.
- Congress should maintain provisions in the Workforce Restructuring Act which require cost comparisons for commercial functions of all sizes.
- There must be increased oversight of contractor performance if the Congress is indeed serious about streamlining federal expenditures and eliminating waste, fraud and abuse. Agencies should conscientiously audit the work of their contractors to ensure that the government pays no more than it should for the services it receives.
- In addition to the cost comparison, other non-cost factors should also be considered in determining whether to contract out or perform certain activities in-house. These include the difference between the quality of services offered by federal versus contractor employees; the timeliness of services available; the availability of federal employees to do the work; the value of flexibility in responding to variable work requirements; and whether the services needed are short-term, non recurring in nature, or of a longer term and recurring.[14]
- Agencies should be allowed to recompete for contracted work and be allowed to raise their FTE level to convert back to in house.
- Agencies should have the flexibility to accomplish their work in the best possible manner and should not be constrained by arbitrary personnel ceilings which can sometimes prove counter productive and inefficient. Budgetary flexibility should be granted to allow funding for contracting-out purposes to be used to hire additional FTEs if cost analysis indicates it would be more efficient to conduct a particular service in-house. As efforts to "re-invent" government go forward, Congress should be careful not to send a conflicting message to Agencies by encouraging them to increase efficiency while at the same time imposing hard personnel caps. Agencies should determine if contracting out for services

[14] GAO, GOVERNMENT CONTRACTORS: Measuring Costs of Service Contractors Versus Federal Employees, (GAO/GGD–94–95) (March 1994) p. 7.

or using government is more advantageous, and managers should be given the flexibility to obtain needed services from the best possible source.

• OMB Circular A–76 should be revised to reflect standardized costs instead of relying on excessive historical data in determining the most efficient organization.

• The Circular should also be modified to allow sufficient time for federal employees to appeal an agency's decision to contract-out. Also along this vein, the Committee should consider allowing the use of a negotiated grievance procedure to resolve such issues as when an agency abuses its authority by contracting-out simply to avoid personnel ceilings.

• Congress should ensure that inherently governmental functions are not performed by private contractors.

This concludes my prepared statement. Again, I thank you for the opportunity to testify before the Subcommittee today, and I am pleased to answer any questions you may have.

Mr. MICA. I thank all three of you gentlemen for your comprehensive testimony, and would like to ask a couple of questions. One of the problems that we have had is trying to develop some basis on which to do comparisons. I think Mr. Tobias just spoke about full and fair competition and a comparison process that does allow us to evaluate whether we can do things cheaper in the private sector versus the public sector.

From a business standpoint, and having come from the business world, it would seem to me that technically you could do it cheaper in the public sector because you don't have to make a profit. In the private sector, your motivation for being in business or enterprise is to make a profit and a return on your investment. In trying to get this full and fair competition that Mr. Tobias spoke about, the comparison process seems to be very difficult. Maybe I could ask the three of you to just comment on how we could best achieve that.

Mr. ENGEBRETSON. First, in the cost comparison process, the big problem that many times when you compare the contractor's proposal versus the government proposal you're going to find that they're comparing bananas and apples. And I use bananas because everybody says oranges and apples, but in this case, it's bananas and apples.

The reason for that is, and maybe the best way I can explain it is, we did some investigation within the transit industry as to how more contracting could be done. And we visited with the manager who was going to make the decision whether they would move forward with contracting, started talking about the cost comparison and just the simple issue of the facility and they were doing their work within this facility.

We said one of the problems is, if you're going to compare costs, is that you don't pay rent on this facility, and our companies would have to pay rent on this facility. And the comment was made to me, well, the building is free. Now, first of all, Mr. Chairman, I don't know of any building that's free, if he considered it free it was only because they didn't have to pay rent because of the fact that it was federally owned.

But in our cost comparison process, we do have to have those rental costs. The other thing I'd like to comment on for just 1 second, if I may, and that is the process we go through when we do an A–76. And I want to do it very quickly so you get the overview of how it works.

When the government manager decides that they want to do an A–76 program, they announce to Congress that they're going to do a study. In years past, there were times when they would announce the study, and then 5 years later, they would start it. Today, of course, they can't do that, with the 24-month, 48-month rule.

When they start the study, they go through the process of evaluating each one of the positions that would be contracted out. Then they put together what is called a most efficient organization, or an MEO. The MEO is then what drives the process to determine the positions that are going to be contracted out, and also what the cost will be; meaning that the government will use that MEO to put their price together.

They do this and then they have the DCAA the auditor come in and audit this MEO to see if prices are right, et cetera. And then they put it in a vault and lock it up. And they use, then, this MEO and the process to put the RFP together for the private sector. The private sector then of course goes through its evaluation of the RFP; puts its proposals together; and then submits their proposals to the government.

The government will evaluate the process, meaning the technical capabilities of the company as well as the price. And once that company has been selected that they're going to compare with the government MEO then they pull the government's MEO, or most efficient organization proposal out of the safe and they compare it. As you probably well know, at that point, the contractor has to beat the government proposal by 10 percent.

That's basically how it works. The process itself does have built in competitions and also the things that could make it work. We know that the process has problems. We're the first ones that will agree with this, for the simple reason that we have some members in our organization that say, I don't want to bid the A–76 RFP. But 3 years later, if it's a 1-year, 2-year project or a 4-year renewal project, then they will bid it on recompetition.

They won't take the chance of that first time, because startup and changing over to the private sector is sometimes difficult. However, our members hire, because of right of first refusal, as high as 75 and 80 percent that have been employed by the government.

Mr. MICA. Did you want to comment, Mr. Concklin?

Mr. CONCKLIN. Yes. First of all, I want to reiterate that we strongly oppose the continued use of cost comparisons, but then I want to respond to your question. And I would hope to demystify the cost comparison debate. The current cost comparison methodology—and intelligent people disagree on this, but most agree, I think—that it has a built-in bias against contractors, on average that's probably in the 10 to 20 percent range, because the government's budget and accounting system, unlike the private sector, does not—does not—fully allocate overhead.

The Pentagon has a sunk cost. When the Department of Defense looks at a motorpool 8 levels down in the DOD vertical organization, the multibillion dollar cost of the Pentagon does not get allocated down into the cost for that motorpool in some fractional way. If you're doing the comparable thing and it's Martin-Marietta, with a 10-level deep organization, bidding on that motorpool, by law—

that is the SEC, the IRS, and the procurement cost principles—you must allocate every penny of overhead or you are committing fraud.

So it's a black and white situation. But to try to answer your question, if it is the ultimate decision to continue in some degree cost comparisons, then it is well within the reach of the government to commission some independent, highly qualified organization, like perhaps one of the best business schools in the Nation, to look at two or three representative government agencies and literally force them, analytically force them, into a full direct and indirect cost—that is, an overhead and direct cost—model, and in the process get much better estimating relationships or estimating methodology than we have today.

Real simple. It's just that we haven't had the collective will to do that, and we've continued, through the A–76 and the Defense Department depot and other enterprises, with a rather flawed system that politically and professionally is not accepted by the community.

Mr. TOBIAS. Mr. Mica.

Mr. MICA. Mr. Tobias.

Mr. TOBIAS. The A–76—I'm stunned to hear that we shouldn't have cost comparisons; that we should just do it, we should just accept the fact that it would be cheaper without any evidence. But that aside, what's compared in A–76, when the comparisons are computed in-house—personnel costs, all personnel costs, all pay, all benefits; material and supply; other specifically attributable costs; overhead costs; cost of capital; one-time conversion costs; and a total.

The contract performance cost; the contract price; the contract administration; the gain or loss under the disposal or transfer of assets; and then the contractor gets to deduct—gets to deduct—the Federal income tax that they would pay as a result of getting the contract. So I don't think these folks are disadvantaged in this arena. And second, the idea that, when government is computing its costs, that it doesn't include the cost of rental is just not accurate.

GSA charges everybody a SLUC fee, and that's what goes into the comparison. I said it right, "SLUC," a SLUC fee. And they charge, actually, about, oh, I think it's somewhere around 25 percent over the actual cost to take care of the building. So I don't think that the costs are excluded from this process. And I think that the A–76 is very comprehensive in what it includes.

So I think that the issue is, whether or not Congress requires, in this $12 billion arena, particularly, that costs be compared and that Federal employees get an opportunity to compete and get back work that goes out.

Mr. MICA. I'll defer now to my ranking member, who's been waiting patiently. Maybe we can get back to some questions in a moment. Thank you. Mr. Moran.

Mr. MORAN. Thank you, Mr. Chairman. Mr. Tobias, you feel comfortable with the A–76 comparison, or would you make changes to it if you had your druthers?

Mr. TOBIAS. You know, I think that the main problem with the A–76 process is the speed with which it's done. I think that that's the real problem, and as a result, very few people are satisfied with

it. Federal employees are not satisfied because everybody knows that an A–76 study is being done and it takes a long time. And everybody is nervous and wondering if they're going to be able to keep their job or not.

The private sector is upset because it's competing for work that it may or may not get over an extended period of time. So if I were to change one thing in the process, it would be to figure out how to do it faster than it's done today. I think that's a real critical need.

Mr. MORAN. But you would not change it substantively. You'd change——

Mr. TOBIAS. I would not change it substantively. I would not. I would expand its coverage to include service contracts, which are not currently covered.

Mr. MORAN. Mr. Concklin, Mr. Engebretson, do you have a structure for what you would replace the A–76 with?

Mr. CONCKLIN. Yes, we have what you could at best call a conceptual structure. And the reason we don't have a specific or design level structure is, you cannot do that unless you can get inside a government agency and go through the process of looking at all—and I apologize if this sounds tutorial—but all of the functions and all of the money and putting them into one bucket which would be called program or direct charge type activity, and another bucket which would be the support or overhead activity, and then seeing what the numbers look like; and from that process—which is exactly what a complex corporation goes through constantly—from that process develop some much more accurate estimating relationships that would indeed remove the current situation, where things that are general purpose, like a Pentagon—and there are countless similar examples—are treated as free goods or sunk costs and do not get flowed down in a fractional sense and incorporated as overhead in the thing—the motorpool or whatever the thing is that is the subject of potential contracting out.

But it's not rocket science; it's relatively easy to do by qualified people. It just hasn't been done.

Mr. ENGEBRETSON. I'd also like to remind my colleague, Mr. Tobias, that not too long ago, the study process, as I've said in my opening statement, went as long as 9 years at one point. I would like to remind him that this is now a 24-month, for a single function, and 48-month for a multifunction, which means the process has moved a little bit faster. But if you will read my testimony, we're saying that we want the study process closed even tighter—12 months for a single function, and 24 months for a multifunction.

We think it could be done in that amount of time. And once that happens, then everybody is saving dollars, the government included.

Mr. MORAN. My impression is that most often the decision is made whether or not to contract out, and then the agency goes through a perfunctory process to do an A–76 to hit whatever their objectives are. And I don't know that's the case. I don't have any scientific experience, empirical—well, I have empirical, I don't have any scientific, statistical analysis. But it's been my observation that the decision whether or not to contract out is generally made first, and then the A–76 is done.

But Mr. Cox suggested that virtually any government activity can be done 40 to 60 percent more cheaply, I gathered, in the private sector. That's generally too high. I haven't seen any experience that would support that, but what—Mr. Concklin, you probably have some figures on that. What studies do you have that would——

Mr. CONCKLIN. The data is as much anecdotal as it is statistical. So I want to carefully qualify that and make sure that's understood. But I would offer to you one significant data point that I think, in part, responds to your question. The U.S. Air Force, it is my understanding, has been the most aggressive and has gone through the largest volume—dollar volume and body-count wise—the largest amount of A–76 contracting.

Now I heard their Deputy Assistant Secretary testify last week that, across a very large universe—I think it was something over 400 million, if I recall the number—of service contracts, many contracts, they have saved approximately 20 percent through going through the process; and importantly, 60 percent of that universe of Air Force contracts were contracted out. The remainder, presumably, based on a cost comparison study and other factors, a decision was made for the remainder to retain them in house. But that is a real world sample, and I believe it's the biggest single sample at an agency level. Certainly the State and local testimony galore suggests that it's clearly in the 15 to 30 percent range, if you look at municipalities. Mr. Engebretson.

Mr. ENGEBRETSON. Also, Congressman Moran, I made a statement—the Wall Street Journal did some investigation on April 1993, and they also stated that it was a 25 percent average. And so I think that number is pretty close, around 25 percent.

Mr. MORAN. Mr. Tobias.

Mr. TOBIAS. You know, this kind of number and this kind of anecdotal evidence, and even the GAO reports, I think, are irrelevant to the basic policy consideration. Unless Congress says, we're going to get rid of—that we're going to adopt Mr. Cox's approach, which is the only thing that we have in the Federal Government are those people who are policymakers and those who are overseeing contracts, the issue is, it seems to me, in each instance, who can do it cheaper; who can do it better?

And let the competition figure that out. Let the competition decide who can do it better; who can do it in a more satisfactory fashion—the Federal employees or the private sector. And in that sense, we wouldn't have to rely on averages; we wouldn't have to rely on anecdotal evidence. We would have the hard facts to evaluate on a case by case basis.

Mr. ENGEBRETSON. I would like to remind my colleague that this is about a 50–50 split right now. About half of the work stays in house through the competition process, and the other half goes to the private sector.

Mr. CONCKLIN. And I'd also like—and I'll be brief—but I'd also like to correct Mr. Tobias. What I stated is not anecdotal. The Air Force experience is empirical and documentable. It is not in any sense anecdotal, and it's the biggest universe of data that we know about.

Mr. MORAN. I don't have any question about those numbers. And in fact, those numbers are what I would expect it to be—15 to 25 percent. And I do think there's some overhead that is not figured in. But I would go beyond what Mr. Tobias lists as the criteria. With the Air Force, for example, there are security considerations. There is a need to retain a certain number of personnel with the kind of expertise, with the kind of loyalty, with the proven dedication to accomplishing a mission that you can't rely upon if you become dependent upon the private sector.

So I do think—and I think that goes beyond defense intelligence functions. It really would be the case in virtually every Federal activity. You want to make sure that there is a certain pool of employees with institutional knowledge; with a certain level of loyalty and dedication; with the skills that you may need. There is a value to having people available immediately when you need them, and also when decisions are made during the process of recommending to the chief executive, ultimately, through OMB and so on, and through the legislative process.

You need a certain number of people who are able to bring their experience to the table in decisionmaking. So I think we need to go some steps beyond simply making the decision whether or not to contract on the basis of the most efficient way to carry out a function. And it worries me in some areas that we may be giving up that kind of security, that pool of people that we may 1 day need, even though we don't necessarily need them on a day to day basis.

And we can't be sure that we're going to have that pool of personnel or expertise if we only contract them when we decide that we need them, because not only is there a lag time, there's a certain question of whether you're going to be able to get them. When we entered the Vietnam War, the person with the greatest expertise on Vietnam in the early—well, actually, even 1959—was not in the State Department.

He had been let go, and he was selling refrigerators in New York City. That was not where he should have been, and in the long run, it would have saved us a heck of a lot of money if we had had the most knowledgeable people working for the State Department. But that wasn't so much downsizing, and a result of the McCarthy era.

But I could find other cases where we have paid a price for not having a pool of employees. So even if we can quantify the difference, and even if it is clearly a cost savings, there are other considerations to make. It's a judgment call. I'm aware of any number of cases where there has been deliberate underbidding on, particularly, cost-plus contracts. And then we wind up being stuck, being committed down a road and dependent upon a contract we wind up paying much more than ever was anticipated.

But I'm also aware of some cases—and Mr. Concklin alluded to it—of this refederalization. There's one case with EPA that is, as far as I'm concerned, it's outrageous; when a contract was made, the personnel had been performing it for 20 years. And then 1 month after it was renewed, EPA decided they were going to buy up the employees, thereby taking away the value that this contractor offered to the government.

In the private sector, that would be cause for immediate legal suit. That's stealing an entity, and with most organizations, the sum is greater than the individual parts. And if you buy up the parts, then you lose the value of the contracting firm. I couldn't believe that that happened, and I think we need to get into that. But there are extremes on both sides.

There are abuses on both sides. I think what we need to do is to come up with some criteria where we can reach the closest to consensus that it is fair that it takes into consideration not just the quantitative aspects, but the qualitative considerations as to what is in the long-term best interest of the Federal Government, and ultimately the American people.

As was said, this is a very controversial area. But I'm glad that you're taking it on, Mr. Chairman. And I think it's imperative that we take it on, given what I think is a rush to downsize as much for political reasons as to accomplish any long-term savings and personnel reductions. But we're going to have to figure out how best to contract out in a way that is fair to the people and consistent with our other responsibilities that we have a legislative requirement to carry out.

We have the right people here, and I would hope that we can have—that this is not the only time that you sit down at the table together. We have conflicting perspectives and interests, but representing both interests in my district, I can see that there are a number of areas where there can be some common agreement. And some of the external factors kind of force that agreement I think, such as the downsizing.

But again, I've taken a lot of my time, Mr. Chairman, I appreciate the fact that you're having the hearing and the opportunity to get some of this important information and perspective on the record.

Mr. MICA. Well, I thank the gentleman, and maybe if we could get Mr. Tobias to consider moving into your district, we could get all three of you together.

Mr. TOBIAS. I'll give that serious thought, Mr. Chairman.

Mr. MICA. But all kidding aside, we do appreciate your line of questioning and also your response. There were a couple of areas where I just might ask a question or two. I think at least two of the panelists talked about removing statutory constraints or restrictions. I think there's some reference to section 5(g), and some bad experiences, I guess, with EPA.

Would the two of you gentlemen, Mr. Engebretson and Mr. Concklin, comment for a moment about what you think needs to be done on removing some of these constraints? Mr. Engebretson.

Mr. ENGEBRETSON. If I could just do one other thing, and that is to add to my Congressman's remarks. And that is that yes, there are abuses on both sides, no question about that; and we'd be the first to admit it. There are bad apples in every barrel, and we know that as well. But we still have one basic question and that is there are many positions that could be contracted out.

We're not sure why they have to be done by the government. And I can give you some examples, such as motorpools or vehicle maintenance. We just don't understand why vehicles have to be maintained by government employees, when the private sector can do it

and do it very efficiently. Or we can go into ground maintenance, or we can go into building maintenance, we can go into food service.

Many of these items don't get into the category that you were talking about, about the policy process, et cetera. And I think that they should be contracted out. The private sector is very competitive. And our industry is so competitive that it sometimes scares me or sometimes I even ask the question, why they're even in this business, because it's so competitive.

But I think that there are areas that more contracting should be done, and the private sector could do a good job for the government. And I would urge that the Congress take a look at these respective areas.

Mr. MORAN. Those are the areas that local governments have tended to contract out, to privatize.

Mr. ENGEBRETSON. Right, yes, right. Now, in reference to impediments, Mr. Chairman, there is quite a long list. And of course, some of these have been addressed through some other areas, meaning that, as you know, FASA I, and FASA II is in the stream now. There are some issues that are going to be addressed in acquisition reform.

Also, we understand some items are going to be addressed in DOD authorization that will streamline the process as well. I think probably the best answer would be through the administrator of OFPP, Steve Kellman—we've been working on what they call performance-based contracting. And as you may know, Mr. Concklin's council and CSA are two of the associations that have signed on to this process.

And that, again, is streamlining the process. So I think the best way to answer the question, Mr. Chairman, is, there are some impediments. And we do have a list of some of them here. But there are more that could be given to you that could be discussed in detail for the future.

Mr. MICA. I want to thank you, Mr. Engebretson. Mr. Concklin, I'm going to have to be a little bit discourteous——

Mr. CONCKLIN. No problem.

Mr. MICA [continuing]. And ask you if you wouldn't mind responding, and Mr. Tobias, in writing, if you could, to that.

Mr. CONCKLIN. Sure, be glad to.

Mr. MICA. I've been called for two votes in another committee and they're waiting on me right now.

Mr. CONCKLIN. OK.

Mr. MICA. We thank you for your participation. We will have an additional hearing, we hope, on contracting, and we hope that you'll continue to assist us. And with that, I declare this meeting adjourned.

[Whereupon, at 4:45 p.m., the subcommittee was adjourned, subject to the call of the chair.]

[Additional information submitted for the hearing record follows:]

PREPARED STATEMENT OF BARRY KRASNER, NATIONAL PRESIDENT, NATIONAL AIR TRAFFIC CONTROLLERS ASSOCIATION

Mr. Chairman and members of the Subcommittee, I am Barry Krasner, President of the National Air Traffic Controllers Association which represents over 15,000 of our nation's dedicated air traffic controllers who work for the FAA. Thank you for

the opportunity to submit this statement on the contracting out of Level 1 VFR towers.

I am fully aware of the severe budget constraints the federal government is under and the genuine desire of Congress to make strides in balancing the federal budget and reducing the size of the federal government. I am concerned, however, that the margin of aviation safety may be lowered in the effort to give the taxpayer economic relief and less burdensome government. I am submitting this statement in an effort to bring to the attention of this able committee a practice exercised by the FAA which affects public safety. While NATCA applauds the Congress' efforts at budget reduction, we do not believe that aviation safety should suffer in any way in these efforts.

The FAA has been forced to make the questionable choice of contracting out Level 1 towers for budgetary reasons. Level 1 towers are towers which rely on "Visual Flight Rules" and controllers working in these towers are responsible for the flow of air traffic within a five mile radius. VFR control towers (Level 1's) are not equipped with radar but many experience a high volume of general and commercial traffic. For instance, in just three of the towers on the 1995 hit list, Hyannis, Massachusetts has a total of 62,863 commercial operations per year and Lihue, Hawaii has 42,474 and Key West, Florida a total of 28,194. When you add general aviation operations to these figures, Hyannis totals out at 125,412, Lihue at 57,686 and Key West at 94,511. The aircraft using these facilities range from Cessna 150's to Boeing 757's. The Level 1 controllers work the aircraft that carry hundreds of thousands of tourists, families and business men and women every year.

We have come to a sad point in aviation history where the FAA feels that it can no longer provide air traffic control services to certain areas of the country, makes a lone determination to contract out such services, conducts no A–76 cost benefit analysis and escapes scrutiny for their actions. This situation exists in part because of the failure of OMB Circular A–76.

In April of 1993, prior to any formal notice to the National Air Traffic Controllers Association (NATCA), the FAA determined to contract out one hundred of its Level 1 VFR towers. NATCA requested formal notification. This request was repeated on January 13, 1994 with a specific request for verification of compliance with OMB Circular No. A–76's cost comparison analysis. The FAA replied that information regarding A–76 cost comparison data was not available. NATCA later found that the information was not available because the FAA had granted itself a waiver of the cost benefit analysis requirement. The ostensible "waiver" of the Circular requirement, issued on January 12, 1994, was six months after the FAA's decision to contract out. The FAA claimed that they had concurrence with the OMB A–76 coordinator. In connection with an expedited arbitration on this issue, the OMB official claimed that no coordination or concurrence of any kind had occurred between the FAA and OMB regarding any waiver of the Circular's requirements. Even if the FAA had complied with the Circular's waiver requirements, certain mandatory decision-making required by the Circular cannot be waived.

The Circular requires agencies to review all of its activities to determine which are "governmental functions" under the OMB's definition and which, therefore, may not be legally contracted out. The FAA should have reviewed all of its activities to determine which were "governmental functions", made a determination as to which were "commercial activities: and then determined whether a "commercial" activity must be performed by government employees for "national defense" purposes.

The FAA did not adhere to the mandatory decision-making process in the Circular as described above. The failure of the FAA to comply with the requirements of OMB Circular No. A–76 was noted in District Court litigation in the Northern District of Ohio between NATCA and the FAA. This litigation continues on appeal. Because of the waiver provision and the lack of enforcement mechanisms for compliance with the Circular's requirements, NATCA believes that there is a fundamental flaw in A–76. An agency may waive its obligations under the Circular, defeat the essential purpose of the Circular and escape scrutiny.

Having made the determination to contract out these facilities, in October of 1994, twenty-five towers were contracted out to private air traffic companies. Some of these companies have ties to former FAA officials who were involved with the contracting decision. After just three months some of these companies had major problems with the level of controller competency. Some of the controllers had to be retrained because they did not know the local terrain; did not know standard phraseology, and were giving confusing and potentially life threatening instructions to pilots. Since most of these facilities now operate for long periods of time with only one controller on duty, pilots have complained to the FAA about coverage and services. Recently, in Hagerstown, Maryland, the FAA was forced to require the contrac-

tor to hire additional staff. In Brownsville, Texas, a flying school decided to move its operations because touch and go's were limited due to scarce staffing.

NATCA has serious reservations with regard to the safety and national security of the privatizing of Level 1 towers. It is clear that the FAA has lowered the standards of these facilities. I cite examples which support NATCA's contention that the standards under which these towers operate are not the same as FAA towers and potentially present safety problems to general aviation and commercial pilots.

As mentioned above, in New Haven/Groton, Connecticut towers and in Hagerstown tower, problems cropped up which required the FAA to come back into the facility to retrain and add staffing. NATCA learned of these problems from private pilots and FBO's based in these communities. These are just two examples of irregularities but should NATCA or Congress conduct an investigation, similar problems in the other 23 facilities might be found. Only twenty-five facilities have been contracted out thus far. Twenty-five more are scheduled for this summer. We must ask ourselves if these problems will exist in the future when more facilities hit the chopping block. Additionally, the next group of towers to be privatized are not towers with little air traffic or relegated to only general aviation. As stated above, in the next twenty-five to be privatized, Key West, Florida and Hyannis, Massachusetts are popular tourist destinations with heavy annual commercial traffic.

With regard to the New Haven and Groton Connecticut towers, they went private in September of 1994. In November of 1994, pilots in that area commenced a computer network campaign to communicate their concerns about the safety of these towers after the conversion. I quote a woman who was the vice president of a flying club in that area, "The controllers do not know local landmarks. Reporting over Lake Gallard, which is the largest lake around, about seven miles from the airport and quite humongous, gets a 'Huh?, where's that?" I think, outside of the blaring errors which don't just compromise safety, but will eventually be the cause of some accident here, the non-professional lingo is getting to me. It is now 2½ months since they started working traffic as 'official controllers' and they aren't getting it yet. Yesterday, arriving VFR, the controllers was very clearly in over his head. I imagine there's a piece of paper somewhere that says that the new controllers are sufficiently trained, but I'm here to tell you—It's pencil-whipped."

In another post from another general aviation pilot, he states, "The tower controller sounded like he was grasping for standard terminology but he never found it . . . not one of the tower's transmissions used standard terminology, and few came at the expected time or in the expected order. Until now, I never realized just how professional the former tower staff was! If we ever get a student returning from his first solo cross-country, at the same time as the United 737 approaches, we're going to have some seriously scary stuff going on."

In Hagerstown, Maryland, a pilots reports "Called for VFR taxi to active runway. Our call went unanswered by ground control. The ground and local control was combined at one position because you could hear the controller talking to aircraft in the air. The controller cleared two aircraft to land but did not have the aircraft in sight and another aircraft had checked on downwind. The controller was trying to locate them. Trying five times to get an acknowledgement from him, I tried him on the tower frequency for taxi, but go no response. It took 10 minutes to get a taxi clearance. I was the only aircraft on the ground and looking up at the tower, I could see only one controller in the tower cab. Upon departure, a Hawker 125 was cleared to depart right behind me, so I asked the controller if I can offset to the right so the jet departure could have a clear departure path. He approved it, then 'ran' the jet right behind us, giving the right turn on course right behind us."

The FAA was so concerned that the safety problem would reach the media that meetings were held to talk with the pilot groups in those areas. The FAA admitted at the New Haven meeting that the controllers did not receive adequate training but the next day told a joint NATCA/FAA contract committee that the next twenty-five towers to be privatized would only receive the same thirty day training program. I bring these problems up as an example of the safety concerns we have with these towers.

A study of the first twenty-five contracts conducted by an outside consultant hired by NATCA concluded that there are numerous hours when only one air traffic controller (and no supervisor) will be on duty. The consultant also noted that the Area 4 contractor indicates that during such times (when only one ATC is on duty) some temporary restrictions may be imposed. This means that touch and go operations will be suspended. As stated above, a flying school relocated from privatized Brownsville airport to Harlingen because their touch and go operations were limited. Without a doubt, services are being cut back in privatized towers. This affects the local community economically and in essential air service.

I am convinced that the contract controllers' lack of training, which is only thirty days, generates safety problems. The FAA asserts that the contract controllers are certified by the FAA. The point I would make is that the FAA makes the certification. If the FAA wants to certify these controllers with thirty minutes on the job training, as Congressman Lightfoot reported in a transportation appropriations hearing this month, then they will and they have. Thirty days provides approximately eight to ten hours of on-the-job training. There is no question that the standards have been lowered. Mr. Hinson testified at the same appropriations hearing that FAA controllers receive much more training than contract controllers. In fact, FAA controllers receive anywhere from three to six months of training at the Academy and anywhere from six months to two years on the job training plus classroom training and refresher courses.

The FAA asserts that contract towers are subject to the same types of periodic evaluations as FAA towers. The truth is that FAA towers are evaluated twice a year, regionally and nationally, on over 240 factors while contract towers are evaluated only once every two years on only 68 factors. An evaluation of the non-federal personnel tower, Stewart Tower, New York, revealed a serious lack of compliance with FAA regulations and procedures. I quote, "Interviews were conducted with almost all facility personnel and with several individuals who utilize the Stewart Airport. This process indicated that there are serious and fundamental problems with the air traffic operation in the Stewart area. It is alleged that operational errors and deviations occur fairly often and are covered up. The most recent significant incident concerned an aircraft that took off while vehicles were sweeping the runway. It is alleged that they missed each other by less than a hundred feet. Neither the Airport Manager, nor anyone else associated with this event, forwarded the information to the FAA." While this tower was not one of the first twenty-five FAA towers to be contracted out but one that was contracted out years ago, this evaluation speaks to the fact that safety suffers at privatized airports. Coverups and large scale deviations do not occur in FAA towers. The problem as I see it, Mr. Chairman, is that the FAA has a poor performance record on contract oversight. The problems cited would substantiate this.

Another safety problem with the contract tower program as designed is the disparity in drug and alcohol testing. Current FAA controllers are subject to random drug and alcohol testing on a yearly basis. Contract controllers are drug tested for a period of five years and, if they test negative for those five years they are thereafter exempt. This lack of consistent FAA oversight is an accident waiting to happen.

For national security reasons, NATCA believes that one unified national air space system is far superior to the fractured system we now have as a result of the contract tower program.

I urge this committee to seriously consider terminating the contract tower program for safety reasons until an investigation can be conducted. The lives of thousands of travelers are at stake. The current contract tower program was a hastily conceived idea which complied with the Administration's National Performance Review. While NATCA supports reinventing government, we do not support reinventing safety. It is time to take a serious look at the effects of this program. Your committee has the power to stop further towers from being contracted. Well over seventy Members of the House signed a letter last November asking the FAA to terminate the program and reprogram the FY 95 funds appropriated for this purpose. You have the congressional support you need to take action.

Thank you for the opportunity you and your committee have afforded the air traffic controllers to address our concerns. I know that you will carefully consider the statement put forward. For this we are grateful. We urge this committee to hold further hearings on this issue so that problems associated with public safety can be scrutinized. Thank you.

PREPARED STATEMENT OF JOHN N. STURDIVANT, NATIONAL PRESIDENT, AMERICAN FEDERATION OF GOVERNMENT EMPLOYEES, AFL–CIO

INTRODUCTION

Mr. Chairman and members of the Subcommittee: My name is John Sturdivant, and I am the National President of the American Federation of Government Employees, AFL–CIO. While I obviously would have preferred to testify in person before your Subcommittee, I appreciate the opportunity to at least submit for the record the views of the over 700,000 federal employees across the nation represented by AFGE concerning the ever-mounting problems associated with service contract-

ing and how they might be resolved through drastic reform of the OMB Circular A–76 process. AFGE has worked to improve service contracting for over 20 years, so I am eager to use this important forum to discuss our own comprehensive service contracting reform proposal.

While not reflexively opposed to contracting-out, federal employees are working and middle class taxpayers who are sadly familiar with both the extraordinary growth in service contracting expenses as well as the consistent and documented inability of service contractors to perform work in a cost-efficient manner. As the record clearly shows, the federal government is contracting-out more and more, but the American people are getting less and less. AFGE members can't help but find a bitter irony in this newfound determination sweeping Capitol Hill to sell off large chunks of the federal government to politically well-connected firms in the private sector. After all, the federal workforce hasn't been this small since the Kennedy Administration. At the same time, service contracting is the costliest part of federal procurement and one of the fastest-growing expenses in the entire federal budget. According to official government estimates, federal service contracting now costs the American taxpayers well over $100 billion every year. Nevertheless, there are some Members of Congress who don't believe that's enough and want to drastically increase the federal government's contracting-out expenses.[1]

Let me say that I did not submit this statement in order to regale members of the Subcommittee with the shocking details of the latest service contracting scandal. That service contractors have managed to perpetrate significant abuses in virtually every federal agency into which they have been given entree, and that these significant abuses have resulted in massive cost overruns and shoddy work are not opinions but facts, established in report after report from the non-partisan General Accounting Office (GAO) as well as the Office of Management and Budget (OMB).[2] The latest independent corroboration of the crisis in contracting came from a GAO report released just last year, inconspicuously entitled GOVERNMENT CONTRACTORS: Measuring Costs of Service Contractors Versus Federal Employees.[3] This report surveyed nine studies on service contracting and found that in each case savings, often substantial, could have been realized if the work had been done in-house.

But now is not the time for federal employees to rub their hands with glee and exclaim triumphantly, "I told you so! This is what happens when the federal government turns over some of its most important functions to often unseasoned, profit-hungry outsiders with little or no oversight." Rather, now is the time for federal employees and their representatives to work with Congress to ensure that agencies are required to make better-informed and more fiscally-responsible decisions about service contracting. In that spirit of cooperation, let me now present AFGE's own comprehensive service contracting reform proposal.

1. Just as Government Must be Reinvented so Must Federal Service Contracting

If I might paraphrase the words of the architects of the reinvention of government initiative, while we clearly don't need more service contracting, we do need better service contracting. And better contracting will come about only if there is real and genuine competition between contractors and federal employees for the federal government's service assignments. This competition would invigorate both groups of service providers, inspiring them to do their best work, and empower the federal government to make the choices that would best serve the nation's taxpayers and service beneficiaries.

Competition is something my membership knows from first-hand experience. As part of the reinvention initiative's attempt to bring the lessons of the private sector to public service, federal employees and the methods by which they perform their work have undergone complete and thorough examinations. In the constant pursuit of efficiency and effectiveness, many old ways and patterns have been tossed aside in favor of new ideas and techniques. As the Members of the Subcommittee know well, federal employees have made numerous sacrifices in order to advance the reinvention of government initiative, the loss of 272,900 jobs over the next five years being only the most prominent. But federal employees are determined to use the in-

[1] ". . . I believe that in the next four years it should be possible to contract out more than fifty percent of the services and activities of the federal government." (Opening Statement of the Chairman of the Subcommittee on the Civil Service, Representative John L. Mica, Hearing on Contracting Out (March 29, 1995).

[2] "Numerous Inspector General and General Accounting Office reports, Congressional hearings and internal agency studies have documented contract performance problems and service contract overruns." (Testimony of John Koskinen before the House Subcommittee on Civil Service, Hearing on Federal Policies Related to Contracting Out (March 29, 1995), p. 3.)

[3] GAO, GOVERNMENT CONTRACTORS: Measuring Costs of Service Contractors Versus Federal Employees (GAO/GGD–94–95) (March 1994).

novations of the reinvention initiative to make the federal government a more effective and efficient instrument for the delivery of services.

Unfortunately, our contracting counterparts have yet to be reinvented. Unlike the federal workforce, they have undergone no complete and thorough examinations. Unchallenged by real competition, they still cling tenaciously to outmoded processes and attitudes. Hence, the crisis in contracting.

2. The Federal Government Must Finally Become a Cost-Conscious, Quality-Conscious Consumer

Any customer who insists on spending freely in a marketplace despite not knowing what he really wants, despite not caring enough to bargain for the best deal, despite not understanding how to determine whether he received that for which he paid will be taken advantage of. And that's true whether the marketplace is the strip mall down the street from where you live or the mythical one where the federal government buys needed services. When the customer is lazy and ignorant but free-spending, the merchant simply has no incentive to provide effective and efficient service at reasonable prices. And that is the problem with the federal service marketplace today.

In order to make service contractors more competitive, the federal government must become a better shopper. First, the federal government must decide precisely what services it wishes to buy. It must then bargain aggressively for the bid that promises to deliver the most effective and the most efficient service, whether it be from federal employees or a contractor. And, finally, the federal government must determine whether the service provider selected lived up to the terms of the contract. One truism after another, you may be saying to yourselves. And you're right, of course. However, those three truisms are still considered novel concepts by far too many senior managers in too many agencies.

3. Agency Managers Must Prepare Better Statements of Work

The contracting process is flawed from the very start. As OMB has reported, Statements of Work (SoWs), the forms used to describe specifically the services to be contractually procured, are frequently so poorly-written that it is difficult to determine the agency's requirements or the standards against which performance is to be measured.[4] Sometimes, bad SoWs are caused by senior managers who are less than certain themselves about just what services they wish to contract out. Often times, however, the cause is simply sloppy drafting. In fact, some contract officers will use the same forms over and over again, even after they are long out of date. Whatever the cause, federal employees and less-established contractors are left at a disadvantage vis-a-vis the more established contractors, usually the ones who have acquired "inside knowledge" from hiring senior managers with special personal connections.

Sloppily-drafted SoWs reduce competition for service assignments between federal employees and contractors. And if there is less competition, whatever cost savings estimated to be realized through service contracting quickly vanish, while the problems associated with contract administration and quality control loom ever larger.

For example, a contractor often appears to be the efficient alternative in the cost comparison process only because the SoW failed to include all of the different assignments that had been required of the federal employees who had been performing the work. Once the contract's been signed, however, the agency has little leverage with the contractor. And when the uncompleted assignments begin to pile up, senior managers have two choices: 1) negotiate an additional agreement with the contractor, i.e., give even more money to the contractor and lose whatever savings had been collected from the decision to contract-out; or 2) use seasoned, reliable federal employees from other offices or installations to get the job done right. Either way, contracting-out winds up costing more, an expensive lesson the taxpayers need not have had to learn.

Another problem with many SoWs is that they fail to anticipate contingencies. No one expects a contract officer to be a latter-day Nostradamus, but the SoW should be drafted with some understanding of how the assignment's requirements might change over the term of the contract, something that occurs with some frequency in government. Of course, this is one of the disadvantages of service contracting. When work is done by federal employees, requirements can be changed in the event

[4] OMB, Summary Report of Agencies' Service Contracting Practices (January 1994), p.v. The report noted that "(t)he statements-of-work used to describe the specific tasks or services to be procured by contract are frequently so broad and imprecise that vendors are unable to determine the agency's requirements. As a result, competition is limited and performance cannot be assessed."

problems emerge, new laws are made, or improved technology becomes available. However, it is much harder to bring about change in a contractual relationship since the requirements must be spelled out in advance and then reduced to legally enforceable language.

But if Congress really wants agencies to write better SoWs, then senior managers should be required to consult in advance with the people who know better than anyone else what it takes to get the job done. And, with apologies to political scientists, journalists, political appointees, and even Members of Congress, those experts to whom I'm referring are, of course, rank-and-file federal employees, the men and women who actually perform the work.

Finally, it cannot be emphasized strongly enough that the drafting of SoWs is an inherently governmental function. Such work must not be left to contractors because of the obvious conflicts of interest involved. According to OMB, the in-house capability to develop adequate SoWs at the Department of State has so atrophied that the work must be contracted out.[5] While this is a situation ripe for satire, it is also cause for concern. After all, the farmer doesn't often ask the fox how high he thinks the fence around the henhouse should be.

4. Agency Managers Must Stop Ignoring Cost Comparison Requirements

I wish I could report that SoWs were the only weak link in the chain. However, the methods by which the federal government determines whether to contract out services are in even greater need of reform. OMB Circular A–76 does require agencies to compare estimated contract and in-house costs for the specific work to be performed to determine the more cost-efficient approach. Unfortunately, agencies often disregard this rule. As OMB itself reported, cost analyses and independent government estimates are not performed by many agencies prior to renewal, extension, or recompetition of existing contracts.[6] And in far too many instances, OMB must admit, cost estimates are not even prepared prior to entering into new contracts![7]

If Congress genuinely wants to reduce service contractors' billion dollar bills, then federal employees must be allowed to compete for service assignments. Clearly, such competition is impossible if senior managers are not required to perform cost comparison requirements before deciding whether to contract-out.

5. Contracting Must Create Genuine Cost Savings and Quality Improvements

What sort of cost savings are we after when we contract out a service in order to achieve greater efficiencies? Let's face the facts: far more often than not the cost savings resulting from a service contracting decision can be attributed in large measure to the contractor's providing her employees with low wages and few, if any, fringe benefits. Ultimately, the federal government should award contracts for only two reasons: 1) The contractor has devised a more effective and a more efficient way of providing a service than that employed by the agency, or 2) the contractor's workforce possesses expertise that cannot be found in the agency's federal workforce.

A contractor who uses the same methods or level of expertise as the agency in rendering a service but is shown in a cost-comparison process to be the more efficient service provider merely because she pays her employees next to nothing creates no program efficiencies.

- Do we really want agencies to save money by taking it from the battered wallets and torn purses of the ever-expanding number of contractor employees toiling at or near the minimum wage?
- Do we really want to give contractors powerful incentives to provide their employees with the lowest salaries and fewest benefits possible?
- Do we really want the federal government to become a silent partner in sweatshop operations scattered across the nation?
- Shouldn't the federal government's role actually be to encourage providers, whether they be federal employees or contractor employees, to come up with better and more ingenious ways of performing important services?

---

[5] OMB, Summary Report of Agencies' Service Contracting Practices (January 1994), p. 5. "The State Department indicated that in-house capability to develop adequate SoWs is so lacking that they now find themselves in a position where they have to resort to contracting for such services. State says they would prefer to do SoWs in-house, but do not have the trained personnel in-house to perform this function."

[6] OMB, Summary Report of Agencies' Service Contracting Practices (January 1994), p. v.

[7] Ibid.

6. Effectiveness—Quality of Work and Timeliness of Delivery—is Just as Important a Consideration as Efficiency in Deciding Whether to Contract-Out

Of course, a service provider must do more than perform an assignment at low cost. The quality of the work and the timeliness of the delivery are just as important considerations. Consequently, the comparison between contractors and federal employees must include quality and timeliness as well as cost. Only if the comparison is broadened to include all factors relevant to performance will the federal government make the best choices for service assignments.

Let's move from the general to the specific. The Department of Defense (DoD) perennially recommends abolishing the prohibition on contracting-out fire fighting functions on its installations. Congress has always rejected this initiative for several very good reasons. Federal fire fighters don't just perform fire suppression work. They provide fire prevention, hazard mitigation and abatement, and emergency medical services. They are also trained to respond to airplane crashes and nuclear and biological incidents.

Do employees of the typical fly-by night fire fighting contractor have such varied and specialized skills? What about the frequently volunteer fire fighters in nearby municipalities? I doubt it. Historically, fire fighter contractors suffer from high employee turnover, a phenomenon which significantly drives up the costs of processing the security clearances necessary to work on sensitive DoD installations. Finally, contractor fire fighters have consistently proven unable to respond in a timely manner to fire fighting emergencies, as required by DoD and OSHA regulations.

Because the lives of soldiers and civilians are at stake, because expensive military hardware is at risk, and because only highly-trained fire fighters are capable of performing tasks as varied as emergency medical services and responding to nuclear incidents, Congress has steadfastly prevented DoD from cutting corners by contracting-out fire fighting functions on its installations. "You get what you pay for," goes that old maxim. And when Members of Congress talk casually about contracting-out important federal services, they should understand that getting what agencies paid for usually means the American people not getting what they need.

Mr. Chairman, some of the witnesses you have permitted to testify today will no doubt refer to this sound policy of relying on skilled and seasoned federal fire fighters exclusively as a "barrier" to contracting-out. As the facts would indicate, it might be more accurate to refer to the moratorium as a "safeguard."

7. Contracts Must Not Be Renewed Reflexively

I also urge the members of the Subcommittee to consider whether the public/profit comparison should include an additional consideration: whether the market for this particular service will remain competitive for the foreseeable future. Frequently, a contractor who wins a significant government service contract acquires such an advantage over his rivals that the latter are forced to significantly retrench or even go out of business, thus greatly reducing the competitiveness in that particular market. The absence of healthy competition removes the incentives necessary for the contractor to provide timely and effective service; consequently, the estimated cost savings realized under the contract usually vanish.

When the contract comes up for renewal, the contractor, having established a monopoly, is able to demand a larger fee the second or third time around. By then, however, the federal government's own bargaining power is significantly reduced since the federal employees who used to perform the service in question have often been separated or dispersed, their valuable expertise lost. If the service contractor knows that the contract will be renewed without further review, what incentive will there be to reduce or eliminate the unnecessary expenses he charges to the federal government?

The best way to keep the market for service assignments competitive is to require that agencies conduct another public/profit comparison at the time of contract renewal. Contracts should not be reflexively renewed. As time passes, it is often the case that more effective and more efficient ways are devised to deliver services. As many municipalities have discovered over the last several years, for reasons of effectiveness and efficiency, it makes sense to bring contracted-out services back in-house. After all, if a contractor can deliver a service more cheaply than the federal government and make a profit, the government can probably find a way to deliver that service as economically as a contractor, but without sacrificing timeliness and customer satisfaction.

8. FTE Ceilings Must Not Be Allowed To Force Wasteful Service Contracting

The most aggravating part of the public/profit comparison, however, is what happens after a determination has been made that it would be more cost-effective for the service in question to be performed by federal employees. One would think that

this determination would be the end of the story: an important service is delivered in the most cost-effective manner possible; the nation's taxpayers enjoy a small victory against waste; the federal government uses the cost savings to address other pressing needs; contractors, finally spurred on by real competition, become leaner and more efficient service providers; and federal employees overcome a biased public/profit comparison process and are justly rewarded for their quiet competence.

Although that is how the story should end, it doesn't always work out that way because of the federal government's stubborn determination to snatch defeat from the jaws of victory. Yes, even when the public/profit comparison process required by OMB Circular A–76 shows that it would be more efficient to render a service in-house, the federal government often still insists that the service be contracted out—cost savings be damned!

As OMB itself reported early last year, several agencies—including the Departments of Agriculture, Health & Human Services, Housing and Urban Development (HUD), State, Education and Treasury, as well as the Environmental Protection Agency—said that they each could have saved several million dollars by performing functions directly rather than having them performed by contractors but did not do so because either their requests to OMB to take on the necessary full-time equivalents (FTEs) were refused or the agencies were so sure such requests would be refused that they were not even submitted.[8]

As the Report of the National Performance Review clearly states, the federal government must avoid using FTE controls to produce downsizing because that technique is "frequently arbitrary (and) rarely account(s) for changing circumstances . . . Organizations that face new regulations or a greater workload don't get new FTE ceilings. Consequently, they must contract out work that could be done better and cheaper in-house."[9] Instead of FTE controls in isolation, Congress must define the scope of an agency's mission. Only when it is understood what work an agency is to perform can the appropriate level of staffing be realistically determined. FTE controls and arbitrary staff reduction targets cannot possibly lead to right-sizing.

If the federal government is ever to become a better shopper for services, it is obvious that senior managers must be given much greater flexibility in using their budgetary resources so that funding for service contracting can be used to hire additional FTEs in the event a public/profit comparison process indicates that it would be more effective and more efficient to render a particular service in-house.[10]

If I might be permitted to make a personal aside: Nothing in all the years that I have worked to advance the interests of federal employees and their families has made me so angry as the federal government's inexplicable determination to contract out a service even when it's been proven that the service could be more efficiently rendered in-house. As I discussed earlier, federal employees have made extraordinary sacrifices in order to reinvent the federal government and make it more effective and more efficient. But why should federal employees make all those sacrifices to become the leaner and more capable service provider if the federal govern-

---

[8] OMB, Summary Report of Agencies' Service Contracting Practices, (January 1994), p.v. "Agencies often assume that additional government personnel will not be authorized and, therefore, there is no alternative but to contract for needed services. Several agencies requested that they be given more flexibility with respect to determining whether work should be performed by agency or contractor staff. Examples were reported where the government (based on the agencies' projections) could save several millions of dollars by performing functions directly rather than having them performed by contract." In the report's Appendix 2, p. 30, OMB reported that it was the consensus of the agencies it surveyed that "OMB needs to review the cost effectiveness of bringing contracted work in-house when there aren't sufficient Full-Time Equivalents (FTEs) to perform the work. More flexibility with the budget limitation on FTEs is necessary when it can be demonstrated through studies that it would be less expensive to perform the work in-house but government personnel ceilings prevent that decision."

Although this alarming information in OMB's report is often ignored or brushed off by the agency's own officials when testifying before Congress, it was corroborated last week in GAO's testimony. "(W)e have found that the personnel ceilings set by OMB frequently have the effect of encouraging agencies to contract out regardless of the results of cost, policy, or high-risk studies." (General Accounting Office, GOVERNMENT CONTRACTORS: An Overview of the Federal Contracting-Out Program (GAO/T–GGD–95–131) (March 29, 1995), p. 12.)

[9] Report of the National Performance Review, Creating A Government That Works Better & Costs Less (September 1993), p. 19.

[10] "To achieve the A–76 program's goal, our work has shown that once agencies consider the comparative costs of contracting-out versus using in-house personnel and relevant noncost factors, the agencies then need to have the flexibility to have the work performed in the most cost-effective manner. Because of the federal downsizing in process, agencies may lack the necessary flexibility to perform activities in the manner that is most beneficial to the government." (General Accounting Office, GOVERNMENT CONTRACTORS: An Overview of the Federal Contracting-Out Program (GAO/T–GGD–95–131) (March 29, 1995), p. 14.)

ment is determined to contract out assignments to contractors who have been proven to be less effective and less efficient?

Let me make one thing perfectly clear and unmistakably understood: Federal employees do not fear competition with service contractors. What federal employees fear is a contracting-out process that is intentionally crafted to keep them from competing.

9. Federal Employees Must Be Allowed To Challenge Agencies' Wasteful Contracting-Out Schemes

In the past, representatives of federal employees like AFGE had used collective bargaining grievance procedures to force agencies to comply with the requirements of A–76. The union contracts stood as a safeguard against cost-inefficient service contracting decisions. However, a recent court decision held that a union could only contest contracting-out decisions in an agency's internal appeal system, a process that often does little more than rubber-stamp management's decisions. Consequently, there is no longer any effective forum to report the failures of agencies to comply with important federal acquisition regulations. I urge the Members of the Subcommittee to include in any reform of the OMB Circular A–76 process a provision that would expressly allow unions to use a negotiated grievance procedure to challenge violations of the Circular.

10. Contract Administration Must Finally Be Taken Seriously

Arguably, "contract administration" is the biggest misnomer in the federal government's entire lexicon. It is rare that any such "administration" ever occurs, and, even when it does, the so-called administrators usually don't know anything about contracts. Service contracting personnel concentrate their efforts on the awarding of contracts and the obligation of funds, not the oversight of contractor performance. As OMB itself reported, agencies believe that they are contracting for mission-essential services; as a result, most of their contract administration efforts focus on ensuring that they receive the required services with costs often becoming a mere peripheral concern.[11] In addition, most contract administration is not done by contracting officers who are skilled in determining whether the service was actually rendered for the price specified in the contract, but rather by program officers, who are merely determined to have the service rendered, regardless of cost.[12]

As GAO has recommended, senior managers must be made accountable for contract administration.[13] Also, the federal government must train more contract officers. Refusal to do so for fear of incurring additional expense is a classic example of being penny-wise and pound-foolish. It does the taxpayers no good for an agency to award a contract in pursuit of greater efficiency only to lose those savings because of poor or even non-existent contract administration.

Much of the refusal to take contract administration seriously stems from the pernicious notion held by many senior agency managers that oversight is a frill, an optional extra that can be discarded during times of austerity. Wrong! It's precisely during times of austerity that we must redouble our efforts to eliminate the massive amounts of waste, fraud and abuse in service contracting. For all of its occasional advantages, service contracting does have extraordinary disadvantages, the difficult and expensive problem of monitoring contractor performance being only the first and foremost of those problems. Contract administration is one of the costs of doing business with contractors. It's that simple. And because it is a cost, contract administration should also be included in any cost comparison analyses.

11. The Use of Wasteful Cost-Reimbursable Contracts Must Be Abandoned

Contractors have insufficient incentives to provide quality service for the lowest cost under the current payment system. The federal government uses two basic pricing arrangements for purchasing services: fixed-price contracts and cost-reimbursable contracts. Fixed-price contracts require a contractor to assume responsibility for performing the agreed upon work at an established price. Cost-reimbursable contracts, on the other hand, reimburse contractors for all allowable costs incurred, and

---

[11] OMB, Summary Report of Agencies' Service Contracting Practices (January 1994), p.v. "Contracting personnel concentrate on the award of contracts and the obligation of funds."

[12] Ibid. "Contract administration, particularly in most civilian agencies, is conducted by agency program staff and not by contracts personnel. The program staffs are often ill-trained in contract administration."

[13] GAO, FEDERAL CONTRACTING: Cost-Effective Management Requires Sustained Commitment (GAO/T–RCED–93–2) (December 1992), p. 13. "The persistence of contract management problems and the inattention to contracting audits indicate a need for top agency managers to intervene, raise the level of concern throughout the agency and see issues through to resolution."

are often used when the assignment is poorly-defined or subject to change. But, as GAO reported, cost-reimbursable contracts "provide contractors with little incentive to control expenses and place a considerable administrative burden on the federal government to oversee, control and identify inappropriate costs."[14] Quite simply, cost-reimbursable contracts give contractors a built-in incentive to low-ball the costs and then collect even larger fees as the contract's costs rise.

Clearly, the federal government needs to eliminate the use of cost-reimbursable contracts whenever possible. OMB should require that an agency justify entering into any cost-reimbursable contract. It should go without saying that the federal government is the most important shopper in the services marketplace.

Accordingly, the federal government should use its extraordinary leverage to make the best possible deal, especially during times of austerity. If that means getting tough with contractors and insisting that they take a fixed-price contract instead of a cost-reimbursable contract, so be it. Surely the nation's taxpayers deserve no less than that. Besides, the need for cost-reimbursable contracts will be greatly obviated if SoWs are sufficiently-detailed and written with an appreciation for contingencies.

12. Senior Managers Must Check the Work Before Paying Their Service Contractors' Billion Dollar Bills

At no point in the process is the lack of adequate oversight more costly than when it's time for the federal government to pay the bill. As OMB reported, agencies do not always review the effectiveness and efficiency of the services performed by contractors prior to the issuance of making payments.[15] The federal government seems to be that rarest of shoppers: one who doesn't care what it gets as long as it spends a lot. AFGE members cannot relate to that sort of attitude, and neither, I suspect, do the rest of the nation's taxpayers. Mr. Chairman, if you had a bill in excess of $100 billion, I know you'd check to see if the work had been done to your satisfaction. So why doesn't the federal government?

Clearly, senior agency managers need to be reminded that the goal of awarding a contract is to have a service performed in an effective and efficient manner. A contract is a means to an end, not an end in itself. Agencies should be required, as part of the contract administration process, to review the service contractor's performance prior to payment to ensure that it achieved the requisite levels of effectiveness and efficiency. Failure to do so will provide contractors with no incentives to improve upon their work.

13. Bonuses Must Be Used as Rewards for Superior Work, Not as an Entitlement Program for Underachieving Contractors

In my dictionary, "bonus" is defined as something given in addition to what is due. I can only conclude that some senior agency managers are using another dictionary because GAO reports that bonuses are being given out to contractors who have only just met contractual requirements, and even to some who have fallen short, often grievously so.[16] As GAO points out, if bonuses are awarded automatically, they reduce the contractor's incentive to provide timely, high-quality work.[17] OMB should promulgate rules that provide senior agency managers with sufficient guidance to make responsible decisions when deciding whether to award bonuses. A bonus should be given as a reward for superior performance, not as part of some government entitlement program for service contractors, no matter how underachieving.

---

[14] GAO, FEDERAL CONTRACTING: Cost Effective Contract Management Requires Sustained Commitment (GAO/T–RCED–93–2) (December 1992), p. 3.

[15] OMB, Summary Report of Agencies' Service Contracting Practices (January 1994), p. v.

[16] GAO, FEDERAL CONTRACTING: Cost-Effective Contract Management Requires Sustained Commitment (GAO/T–RCED–93–2) (December 1992), p. 8. "(GAO) found that EPA had granted interim award fees to contractors whose performance was rated as less than satisfactory at the end of the contract. (GAO's) 1988 report disclosed that 6 contractors in (its) sample of 11 that had received a less than satisfactory overall performance rating earned between 29 and 45 percent of the available award fees . . . Similarly, in (GAO's) 1989 review that included six DOE-award fee determinations, the contractors' environmental performance was rated as satisfactory or better. As a result, these contractors received the majority of the available award fees even though they had been cited for repeated Resource Conservation and Recovery Act (RCRA) violations. For example, one of these contractors was cited by EPA and a state for 17 RCRA violations yet received an 'excellent' rating for environmental management."

[17] Ibid.

14. Agency Managers Must Audit Their Contractors' Bills as If They Were Spending Their Own Money

Agency managers must conscientiously audit the work of their contractors to ensure that the government pays no more than what it should for the services it procures. As GAO reports, "(i)ndependent audits show millions of dollars in unallowable and questionable costs have been charged that do not contribute directly to the agency's intended mission."[18] And during just a six-month period in FY 93, defense contractors returned to the government $751 million, and in FY 94 they returned $957 million, most of which appears to have been overpayments.[19] If those gigantic sums are being returned, would it be too cynical to ask just how much money is being kept?

Requiring agencies to systematically audit a representative number of their contracts will keep the government from overpaying and being overcharged and help to provide service contractors with the incentives necessary to improve their work.

15. Agency Managers Must Prevent Service Contractors From Taking Federal Property and Using it as Their Own

Better auditing will also allow the federal government to recover the expensive materials and equipment agencies purchase for their service contractors. Imagine for a moment that you are a homeowner who has determined that it would be more effective and more efficient to hire someone to paint your house than to do the work yourself. And imagine that after hiring this person, presumably in possession of the requisite skill and ability, you pay her the money needed to procure the materials and equipment necessary to perform the service, i.e., paints, brushes, trucks, ladders, smocks, etc. Then, imagine that after completing your assignment, this splendidly-equipped painter keeps the materials and equipment you provided for the painting of your house, and then proceeds to use those supplies for her own benefit. Well, something very much like that happens in too many federal service contracts because the law does not specifically provide for the return of such materials and equipment, and neither do most contracts.

Mr. Chairman, what would you say if I told you that billions and billions of dollars in government property had mysteriously disappeared? Would you think that I was telling you about some episode of "The X Files" in which kleptomaniacal aliens visited Earth, filled up their shopping bags with federal property and then zoomed back to the faraway but newly-enriched planet they call home? Unfortunately, the losses suffered by the federal government are not the figment of a science fiction screenwriter's lurid imagination.

Several years ago, the House Committee on Government Operations reported that more than $40 billion worth of materials and equipment purchased by the federal government for use by contractors in the performance of their services was still in the possession of those contractors.[20] The report noted that, in many cases, contractors had improperly used this federal government property to perform commercial work unrelated to the contract. In addition, according to the report, some of that property had even been sold back to the government. Well, I think we've all dealt with the proverbial parasitical neighbor who borrows a lawnmower, rake or some other garden implement which he can't be persuaded to return without dire threats of criminal prosecution, but at least he never tried to sell us back our own property! Clearly, many contractors will continue to have sticky fingers until Congress insists that agencies use tougher audits to clean up the mess in contracting.

The findings of that 1985 Congressional report have not been followed up on by the executive branch to determine whether these inept management practices have been corrected and the wasteful giveaways stopped. Last year, however, GAO reported that almost $75 million of government property had been lost by a single contractor at just one DoE facility.[21] Even worse, that $75 million figure is only the tip of the iceberg. As GAO reports, "this amount represents only what the contractor reported to DoE as missing. We believe that figure probably understates the actual amount of missing property, in light of our detailed review of property management at the (facility)." Where are Rush Limbaugh and the rest of the radio shock show hosts when you really need them?

---

[18] GAO, FEDERAL CONTRACTING: Cost-Effective Contract Management Requires Sustained Commitment (GAO/T–RCED–93–2) (December 1992), p. 11.

[19] General Accounting Office, Defense Contract Management (February 1995), p. 6.

[20] House Report 99–139 (May 21, 1985).

[21] GAO, Managing DOE: Government Property Worth Millions of Dollars Is Missing (GAO/T–RCED–94–309) (September 1994).

16. Congress Must Level With the Taxpayers About Just How Much Service Contracting Really Costs ($105 Billion+)

Isn't it time that contractor expenses were listed as a line item in the federal budget, instead of being scattered here, there and everywhere throughout the eye-straining fine print of that massive tome? As Everett Dirksen is said to have observed, a billion here, a billion there, and pretty soon you're talking about real money. Well, $105 billion, the extraordinary sum the federal government spends every year on services of varying quality and timeliness from contractors, is real money by anyone's definition.[22] Displaying prominently the staggering grand total for service contractor expenses as a line item in the federal budget will do much to bring the crisis in contracting to the attention of policy-makers and taxpayers alike.

17. Congress Must Require Service Contractors to Make the Same Sacrifices That Federal Employees Have Already Made to Save Money for the Taxpayers and Reduce the Deficit

As Members of the Subcommittee know, federal employees have already shouldered a disproportionate share of the burden of deficit reduction. Reductions in federal employee compensation from 1981 to 1994 have already saved the federal government almost $170 billion, according to figures compiled by OMB and the Office of Personnel Management (OPM).[23] And, of course, 272,900 federal employees will lose their jobs through downsizing over the next five years.

But while federal employees have been making one sacrifice after another, year after year, in order to achieve deficit reduction and advance the reinvention of government initiative, service contractors have been digging deeper and deeper into the public purse. In fact, OMB reported earlier this year that service contracting is the fastest growing part of federal procurement, now accounting for more than one-half of the $200 billion spent each year by the government for goods and services.[24]

If Dickens had been alive today and interested in public policy he might have referred to this strange turn of events as a tale of two workforces. For the contractor workforce it is the best of times. Even in the face of mounting concern over massive cost overruns and shoddy work, funding for the contractor workforce grows and grows. But for the federal workforce it is the worst of times. Despite making the sacrifices necessary to bring about dramatic improvements in the effectiveness and efficiency of service delivery, federal employees must still engage in a Sisyphean struggle every year merely to secure the wage increases guaranteed to them by law.

This is wrong! When will Congress insist that contractors emulate the example of federal employees by shouldering their fair share of the burden of deficit reduction in order to advance the national interest? What possible rationale can there be for treating similarly-situated workforces so very differently? What reasons can be advanced to support reductions in the more efficient and the more effective federal workforce and, at the same time, increases in the more costly and the more wasteful service contractor workforce?

---

[22] OMB, Summary Report of Agencies' Service Contracting Practices (January 1994), p. iv. In his testimony before your Subcommittee last week, Mr. Chairman, OMB Deputy Director for Management John Koskinen estimated a "total of approximately $108 billion in service contracts in FY 1994." Please keep in mind that both the $108 billion and the $105 billion figures are based on information from calendar year 1993. Considering that service contracting is the fastest-growing part of federal procurement and one of the fastest-growing expenses in the entire federal budget, those figures are likely to constitute significant underestimates. Based on off-the-record conversations with OMB's policy analysts, the actual amount the federal government currently spends on service contracting is probably in excess of $125 billion. The Professional Services Council, in its recent testimony before the Subcommittee on Government Management, Information and Technology, House Committee on Government Reform and Oversight, erroneously stated that the grand total of federal service contracting "was approximately 70 billion dollars." (Statement of the Professional Services Council on Privatization, March 14, 1995)

[23] Federal Government Service Task Force, "Changes Affecting The Pay And Benefits Of Federal Employees" (January 1993). This chart was assembled by a respected legislative service organization, using data compiled by OMB and OPM. Its accuracy has been verified by GAO. The chart reveals, year-by-year, some fourteen different types of cuts in compensation for federal employees, including: 1) reductions in scheduled pay increases; 2) delays in scheduled pay increases; 3) reductions in health benefits; 4) Medicare tax increases; 5) elimination of paid holidays from lump sum pay-outs; 6) revised computations of GS pay from 2080 to 2087 hours; 7) elimination of 1% add-on to retiree COLAs; 8) revision of minimum benefits for disability retirement; 9) repeal of look-back annuity guarantee provisions; 10) semi-annual to annual COLA adjustments; 11) limitation of COLAs to one-half of the Consumers Price Index for retirees under age 62; 12) delays in COLAs from June to December; 13) revision of eligibility requirements for disability retirement; 14) sequestration of COLA required by the Deficit Reduction Act.

[24] OMB, Summary Report of Agencies' Service Contracting Practices (January 1994), p. iv.

18. Congress Must Insist That OMB Document the Actual Size of the Burgeoning Service Contractor Workforce

The most distressing aspect of this crisis in contracting is that we just don't know how big the crisis really is because we just don't know how big the contractor workforce really is. Considering that the federal government now spends at least a whopping $105 billion per year on thousands and thousands of labor-intensive service contracts, the contractor workforce is somewhere between 1,000,000 and 2,000,000 employees. I'm sorry I can't provide the Subcommittee with a precise figure, but then our friends at OMB can't provide one either—and that's their job. And, absent the force of legislation, the light of truth will never begin to shine on what has been shrewdly dubbed the "shadow government." As points of reference, however, the Members of the Subcommittee should keep in mind that the 2,017,167 employees who make up the entire federal workforce earn a combined $75.3 billion in salary per year.[25] Officials at OMB talk often about making the federal government run more like a business. But is there a single firm in the private sector that fails to keep any records about a mushrooming subset of employees who make up anywhere from one-third to one-half of its total workforce? I very much doubt it. In previous hearings, Mr. Chairman, you have shown great interest in this matter, and I urge you and your staff to aggressively pursue that inquiry.

19. Congress Must Recognize That Federal Employees and Service Contractor Employees Ultimately Work for the Same Employer

As part of the reinvention initiative, OMB is charged with supervising the downsizing of the federal government's workforce. At the risk of sounding like a New Age prophet, I urge the Members of the Subcommittee to take a holistic view of the federal government's workforce. The overall federal workforce is made up of federal employees and contractor employees. Federal employees and contractor employees are ultimately part of the same workforce.

Now, reinvention requires that almost 272,900 federal employees be separated from the federal government's workforce during the next five years. At the same time, however, service contracting will continue to be the fastest growing area of federal procurement. Consequently, one part of the federal government's overall workforce is shrinking, while the other part is growing. But since the contractor workforce is shrouded in secrecy, its phenomenal level of growth goes unnoticed, allowing OMB to point to the reduction in the number of federal employees and claim that the federal government's workforce is actually shrinking. However, we know better. Downsizing federal employees while upsizing contractor employees only wrongsizes the federal government's overall workforce and capsizes the American taxpayers. In fact, absent the sort of service contracting reform we've been talking about here today, downsizing OMB-style will lead to an increase, not a decrease, in federal spending. This is reinvention? No, this is ridiculous!

20. Congress Must Take the First Step Towards Service Contracting Reform by Reducing Contracting Expenses by 10 Percent, Saving the Taxpayers $50 Billion—but Without Reducing Services

Considering the phenomenal level of growth in federal service procurement in recent years and the apparent lack of interest of the executive branch in even broadly defining the parameters of this very serious problem, it is imperative that Congress take the lead in dealing with the crisis in contracting. Therefore, I urge the Members of the Subcommittee to begin that important process by working to achieve a 10% reduction in the federal government's service contracting expenses. Such an initiative will not just save the nation's taxpayers over $50 billion during the next five years, but it will also ensure that agencies only resort to service contracting when the work cannot be performed more effectively and more efficiently in-house.

To see the effect such a reform would have, let's take a closer look at the Department of Energy (DoE), a mere shell of an agency in which service contracting has been allowed to run amok—partly as a result of an FTE ceiling which has forced much wasteful service contracting.[26] In FY 93, almost four-fifths of DoE's $24 billion budget went towards paying off service contractors.[27] Almost $11 billion was used to provide compensation for the massive service contracting workforce.[28] DoE's fed-

[25] OPM, Pay Structure of the Federal Civil Service (March 31, 1993), pps. 12–13.

[26] According to GAO, DoE is one agency in particular which has been forced to take a cost-savings-be-damned policy on service contracting because of its in-house personnel ceiling. (General Accounting Office, GOVERNMENT CONTRACTORS: An Overview of the Federal Contracting-Out Program (GAO/T–GGD–95–131) (March 29, 1995), p. 12.

[27] Inside Energy/with Federal Lands (March 6, 1995), p. 2.

[28] Ibid.

eral employees received slightly more than $1 billion in salaries and wages.[29] As one DoE official said in trying to make sense of the agency's one-sided workforce, "Basically . . . the only way of making a significant dent in DoE's budget will be to require substantial reductions in contract personnel."[30] But how will that be possible when, on the one hand, FTE ceilings prevent the agency from bringing work back in-house where it can be performed by reliable, cost-efficient federal employees and, on the other hand, certain Members of Congress demand that the federal government contract-out over the next four years more than fifty percent of the services it currently provides? To say that DoE's senior managers face a challenge would be to engage in understatement on a grand scale. And let's remember that this sorry situation is in no way unique to DoE.

To the agency's credit, Secretary Hazel O'Leary and her staff are attempting, however haltingly, service contractor reform. Whether their effort will prove to be a model for other agencies remains to be seen. However, we can say that no elaborate schemes or strategies were necessary to begin to deal responsibly with the agency's own crisis in contracting. Instead, Secretary O'Leary merely hinted to DoE's army of service contractors that their contracts would no longer be automatically renewed. The results? Service contractors offered to reduce their billion dollar bills by 15% to 20%.[31]

Imagine the savings that would be generated if the federal government insisted that service contractors at every agency cut that much waste, fraud, and abuse out of all their contracts! If taking the first step towards real service contracting reform is that easy, why is Congress sitting by idly while the crisis in contracting in every agency grows ever larger? Mr. Chairman, you and your colleagues deal every day with that wearisome conundrum: how to reduce the deficit without cutting important services? Well, here's your answer: cut service contractors' expenses by imposing a ten percent reduction on their billion dollar bills—without any effect on their ability to deliver services.

I realize that federal service contractors with their well-placed friends in the legislative branch and their overflowing campaign funds wield enormous influence on Capitol Hill, far more than the working and middle class Americans who belong to federal employee unions like AFGE, but for how much longer can Congress manage to resist the irresistible? To paraphrase a British statesman from earlier in this century, federal service contractors should be squeezed, as a lemon is squeezed—until the pips squeak. My only doubt is not whether there is enough juice in those lemons to meet a significant fraction of our deficit reduction needs, but whether Congress will ever get around to squeezing them hard enough.[32]

CONCLUSION

In closing, Mr. Chairman, I'd like to put the contracting-out/privatization mania sweeping Capitol Hill I spoke of earlier in perspective. In the pitched, partisan battles taking place these days in our Nation's Capitol, there are few public policy objectives that unite Americans on the right, middle, and left segments of the political spectrum. One such objective that is gathering increasing bipartisan support is the need to abolish corporate welfare. Last month, the libertarian Cato Institute, the moderate Democratic Leadership Council, and Secretary of Labor Robert Reich held an extraordinary joint media conference to press Congressional lawmakers like yourselves to take a long, hard look at costly taxpayer subsidies to politically well-connected businesses.

Corporate welfare—estimated by the Cato Institute to be more than $86 billion per year and by the Democratic Leadership Council to be almost $265 billion annually—includes a wide variety of ingenious but completely taxpayer-subsidized giveaways, everything from income tax exemptions worth more than $18 billion over five years for firms doing business outside of the U.S. to subsidies for ski resorts and casinos in some of America's toniest towns. But, as The New York Times pointed out, "little is being done to curb (corporate welfare) practices." "Why?" you might ask, Well, according to the newspaper's account, "Many of them are popular with

---

[29] Ibid.

[30] Ibid, p. 3.

[31] The 'specter of competition' at DoE has proved so frightening that "some contractors (have offered) to reduce costs by 15 percent to 20 percent . . . 'If implied competition will do that, imagine what real competition will do,' (a senior agency official) quipped." (The Washington Post, "Energy Dept. Plans Competition for Big Contracts (July 7, 1994), p. A24.)

[32] "The Germans, if this Government is returned, are going to pay every penny; they are going to be squeezed, as a lemon is squeezed—until the pips (seeds) squeak. My only doubt is not whether we can squeeze hard enough, but whether there is enough juice." Sir Eric Geddes (1875–1937)

politically influential businesses and other groups that are heavy contributors to both Republicans and Democrats."

Should the taxpayers, whose backs are already straining from having to support "politically influential businesses and other groups that are heavy (campaign) contributors" now be required to take on the additional burden of propping up an ever-expanding army of service contractors that possesses connections and influence but, as the record show, often offers little in the way of effectiveness and efficiency? Members of Congress, if they are genuinely interested in saving money for the taxpayers, reducing the deficit, and putting American businesses back on the free market, must give very serious consideration to that question before selling off large chunks of the federal government to politically well-connected private sector operators.

Contracting-out advocates often claim that we have much to learn from local governments. How right they are! Unfortunately for them, those lessons are the opposite of what they intended for us to learn. According to the International City/County Management Association, "The first signs of discontent with service contracting are already visible: several local governments have reestablished themselves as the principal deliverers of services formerly contracted out, and more will no doubt follow their example. Among others, Phoenix, Arizona, and Arlington, Virginia, have found that contracted services can be delivered in-house and at less cost than through contracting out by establishing more efficient and effective service delivery systems than those that existed when the services were originally contracted to the private sector."[33]

In fact, public policy analysts have even coined a term to describe this welcome development: "publicization." The logic behind publicization is both simple and irrefutable: if a private contractor can deliver a service more cheaply than the federal government and make a profit, the federal government can probably find a way to deliver that service as economically as a private contractor, but without sacrificing timeliness and customer satisfaction.

The real lesson we must learn from our friends at the local level is that the more management and labor work together as partners to identify problems and craft solutions in accordance with the common goals of productivity, efficiency, and quality customer service, the less tempted some politicians will be to waste the taxpayers' money contracting-out important federal services. AFGE's members are committed to working with the Administration and Congress to make the federal government the world's ultimate service provider and a source of pride for the citizens it serves. We would welcome the active and sincere involvement of the Members of this Subcommittee in that process.

That concludes my testimony. Thank you again, Mr. Chairman, for allowing me the opportunity to submit this material for the record. I would be happy to answer any questions Members of the Subcommittee may have about the views expressed herein about the federal government's crisis in contracting.

QUESTIONS FROM HON. JOHN L. MICA AND ANSWERS FROM JAMES B. KING, DIRECTOR, OFFICE OF PERSONNEL MANAGEMENT

1. What system does the Office of Personnel Management have in place to monitor the right of first refusal and ensure contractor compliance?

Under Federal Acquisition Regulations, when an agency's functions are contracted out, its employees are afforded rights of first refusal to work for contractors who succeed in winning cost competitions conducted under Circular A–76. As part of the overall procurement process, individual agencies are responsible for monitoring and enforcing contractor compliance with these rights. OPM's responsibilities do not extend to contractor compliance with procurement regulations.

2. What measures has OPM taken to implement protections for federal employees adversely affected by contracting out decisions, such as priority consideration for positions within the agency, establishing reemployment priority lists, paying reasonable costs for training and relocation, and coordinating with the OPM to provide Governmentwide placement programs?

In contracting out situations, agencies must follow reduction in force (RIF) procedures if any employee will be downgraded or separated as a result of the agency's decision to contract out. Affected workers have the right to compete for retention. For those employees who are separated from Federal employment due to RIF reasons, including contracting out, a wide range of transition assistance is available.

---

[33] International City/County Management Association, Service Contracting: A Local Government Guide, p. 186.

Under OPM regulations, agencies maintain Reemployment Priority Lists through which former agency employees separated by RIF receive reemployment consideration. Agencies are prohibited from filling positions from outside the agency if a displaced agency employee is qualified and available. In our report, we have recommended that legislation be passed to require that agencies give priority consideration to their displaced employees even when filling positions from within the agency. OPM currently does not have the authority to block internal agency movement or require that agencies operate mandatory inplacement programs.

OPM operates a Governmentwide Interagency Placement Program (IPP) which provides displaced employees special employment consideration for vacancies in other agencies over candidates who have never held a Federal position.

In a transfer from one agency to another because of a RIF, relocation expenses may be paid in whole or part by the agency from which the employees transfer or by agency to which he transfers, as may be agreed upon by the heads of the agencies concerned.

Agencies may retrain employees for placement within the same agency or in other Government agencies. Additional assistance, including retraining for placement outside the Federal Government, is available through Department of Labor programs. Under the Job Training Partnership Act, individual States receive funds from the Department of Labor to provide retraining assistance to displaced Federal workers.

In January 1995, OPM published regulations to help affected workers earlier in the downsizing process. Agencies may now issue a Certification of Expected Separation to employees when the agency expects to separate them within 6 months by RIF or contracting out. This notice allows employees to register up to 6 months before separation for placement and retraining programs administered by an agency, OPM, and the Department of Labor.

The following is a comprehensive list of programs and benefits currently available to employees displaced as a result of a decision to contract out work. These benefits are also available to employees reached for RIF actions for other reasons. Also included is a list of those benefits and programs available only to Department of Defense displaced employees and a list of transition services now provided to employees in some agencies and locations.

GOVERNMENTWIDE PROGRAMS AND BENEFITS AVAILABLE TO EMPLOYEES SEPARATED BY REDUCTION IN FORCE

PLACEMENT ASSISTANCE

Interagency Placement Program (IPP)—A pre- and post-RIF program administered by OPM to give employees who were or will be separated priority reemployment consideration for positions in other Federal agencies over applicants who do not have Federal status when agencies fill jobs from competitive examinations.

Reemployment Priority List (RPL)—Primarily a post-RIF program administered by individual agencies that gives separated employees priority for vacancies in their former agency over candidates who are not agency employees.

MODIFICATION OF QUALIFICATION REQUIREMENTS

Agencies may modify qualifications standards for inservice placement actions of RIF-ed employees if the agency determines that the employee can successfully perform the work of a position even though the employee may not meet all OPM qualification requirements .

JOB INFORMATION

Career America Connection—A touch tone telephone system which provides up-to-date job information.

Federal Job Opportunities Bulletin Board—A computer-based bulletin board system which provides general and specific employment information, current worldwide Federal job opportunities, and salary and pay rates. This information is also available through OPM Federal job information touch screen computers which are pc-based systems that use touch screen technology to provide job seekers with daily updated worldwide Federal employment information at the touch of a finger. Key features include: current worldwide Federal job opportunities, information on the hiring process, general and specific employment information, and the capability for individuals to request application materials.

Federal Employment Information Centers—OPM Federal Employment Information Centers are located throughout the United States to provide up-to-date information on Federal employment opportunities.

ADVANCE WARNING OF SEPARATION

Agencies may issue a Certification of Expected Separation to employees when the agency expects to separate them within 6 months by RIF. This notice allows employees to register early for outplacement and retraining services provided through their agency, OPM, and the Job Training Partnership Act administered by the Department of Labor. By law, Federal employees are entitled to 60 day advance notice of RIF separations.

JOB TRAINING PARTNERSHIP ACT (JTPA)

A Department of Labor program which disburses funds to the individual States to provide readjustment and retraining services for individuals who are involuntarily separated from employment. Services may include career counseling, testing, retraining, placement assistance, support services and financial counseling to eligible employees both before and after the RIF.

SEVERANCE PAY

Continuation of pay for up to 1 year for eligible employees separated by RIF using a standard formula based on length of service and age.

UNEMPLOYMENT COMPENSATION

A program administered by the Department of Labor, through agreements with state governments, which provides weekly income for a limited time period to eligible separated Federal employees.

REFUND OF UNUSED ANNUAL LEAVE

Separated employees receive a lump-sum payment for accrued annual leave. (Employees may generally carry over 240 hours of annual leave each year.)

Employees are entitled to have their sick leave recredited if reemployed in the Federal service, or have it added to their total service if eligible for annuity benefits under the Civil Service Retirement System.

PAYMENT OF RELOCATION EXPENSES

Title 5, United States Code, Section 5724(e), and Federal Travel Regulations prepared by the General Services Administration state that in a RIF or transfer of function, expenses may be paid in whole or part by the agency from which the employee transfers or by the agency to which he/she transfers.

RETIREMENT

Discontinued Service Retirement—A discontinued service or involuntary retirement provides an immediate annuity for employees who are separated by RIF provided they have at least 20 years of service and are age 50, or have at least 25 years of service regardless of age.

Refunds—Separated employees who are not eligible to receive an annuity may receive a refund of retirement contributions.

Deferred Annuity—Separated employees who have completed 5 years of creditable civilian service, but are not eligible to receive an immediate annuity, may defer their annuity until age 62 or when eligible.

Using Annual Leave to Gain Retirement Eligibility—Employees close to being eligible for retirement when a RIF separation occurs, may be able to stay on the rolls (beyond the date of separation) if they have enough annual leave to carry them over to the date they become eligible for retirement.

FEDERAL EMPLOYEE HEALTH BENEFITS (FEHB)

Employees who retire on an immediate annuity whether voluntarily or as the result of a RIF may continue their enrollment in the FEHB program if all other enrollment requirements are met.

Employees who are displaced due to a RIF action may continue their health insurance for 18 months past the RIF separation date provided they pay both the employee and Government shares of contributions plus any additional administrative costs.

Employees who separate and are not eligible for an annuity may convert their health insurance to an individual coverage and pay the full cost.

FEDERAL EMPLOYEES GROUP LIFE INSURANCE (FEGLI)

Employees who retire on an immediate annuity may continue their enrollment in the FEGLI program if enrollment requirements are met.

Employees who separate and are not eligible for an annuity may convert their life insurance to individual coverage and pay the full cost.

SPECIAL PROGRAMS AND BENEFITS AVAILABLE ONLY TO DEPARTMENT OF DEFENSE EMPLOYEES

In addition to the other benefits and services listed above, the following benefits and services are available only to Department of Defense employees. Many of these benefits have been authorized under special legislative provisions in annual Defense Authorization bills passed over the last few years.

PLACEMENT ASSISTANCE

DOD Priority Placement Program (PPP)—An internal DOD mandatory placement program which provides placement rights for separated DOD employees to other vacant positions within DOD. When a vacancy occurs, DOD components must consider displaced DOD employees who have matching skills and grades before filling the vacancy through other means. Most internal personnel movement is prohibited if a qualified displaced DOD employee is available.

Defense Outplacement Referral System (DORS)—DORS was developed to assist DOD civilian and military workers and their spouses. This program is administered jointly by DOD and OPM. DORS provides public and private sector employers lists of DOD workers who match skills needed for employers' vacancies. The program is open to all DOD employees and employers, but there is no requirement to use it.

JOB TRAINING PARTNERSHIP ACT (JTPA)

Assistance available for job search or retraining may begin 2 years prior to RIF separation for DOD employees working at components listed on Base Realignment and Closure lists, instead of the maximum 180 days authorized for other employees.

OUTPLACEMENT SUBSIDY

In addition to the option available to all agencies, GSA has permitted DOD to authorize relocation payments for employees who are:

—in receipt of a Certificate of Expected Separation;

—in receipt of a notice or proposed separation as a result of RIF; or

—in particular occupational series and grades designated as surplus by DOD, when it is determined that their voluntary transfer to another Federal agency would create a vacancy for an employee in receipt of a notice of expected or proposed RIF separation. (Payment for this particular action is not available for non-Defense agencies.)

DOD policy allows payment of up to $20,000 in these cases.

UNLIMITED ANNUAL LEAVE CARRYOVER

To encourage retention until closure, DOD employees located at installations designated for closure may carry over unlimited annual leave beyond the normal 240 hour cap.

ADVANCE NOTIFICATION PERIOD

A 120-day RIF notice period (instead of the usual 60 days) is required for DOD employees at activities anticipating 50 or more separations.

EXTENDED FEDERAL EMPLOYEE HEALTH BENEFITS (FEHB) COVERAGE

Employees enrolled in the FEHB Program may elect to continue enrollment for 18 months following separation with the agency continuing to pay its share and any additional administrative costs. Employees would continue to pay their share.

FULL CONSIDERATION

Non-DOD agencies are required by law to give full consideration to qualified displaced DOD employees before selecting a candidate from outside the agency for a vacant position.

NON-FEDERAL EMPLOYMENT INCENTIVE PILOT PROGRAM

The Secretary of Defense may establish a pilot program to pay up to $10,000 retraining and relocation incentives to non-Federal employers to encourage them to hire and retain DOD employees affected by RIF.

VOLUNTARY SEPARATION INCENTIVES PAYMENTS

DOD may offer voluntary separation incentive payments (buyouts) to employees until September 30, 1999.

CAREER TRANSITION SERVICES AVAILABLE IN SOME AGENCIES

Some agencies use internal transition assistance programs to help their displaced employees. These programs are not available in all agencies and locations. Some agencies use in-house employee assistance specialists, personnelists and trainers; others contract with private sector firms which specialize in outplacement and career transition.

Typical services provided include:

Transition Centers/Skills Clinics—both in headquarters and field activities.

Comprehensive Job Vacancy Information:

—Automated Federal Job Opportunity Bulletin Board (FJOB)
—Automated Labor Exchange (State Employment Service)
—Federal Job Information Touch Screen Computer
—Private Sector Employment Information Vacancy Listing

Job Search Information:

—Job Resume Books/Articles
—Job Search Videos

Career Transition Workshops/Training:

—Individualized Job Development
—Interviewing Strategies
—Resume Preparation Programs
—Mounting an Effective Career Search
—Building Networks
—Dealing with Placement Agencies and Search Firms
—Retraining or Reskilling Programs
—Retirement Planning
—Starting Your Own Business Planning
—Decision Training
—Personal Financial Planning

Person-to-Person Counseling:

—Group Career Counseling
—Job Clubs
—Individual Career Counseling (Peer or Professional)
—Employee Profile Development (Occupational, Career Aspiration, Career Planning)
—Diagnostic Assessment Tools (Tests): Abilities, Skills, Interests
—Retirement Planning and Assistance
—Spouse Assistance
—Job Matching
—Employee Assistance Counseling

3. Does the 2,018 employees registered in the IPP on September 16, 1994, reflect all Federal employees separated involuntarily during this period, or only those separated as result of Circular A–76 studies?

The 2,018 employees registered in the IPP on September 16, 1994, reflect employees who requested OPM's assistance due to involuntarily separation by RIF, refusal to relocate with a transfer of function, recovery from a workers compensation injury, or ability to return to work after retiring with a disability. Employees whose functions are contracted out receive RIF notices. OPM provides placement assistance to any Federal worker who receives a RIF notice regardless of the reason for the RIF. We do not monitor reasons for RIFs, and are therefore unable to provide the specific number of RIF-ed employees registered in the IPP due to contracting out.

OPM and agencies have certain obligations toward veterans occupying restricted positions whose functions are contracted out under Circular A–76. Therefore, veterans separated from those positions (i.e., guards, elevator operators, messengers, and custodians) are provided assistance through the IPP. No one has registered in the IPP due to this reason.

4. How many people were hired by Federal agencies during this period and do your records identify the job series of the separated employees and the record of agencies' hiring during that period?

During the period from December 1, 1993 to September 16, 1994, approximately 15,000 hires were made by Federal agencies.

Top Fifteen Occupation Series

[RIF-ed In All Agencies Fiscal Year 1994]

Rank	# RIF-ed	Occup. Series RIF-ed	Occupations
1	418	3111	Sewing Machine Operator
2	262	1810	Investigator
3	243	4204	Pipefitter
4	238	5334	Marine Machinery Mechanic
5	210	3806	Sheet Metal Mechanic
6	172	3414	Machinist
7	168	0318	Secretary
8	167	3820	Shipfitter
9	156	2604	Electronic Mechanic
10	150	2805	Electrician
11	143	0802	Engineering Technician
12	126	0303	Miscellaneous Clerk & Assistant
13	118	3105	Fabric Worker
14	113	3703	Welder
15	105	4102	Painter

Source: OPM Central Personnel Data File

Top Fifteen Occupation Series

[for New Hires In All Agencies Fiscal Year 1994]

Rank	# New Hires	Occup. Series RIF-ed	Occupations
1	745	0007	Correction Officer
2	669	0610	Nurse
3	525	0318	Secretary
4	476	0326	Office Automation
5	410	0621	Nursing Assistant
6	389	1896	Border Patrol
7	370	0105	Social Insurance Adm.
8	362	0334	Computer Specialist
9	329	0962	Contact Rep.
10	247	0301	Misc. Admin.
11	237	0855	Electronic Engineer
12	233	0303	Miscellaneous Clerk & Assistant
13	233	1340	Meteorology
14	230	0185	Social Worker
15	228	0602	Medical Officer

Source: OPM Central Personnel Data File

Our records show that displaced employees generally do not have the same occupational skills required for jobs in other Federal agencies. For example, of the top 15 occupations in which RIFs occurred, only 2 were among the top 15 occupations with the most new hires.

5. Do your records indicate any effort on the part of OPM to provide additional training for separated employees? If so, please describe those measures. If not, please explain?

Agencies may retrain employees for placement within the same agency or in other Government agencies. Additional assistance, including retraining for placement outside the Federal Government, is available through programs administered by the Department of Labor. Under the Job Training Partnership Act, individual States receives funds from the Department of Labor to provide retraining assistance to displaced Federal workers.

6. Do you have any additional information that you might provide to describe OPM's efforts to monitor the A–76 program's effects on Federal employees?

In January 1995, OPM published regulations to help affected workers earlier in the downsizing process. Agencies may now issue a Certification of Expected Separation to employees when the agency expects to separate them within 6 months by RIF or contracting out. This notice allows employees to register up to 6 months before separation for placement and retraining programs administered by an agency, OPM, and the Department of Labor.

OPM extensive study of transition assistance resulted in several recommendations to improve assistance provided to displaced employees. We found that a wide range of tools and strategies is necessary to best help affected workers. The recommended new initiatives are built around three major themes:

- empowering RIF-ed employees to take charge of their own careers through a new model of transition assistance which provides:
  —placement assistance and selection priority from their own agencies through mandatory inplacement programs;
  —interagency job search assistance; and
  —selection priority in other agencies when they apply and are well qualified.
- improving transition support for employees by giving all Federal agencies access to the same kinds of tools and assistance programs, including:
  —earlier assistance under the Job Training Partnership Act;
  —studying the feasibility of continuing the employer share of health benefits after separation at agency discretion to facilitate placement of employees in the private sector;
  —continuing access to agency counseling and employee assistance programs for up to one year after a RIF;
  —cross-agency buyouts to create placements; and
  —authority for agencies to use a full range of professional transition services including fee for placement assistance.
- developing new incentives for public and private sector employers to use on a discretionary basis to hire displaced Federal workers, including:
  —vouchers for retraining/relocation;
  —no-cost tryouts;
  —FTE ceiling relief for the first year after a displaced worker is hired; and
  —new probationary period when an agency modifies qualifications to hire a displaced employee from another Federal agency.

These initiatives represent significant new directions in employee outplacement assistance programs. Some will require legislative approval by Congress. Others can be implemented by regulations, executive orders or local agreements. To gain more experience with these new approaches, some may best be tested on a local basis or implemented as models to gauge their effectiveness. OPM intends to pursue such initiatives vigorously.

7. Can OPM provide examples of cities where Federal Executive Boards or other interagency organizations have facilitated transitions for people affected by contracting decisions?

To expand the availability of outplacement help to displaced employees, OPM is working with agencies to establish interagency assistance centers which provide help to any Federal displaced worker. The following are examples of innovative interagency programs at the local level:

SACRAMENTO, CALIFORNIA

Currently, OPM has a partnership with Federal agencies to operate such a center at McClellan Air Force Base, California, for displaced employees in the greater Sacramento area. This project has been well received and OPM is extending its efforts to other areas in the country, especially those severely affected by downsizing and restructuring.

The Sacramento Army Depot Activity (SADA) was identified for closure by the Base Realignment and Closure Commission. To assist in the outplacement of its employees during the downsizing, the SADA opened a Future Opportunities, Career and Ultimate Success (FOCUS) Center. The Center offers a variety of services ranging from computerized employment application programs to extensive job vacancy listings for public and private sector positions.

In anticipation of other agencies facing downsizing and knowing the extensive start-up costs to establish an effective outplacement center, OPM proposed continuing operation of the FOCUS Center as a transition assistance and career resource center to help all displaced Federal Government employees in the area.

The Center's mission is two-fold: 1) to act as an outplacement center for Depot employees who are looking for employment and other Federal employees from local agencies who are in receipt of a reduction in force notice; and 2) to serve as a career

resource center for local agency employees so that they could, on their own, pursue a job change and hopefully reduce the need for or the number of employees affected by a RIF. The partners also agreed that if McClellan Air Force Base was affected by another major RIF, the Center would return to being strictly an outplacement center.

Together, the SADA, McClellan Air Force Base and OPM operate the FOCUS center to help displaced employees, with OPM being administratively responsible for the program. The State of California's Employment Development Department also provides a staff member to assist employees with their job searches.

SAN FRANCISCO, CALIFORNIA

The OPM San Francisco Service Center uses its job information mini-van as a mobile outplacement center. The mini-van is designed and equipped to assist agencies undergoing downsizing related activities. OPM Service Center staff are able to work directly from the vehicle providing information to employees on transfer, reinstatement, employment opportunities, OPM Interagency Placement Program registration and general employment counseling services.

TWIN CITIES, MINNESOTA

The Federal Employment Council, a subcommittee of the Federal Executive Board's Equal Employment Opportunity Committee, recently implemented an Informal Outplacement Assistance program. The referral program is designed to assist candidates in the Twin Cities metropolitan area whose jobs may be threatened by reorganization or downsizing.

Employees who have serious concerns about their job security may complete a registration form and submit it to the Federal Employment Council. The Council maintains a computerized list of applicants. Agencies who have vacancies may request a list of status candidates who have indicated an interest in the appropriate occupation. Participation is voluntary for both the employee and the employer.

Upon referral, the agency may contact the individuals to request an application/resume and verify that both appointment eligibility and qualification requirements are met.

WASHINGTON, DC

In Washington, D.C., the Interagency Advisory Group (personnel directors of Executive Branch agencies) has formed a Career Transition Committee which is looking to develop strategies for sharing outplacement and transition services across Federal agencies.

[NOTE.—To reduce publication costs, the subcommittee has omitted from the record a report entitled, "New Directions, Improving Transistion Assistance for Federal Employees Affected by Downsizing." A copy of the report may be found in the subcommittee files.