Work Reserved for Performance by Federal Government Employees

OFPP Draft Policy Letter dated March 31, 2010

Issues and Challenges

a

White Paper

Prepared by a Task Force of the American Bar Association
Public Contract Law Section
Privatization, Outsourcing and Financing Transactions and Battlespace Committees

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Defining work that is or is not to be performed by Federal employees has vexed many in the past. OFPP's proposed policy letter on the subject of "Work Reserved for Performance by Federal Government Employees" represents a big step in articulating criteria for agencies to apply when deciding whether to contract or to rely upon in-house resources. The task force offers the following thoughts on the draft policy letter designed to encourage thinking on ways to tighten and refine the thoughtful approach evident in the draft policy letter.

I. BACKGROUND

On March 31, 2010, OFPP issued a "Notice of proposed policy letter" entitled "Work Reserved for Performance by Federal Government Employees." Federal Register, Volume 75, Number 61, pp. 16189 - 16197. As explained in the Overview section of the notice, the purpose of the proposed policy letter ("Policy Letter") is "to provide guidance addressing when work must be reserved for performance by federal employees."

The proposed Policy Letter follows the President's March 4, 2009 Memorandum on Government Contracting which required OMB to "clarify when outsourcing for services is or is not appropriate." The President's Memorandum directed OMB to undertake this effort consistent with Section 321 of Public Law 110-417, the National Defense Authorization Act for FY 2009. Section 321 obligated OMB to develop a single consistent definition for the term "inherently governmental function" as that term was used in identifying work that could be outsourced to the private sector and work that must be performed by Federal government employees. Definitions of "inherently governmental function" currently reside in the Federal Activities Inventory Reform Act of 1998, Public Law 105-270, 31 USC 501 (the "FAIR Act"), 10 USC 2383, OMB Circular A-76 and the Federal Acquisition Regulation. Section 321 went further to direct that OMB develop criteria to assist agencies in identifying "critical functions" that are not inherently governmental, but nevertheless should be performed by Federal government employees to ensure that the government maintains control of its mission and

operations and to identify positions where government employees are required to develop and maintain sufficient organic expertise and technical capability within an agency.

In the notice, OFPP poses a number of questions and welcomes comments from the public. This White Paper offers a discussion of issues which run through several of OFPP's questions. The White Paper discussion does not align directly with the OFPP questions, however. Where the discussion relates to a specific question or questions, we have identified that question or questions.

In general, this White Paper offers thoughts on simplifying the policy by reducing the number of categories of functions that are treated in the policy. Specifically, the category of "functions closely associated with the performance of inherently governmental functions" could be eliminated thereby leaving two categories, i.e., "inherently governmental" functions and all other functions that for reasons of agency control of mission and operations or retention of critical expertise require a balancing of considerations before deciding whether Federal employees or private entities, or a mix, are required or appropriate. Additionally, 1) the definition of "function" in the Policy Letter could be defined to distinguish "function" from "position" and "activity," 2) detailed guidance on Organizational Conflicts of Interest ("OCIs") might better be left to other policy statements or regulations, 3) a temporary exception could be recognized for agencies that under the Policy Letter are to use Federal employees but do not have those resources when required, 4) OFPP might consider advising agencies that are engaged in insourcing activities in advance of the final Policy Letter to withhold taking action until the proposed Policy Letter is final (and that OFPP withhold issuing the final Policy Letter until current legislative proposals regarding insourcing are final) and 5) OFPP could consider as part of the Policy Letter, or separately, issuing guidance on how to conduct cost analyses when the Policy Letter makes cost-effectiveness a criterion.

II. ISSUES

A. Eliminate "Functions Closely Associated with the Performance of Inherently Governmental Functions" as a Class for Individual Treatment Under the Proposed Policy Letter

The Policy Letter might be simplified by eliminating the category of "functions closely associated with the performance of inherently governmental functions," leaving "inherently governmental" functions and all other functions that for reasons of agency control of mission and operations or retention of critical expertise require a balancing of considerations before deciding whether Federal employees or private entities, or a mix, are required or appropriate. See question 3(c) of OFPP's notice. In short, although the "closely associated" category currently exists in both statute and regulation, close association with an inherently government function does not obviously warrant placing a function in its own category. A function is either inherently governmental or it is not. If an agency does not have the ability to mitigate the risk of contracting out a function, it should not do so except in limited circumstances. Using another defined term for functions that have heightened management challenges adds needless complexity. Indeed, including the "closely associated" category, which was not included in the section 321 request, adds to the definitional confusion that Congress asked OMB to clarify while it contributes little to the analytical framework. Finally, the Policy Letter refers agencies to

OMB's July 29, 2009, memorandum for guidance on special consideration of federal employee performance of functions in this category, without acknowledging that OMB's memo does not include a "closely associated" category. Indeed, the discussion to which the Policy Letter refers appears to be, at least in part, OMB's description of "critical" functions. This will likely cause, rather than reduce, confusion.

First, the proposed justification for a category of "functions closely associated with the performance of inherently governmental functions" is that "the risk that their performance, if not appropriately managed, may materially limit Federal official's performance of inherently governmental functions." Policy Letter at C.3. Adding this distinct category based solely on the potential management challenges seems unnecessary, as it is axiomatic that every function contracted out must be managed and the amount of oversight required will vary depending on the type of function. And, as the Policy Letter makes clear, agencies must have sufficient staff performing "critical functions" so they are able to maintain control of, or manage, their missions and operations. Ultimately, an agency may determine that it has insufficient management resources to contract out a function, but creating separate categories of functions based on where they fall on this spectrum has the potential for adding confusion to the analytical framework and unnecessarily restricting agencies' ability to re-balance their workforces. Consequently, the OFPP might drop the category and recommend that Congress do the same.[1]

Second, including a category for "closely associated" functions seems contrary to Congress' request for definitional clarity. As the Congressional Research Service has recognized, attempting to "insulate" inherently governmental functions within additional layers of functions that cannot be contracted out "might ... serve only to shift the functions about which disagreements arise." U.S. Congressional Research Service R40641, Inherently Governmental Functions and Department of Defense Operations: Background, Issues, and Options for Congress (Feb. 1, 2010). Rather than further the definitional confusion, OFPP, consistent with Congress' request, could assist agencies in determining what functions are inherently governmental or simply require enhanced management attention or the development of in-house expertise before they can be contracted out.

Finally, the Policy Letter's reference to preceding OMB guidance on the subject of "closely associated" functions may cause unnecessary confusion. In section 5-2(b)(1), the Policy Letter refers to OMB's July 29, 2009, memorandum, Managing the Multi-Sector Workforce, and recommends that civilian agencies refer to Attachment 3 of M-09-26 for guidance regarding the special consideration to using federal employees for "closely associated" functions as required by section 736 of Division D of the Omnibus Appropriations Act, 2009, Public Law 111-8. The Policy Letter then refers to OMB's explanation that Federal employee performance would be

[1] Section 321 of the FY09 NDAA, which OFPP cites, together with the President's March 4, 2009 memo, as the authority for the proposed policy, directed OFPP to report to Congress on any "legislative recommendations" the Director [of OMB] deemed necessary to further the purposes of Section 321. Section 321 makes no mention of functions "closely associated with inherently governmental functions," referring only to "inherently governmental" and "critical" functions. OFPP seems clearly to have the opening to recommend to Congress that any legislation which recognize the category of functions "closely associated" with performance of inherently governmental functions be amended.

expected if contractor performance causes the agency to lack sufficient internal expertise to maintain control of its mission and operations or public sector performance is more cost effective. While OMB's guidance is useful, the Policy Letter might be improved by dropping this reference to external guidance. To the extent OFPP believes directions issued in another document would be useful, we recommend that guidance be directly incorporated into the Policy Letter.

More importantly, as discussed below, Attachment 1 of OMB's 2009 memorandum does not use the "closely associated" category at all. Instead, it divides functions into inherently governmental, critical, and essential. While OMB does briefly discuss in Attachment 3 the special considerations necessitated by section 736 of Division D of the Public Law 111-8, its analysis of when Federal employee performance would be expected appears to be related to the "critical," not "closely associated," functions. This is likely to cause significant confusion. Any confusion might be avoided by dropping the reference in the draft Policy Letter to the OFPP 2009 memorandum.

B. Clarify and Consistently Use the Terms "Function," "Position," and "Activity"

While the proposed Policy Letter uses the term "function" throughout, it is never defined, resulting in multiple inconsistent uses, some of which contradict its ordinary meaning. This condition could be avoided by defining the term and reviewing the Policy Letter to ensure that the term "function" is used consistently throughout.

Simply put, people who occupy positions perform functions. Activities are groups of people who perform functions. i.e. assigned duties, to achieve objectives, including supporting others – at least that is the sense in which OMB Circular A-76 uses the term "activity." The proposed Policy Letter could better use the term "activity" consistently with A-76 instead of using "function." The term "activity" as denoting a group of people makes eminent sense in the A-76 context since the concern there is to evaluate, among other things, whether an organizational unit, that is an activity, would be a logical candidate for outsourcing, which necessarily includes development of a statement of work or another document defining what the organization is to achieve – not an analysis by function or even position.

In contrast, while the proposed Policy Letter impacts the outsourcing issue, it seems to focus more on the positions that need to remain occupied by government employees because of the functions they perform. It would be helpful if it discussed which functions the government needs reassigned from contractor to government employees because the function is inherently governmental or critical.

Unfortunately because the proposed Policy Letter uses "function" to mean both position and function, one cannot tell if the proposed Policy Letter contemplates reassigning a function as opposed to insourcing an entire position. We submit that clarifying and consistently using the terms "function," "position" and "activity" will clarify each agency's analysis.[2]

[2] It would also avoid using the ungainly and obscure term "portions of functions." 75 Fed. Reg. 16189.

An example of the ambiguity created by using "function" to mean function, position and activity, is found in questions 3(a) and 3(d) which OFPP poses in its March 31, 2010 notice:

> 3. Closely associated and critical functions
>
> a. Should the policy letter set out a presumption, or a requirement, in favor of performance of "closely associated" and/or critical functions by federal employees?
>
> d. What, if any, additional guidance might be provided to help agencies identify the extent to which a critical function may be performed by a contractor?

While the proposed Policy Letter tries to make clear that not everyone performing closely associated and critical functions need be Federal employees, the use of the term "function" in these questions suggests that either the presumption applies to all positions or it does not. Likewise, the question is not whether a contractor can perform critical functions, but rather are there practical ways for the government to control contractor employees or a contracted out activity by having some government employees occupy "positions" to perform that function or occupy other key positions that control that contractor's performance, e.g., contracting officer's technical representatives, program managers, etc.

An example of Congress using the terms "position" and "function" consistently is Section 820 of the John Warner National Defense Authorization Act for Fiscal Year 2007, P. L. 109-364. Congress entitled the section, "Government Performance of Critical Acquisition Functions," but named five positions that DoD needed to target to be filled by Federal employees on major defense acquisition programs. For example, many system engineer positions can be filled by contractors under section 821 although the function is called critical.

C. Treatment of Organizational Conflicts of Interest ("OCIs") Resulting from Private Sector Performance of Functions, Positions or Activities Could be Reserved for Separate Policy Guidance

The proposed Policy Letter currently identifies the avoidance or mitigation of OCIs as a special consideration whenever functions closely associated with the performance of inherently governmental functions are being performed by a contractor. Proposed Policy Letter at 5-2a(b)(4). The proposed Policy Letter goes further and provides detailed guidance on what might be done to avoid or mitigate an OCI such as physically separating the contractor from government personnel at the worksite or having the contractor work offsite. Putting aside the practicality of such physical separation where, by definition, the work is "closely associated with" inherently governmental work, the proposed Policy Letter might leave the details of OCI avoidance or mitigation to other, more comprehensive, policy statements or regulations. The proposed Policy Letter correctly should refer to conflict issues and conflict of interest rules, but it need not create any special categories of services that need more attention outside of the standard rules or details on how to avoid or mitigate the conflict. To do so creates unneeded complexity in an already complex area and potentially divergent results between the different areas.

What currently appears in the proposed Policy Letter on OCIs appears too brief to be of much help to agencies and too pointed to ignore, e.g., physical separation. The suggestions in the Policy Letter may or may not assist in resolving any particular conflict. The recently released proposed Department of Defense Federal Acquisition Regulation Supplement ("DFARS") rule and the soon expected FAR proposal on OCIs will provide the requisite guidance in an already complex area.

D. Need for an Exception from Federal Employee Performance in Specified Circumstances

OFPP's proposed Policy Letter does not contain any exceptions from the requirement, after application of the Policy Letter's guidance, that work be reserved for Federal employees. This might be an oversight, and is in contrast to OMB guidance issued last year. The lack on an exception could cause significant difficulties for agencies that are unable to have all functions the proposed Policy Letter requires be reserved for Federal employees actually performed by Federal employees. For this reason, the draft Policy Letter could incorporate the language from OMB's July 29, 2009 memorandum, M-09-26, entitled "Managing the Multi-Sector Workforce" regarding a temporary exception.[3]

The focus of the draft policy guidance is to assist agencies in determining which functions must be performed by Federal employees by clarifying the definition of inherently governmental function and establishing a test to determine which functions are "critical" such that a certain number of Federal employees must perform them for an agency to maintain control of its mission and operations. The fact that an agency has determined, based on the proposed Policy Letter, that a function must be performed by a Federal employee should not, however, end the analysis. The reality is that, whether because of budget, timing, or other exigent circumstances, agencies may not be able to immediately fill positions where Federal performance has been deemed necessary. OFPP's proposed Policy Letter contains no guidance regarding what an agency should do in such circumstances.

Rather than effectively causing agencies to let what may be necessary work go undone because mandated Federal performance is not feasible, OFPP might incorporate OMB's July 29, 2009, guidance regarding a temporary exception. In its July 29, 2009 guidance, OMB provides criteria for insourcing to civilian agencies pursuant to section 736 of Division D of the 2009 Omnibus Appropriations Act, P.L. 111-8. Attachment 3 of that memorandum, "Criteria for In-sourcing Work Under Public Law 111-8," states:

> In cases in which the … analysis indicates Federal performance, but the agency is having difficulty in recruiting Federal employees or developing Federal employees would take too long, the

[3] A similar exception exists in DOD's "In-sourcing Contracted Services - Implementation Guidance" issued on May 28, 2009. For insourcing based on cost, meaning for positions that are not inherently governmental or otherwise exempted from private-sector performance, if DOD civilian employees are determined to be the most cost-effective provider but cannot be obtained "within the required time frame," requiring officials are instructed by paragraph 5.2.1.2 to obtain contract support on a temporary basis.

> acquisition office should proceed with a temporary contract that provides services to the agency only until Federal employees can be hired.

Such a limited exception might be a practical, and necessary, solution to short-term staffing issues agencies are likely to face after OFPP clarifies the question of which functions must be performed by Federal employees.

Further, in the context of contingency operations contracts, DoD and, in particular, military planners may need a degree of flexibility in permitting contractors to perform jobs that indicate Federal performance both during planning and as contingency operations evolve. The short fused nature of contingency operation planning and the operations themselves do not allow military planners lead time to adjust the Federal and contractor personnel mix to accomplish the goals of the operations plan. For example, recent US contingency operations have utilized contractor personnel for logistical and life support functions due in part to limitations on available uniformed personnel. While under perfect conditions contingency planners may want to use military personnel for some or all of these functions in the contingency operations area, Defense Department end-strength and required troop rotations will continue to make use of uniformed personnel for these and other functions extremely difficult. And required use of uniformed personnel during operation planning may even detract from the military's ability to field a force capable of accomplishing US national security goals. In addition to initial planning decisions, contingency operation planners should have a degree of flexibility in permitting contractor performance of functions that may require Federal performance as circumstances "on the ground" change. Unlike domestic use of contractors, a determination regarding whether a function requires Federal performance may change as the security situation or other factors in a contingency operation evolve. Thus, while adhering to the spirit of the "inherently governmental function" policy, the military likely needs an amount of flexibility not incorporated inn the proposed Policy Letter that permits the use of contractors under changing circumstances. A limited exigent circumstances exception, or urgent and compelling need exception similar to the CICA stay override provisions in 31 U.S.C. § 3553(3)(C)(i)(II), might be practical. Such an exception could be limited to contingency operations (as defined in 10 U.S.C. § 101(a)(13)) and require a re-assessment of circumstances at intervals if the operation becomes extended.

E. Patchwork of Statutory Initiatives May Impede OFPP's Efforts to Unify Government Guidance

The efforts currently underway by Congress and the Administration to clarify what work must be reserved for performance by Federal government employees are commendable. The Federal government is, however, simultaneously pursuing multiple efforts and agencies are moving forward with insourcing initiatives prior to the issuance of OFPP's final Policy Letter. Given Congress' clear intent that OFPP's guidance attempt to unify the various definitions of inherently governmental functions, as well as provide direction to Federal agencies with regard to what other functions must be reserved, in whole or in part, for Federal employees, OFPP might recommend that all agencies pause in their efforts to apply insourcing guidelines until the Policy Letter is finalized. In addition, OFPP might recommend that Congress make the legislative changes necessary to unify Federal law with regard to work that must be reserved for Federal government employees. Finally, in light of legislative developments discussed below, it

may be better to await final enactment of the FY 2011 National Defense Authorization Act ("NDAA") before issuing the final Policy Letter.

First, some agencies are moving forward with insourcing initiatives in advance of OFPP's guidance being finalized. These efforts seem premature, and may impede OFPP's effort to develop a unified definition of inherently governmental function. Arguably, the agencies would benefit from delaying further insourcing actions until the Policy Letter is final.

Second, although section 321(c)(2) of Public Law 110-417 directed OMB to make legislative recommendations "as the Director determines necessary to further the purposes of this section," the proposed Policy Letter provides none. This appears unfortunate, as conflicts with current insourcing initiatives may cause confusion when agencies are asked to implement the Policy Letter later this year. Indeed, OMB's July 29, 2009 guidance on the multi-sector workforce provided criteria for civilian agencies to consider as they develop guidelines for insourcing. In some respects, the July 29, 2009 guidance and the proposed Policy Letter appear to be inconsistent. For example, while both polices include three categories of functions, the categories differ. While both use the terms "inherently governmental function" and "critical function," the July 29, 2009 guidance discusses "essential functions," all of which may be performed by government or contractor employees, while the proposed Policy Letter includes "functions closely associated with the performance of inherently governmental functions." Similarly, the Department of Defense currently has insourcing procedures as required by 10 U.S.C. 2463, enacted in section 324 of the FY 2008 NDAA, P.L. 110-181. DOD implemented these requirements in 2008 and 2009, and is moving forward with insourcing initiatives based on that policy. In addition, 10 U.S.C. 2383 allows the head of a defense agency to contract for functions closely associated with inherently governmental functions only when certain conditions are met.

This patchwork of statutory direction may impede OFPP's effort to bring clarity to this area of law. For this reason, OFPP might take up Congress' request for legislative recommendations that may be necessary to achieve the goals set forth in section 321.

Finally, as OFPP is no doubt aware, Congress currently is considering the FY 2011 NDAA (H.R. 5136). Final passage of the FY 2011 NDAA should not be expected before October 2010.[4] Insourcing is likely to be addressed in the FY 2011 NDAA, but the final bill cannot be known. The bill currently contains at least one provision relating to insourcing. It would prohibit quotas for insourcing, while preserving DOD's ability to insource. It is not possible to predict what the final bill will contain. In light of these on-going legislative developments, it may be advisable to await final enactment of the FY 2011 NDAA before issuing the final Policy Letter.

[4] The FY 2010 NDAA became law on October 28, 2009 (P.L. 111-84); the FY 2009 NDAA became law on October 14, 2008 (P.L. 110-417); the FY 2008 NDAA became law on January 1, 2008 (P.L. 110-181); the FY 2007 NDAA became law on October 17, 2006 (P.L. 109-364).

F. Cost Analysis

The proposed Policy Letter makes "cost-effectiveness" a criterion when assessing any mix of Federal and contractor personnel performing functions closely associated with the performance of inherently governmental functions or performing critical functions. Proposed Policy Letter at 5-2a(b)(1), 5-2b(a) and 5-2b(b)(2)(ii). For example, once an agency has sufficient internal resources to control its mission and operations, performance of critical functions is subject to "cost considerations:"

> "Supporting cost analysis should address the full costs of government and private sector performance and provide like comparisons of costs that are of sufficient magnitude to influence the final decision on the most cost effective source of support for the organization."

Proposed Policy Letter at 5-2b(b)(2)(ii).

With the reliance upon cost considerations in determining an appropriate Federal employee/contractor mix of workers for functions closely associated with inherently governmental functions and for critical functions, there is a significant need to address in either the proposed Policy Letter or separately the issue of how best to undertake a comparison of costs between the private and public sectors for work to be undertaken in the future.

This is an issue that has not been the subject of serious scrutiny for many years, dating back at least to 1983 when OMB issued a modern version of OMB Circular A-76. In 1996, when OMB issued Supplemental Handbook Number 4, OFPP structured a cost comparison methodology; but the methodology was subject to criticism by arbitrarily assigning overhead values of 12% across the board for government enterprises as well as imposing "plug" numbers for personnel costs as opposed to actual loaded labor costs. When OFPP examined the A-76 process in the early 1990s, it made revisions to the procurement aspects of A-76 but did not address the cost comparison methodology.

An issue arises because the public sector does not have in place accounting systems that fully allocate costs to units within government that perform activities. Labor costs can be identified by looking at actual wages (direct labor) and fringe benefits, (loaded direct labor), but there is no systematic way of tracking time spent on a particular matter (i.e. no time cards) so idle labor is not tracked. Similarly, facilities costs are not allocated to the activities in a structured fashion, so idle facilities costs and related utility costs are not tracked.. In recognition of this situation, government agencies frequently resort to surrogate methods to approximate what the total allocated costs should be using methods such as Activity Based Costing, Avoided Costing, and the like.

In contrast, private sector companies who do business with the Federal government must have job cost accounting systems that allocate all costs within the company to the activity level. As such, companies must be able to identify costs for idle labor, idle facilities, all overhead costs (including indirect and G&A costs) and all applicable "other direct costs."

Given the proposed Policy Letter's specific reference to and reliance upon "cost-effectiveness" and the "full costs of government and private sector performance," specific attention could be given to assure that any cost comparisons performed in accordance with the proposed Policy Letter accurately capture the full cost of Federal and private sector-performed work.

III. CONCLUSION

This White Paper is offered with the hope of raising awareness of a number of issues which might simplify and clarify OFPP's guidance. As noted, the question of when work should be reserved for Federal employee performance or contracted out has proven complex. OFPP's draft Policy Letter is a large step in the right direction. The discussion in this White Paper is intended to help move this process positively forward.