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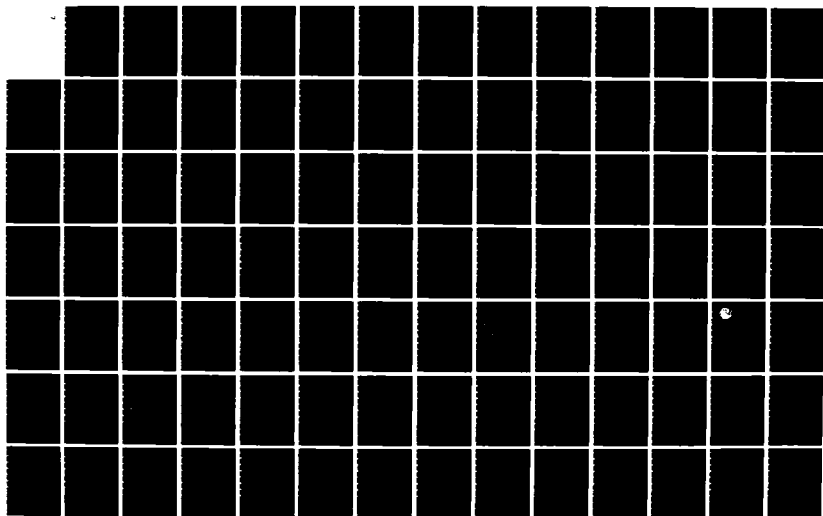
IMPLEMENTATION OF THE COMMERCIAL ACTIVITIES PROGRAM AT
NAVY PUBLIC WORKS CENTER PEEBACOLA (U) FLORIDA UNIV
GAINESVILLE DEPT OF CIVIL ENGINEERING J L BULLOCK 1984
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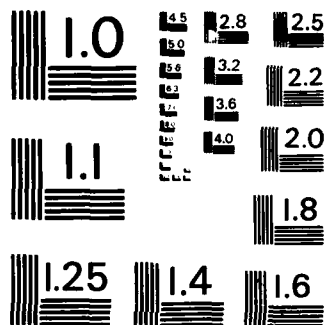
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IMPLEMENTATION OF THE COMMERCIAL
ACTIVITIES PROGRAM AT
NAVY PUBLIC WORKS CENTER PENSACOLA

By

James L. Bullock

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A REPORT PRESENTED TO THE GRADUATE
COMMITTEE OF THE DEPARTMENT OF
CIVIL ENGINEERING IN PARTIAL FULFILLMENT
OF THE REQUIREMENTS FOR THE DEGREE OF
MASTER OF ENGINEERING

UNIVERSITY OF FLORIDA

SPRING 1984

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DEDICATION

This report is dedicated to my wife and children. Over the past months of study, their love patience and support have given me strength and purpose.

ACKNOWLEDGEMENTS

The following is a list of the individuals to whom I owe my gratitude. Their knowledge and expertise helped me in my understanding of the subject matter and in publishing the final report.

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At Naval Material, Washington, D.C.: Commander Thomas McClure.

At the University of Florida, Gainesville, Florida:
Professor Willard Shafer, Academic Advisor; and Joanne Stevens, my typist - "bon voyage!"



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CHAPTER ONE INTRODUCTION

The Commercial Activities Program has had a long and controversial history since its inception in the mid 1950's. The basic premise is a simple one, that is, the Government of the United States should rely on commercial sources to supply its needs. This particular desire by the Government not to "compete" with its citizens has drawn its fair share of criticism from all sectors. Private enterprise has complained that the Government favors in-house performance of its functions, making it very difficult for a private contractor to competitively bid for commercial activities contracts. The Federal employees on the other hand have felt that the system unjustly favors the private contractor. The pendulum has swung in both directions over the past thirty years. If the concerns of small business, non-profit organizations and such are considered, then, the equation becomes even more complex.

The author's goal in this report is to examine the effect of the Commercial Activities Program on a particular field activity, namely, the Navy Public Works Center in Pensacola, Florida. In order to develop this goal, it is necessary to examine the history of the Commercial Activities Program in some detail. Areas of controversy are addressed with particular emphasis on recent revisions to the program. A background discussion of the Navy Public Works concept is then presented. The actual implementation of the Commercial Activities Program at the Navy

Public Works Center level is then addressed. Governing directives, problems encountered and the current status of the program at Navy Public Works Center Pensacola, Florida are then examined. Future studies, and their potential impact, are also discussed.

The Commercial Activities Program has had some very positive results with respect to productivity and efficiency. Cost savings obtained to date and future study projections by the office of the Assistant Commander for Public Works Centers at Naval Facilities Engineering Command headquarters, Washington, D.C. are discussed. Finally, the author's conclusions and recommendations are presented.

Information for this report was obtained primarily from library research and visits to Washington, D.C. and Pensacola, Florida. Personnel from Navy Public Works Center, Pensacola and Naval Facilities Engineering Command were interviewed during these visits and points of contact were established for subsequent correspondence.

CHAPTER TWO
HISTORY AND IMPLEMENTATION OF
THE COMMERCIAL ACTIVITIES PROGRAM

A. Birth of Program

As early as 1932, discussions took place concerning reliance by the Government on the private sector for required goods and services. These early discussions were part of a series of Congressional inquiries into the subject. The Executive Branch, however, established most of the actual policy.

1. Bureau of the Budget (BOB) Bulletin 55-4

President Eisenhower in his initial budget address stated that his budget would mark the beginning of a move to shift to the private sector those Federal activities which could be more efficiently handled that way. As a result of this stated policy, the BOB published BOB Bulletin 55-4 on January 15, 1955.¹

This bulletin stated:

"The Federal Government will not start or carry on any commercial activity to provide a product or service for its own use if such product or service can be procured from private enterprise through ordinary business channels."

Exceptions to the policy, by the head of an agency, were permitted,

"only where it is clearly demonstrated in each case that it is not in the public interest to procure such product or service from private enterprise."

Manufacturing activities received the major emphasis and two of the early conversions included the Navy's rope manufacturing and the Army's coffee grinding activities.²

2. BOB Bulletin 57-7

On February 5, 1957, BOB Bulletin 57-7 superseded BOB Bulletin 55-4. The same policy statement was included but the emphasis against cost comparison was softened somewhat. In-house provision of goods or services was justified when the goods or services were not available on a competitive basis or at a reasonable price. Additionally, the policy stated that in-house provision was justified if the goods or services should not be procured due to overriding considerations of law, national security or national policy.³

3. BOB Bulletin 60-2

On September 21, 1959, BOB Bulletin 60-2 further revised the original policy by adding more exceptions to the policy. Again the same policy statement was made but three major exceptions were listed defining when an activity could be performed in-house. These exceptions included national security, relatively large and disproportionately higher costs, and clear infeasibility. The term "relatively large and disproportionate cost" was not explained and the bulletin further stated that such a finding did not prohibit procurement from a more costly commercial source.⁴

B. Program Formalization

1. BOB Circular A-76

In the early 1960's, cost-benefit type analysis increased in popularity. In March 1966, BOB Bulletin 60-2 was superseded by BOB Circular A-76. The issuance of Circular A-76 followed a lengthy and quarrelsome process involving BOB, the General Accounting Office (GAO) and the Department of Defense (DOD). The policy statement was condensed stating simply that:

"The guidelines in this Circular are in furtherance of the Government's general policy for relying on the private enterprise system to supply its needs."

It also stated that in some instances

"It is in the national interest for the Government to provide directly the products and services that it uses."

Relative cost was stressed in the new policy and the cost criterion stated that Government activities should not be continued on the basis of relative cost unless the savings, compared to contract performance were sufficient to outweigh the disadvantages of Government commercial and industrial activities. New Government commercial activities, justified on a cost basis, were required to show a savings of at least 10 percent over commercial performance.⁵

2. Circular A-76 (Revised)

With increased emphasis on relative cost came the first major revision of Circular A-76 on August 30, 1967. This revision dealt primarily with cost comparisons and informed Government agencies that a cost comparison should be performed prior to conversion of a Government commercial activity to a private contract. Another change directed that incremental costing should be used in developing the Government cost estimate, rather than full allocation of overhead and indirect costs. The 10 percent differential was also softened by stating that when a new activity was under consideration, the differential was not a firm figure and could vary with individual cases.⁶ During the late 1960's while DOD was occupied with the Vietnam conflict, there was minimal program implementation. During the early 1970's, DOD and the Department of the Navy issued their respective instructions dealing with the "Commercial or Industrial Activities Program." During this same time frame, the Office of Management and Budget (OMB) replaced the BOB.

3. Department of Defense (DOD) Instruction 4100.33 of July 16, 1971

This instruction contained detailed implementation procedures and assignments of responsibility. Several extensions were made to the policy contained in OMB Circular A-76 (Revised). Two important extensions dealt with the definition of DOD Commercial or Industrial (C/I) Activities and with the establishment of a procurement review requirement. The DOD instruction in its definition of Commercial-Industrial Activities had excluded many "white collar" activities from consideration under the C/I Activities Program. The second major policy extension was the requirement for an economic review of existing and planned contract procurement of goods and services. Circular A-76 established a requirement to inventory in-house operation of C/I Activities. The DOD instruction extended the inventory requirements to include contract operations and established an additional inventory report.⁷

4. Secretary of the Navy (SECNAV) Instruction 4860.44A of October 27, 1971

The Department of the Navy published its "Commercial or Industrial Activities Program" instruction on October 27, 1971. This instruction dealt primarily with the assignment of responsibilities for implementation of the C/I Activities Program within the Department of the Navy. No policy extensions were made and no new reporting requirements were discussed. Responsibility assignments in the areas of approval levels and program audits were covered in the instruction. The Comptroller of the Navy was tasked with reviewing actions by Naval and Marine Corps installations in meeting review responsibilities and when requested, to audit new starts and conversions to contract. A second Navy instruction (Chief of Naval Operations [OPNAV] Instruction 4860.6) dated November 30, 1971

delegated responsibility for implementing the C/I Activities Program within the Navy to the Chief of Naval Material.⁸

5. Chief of Naval Material (NAVMAT) Instruction 4860.12A of January 25, 1972

The Chief of Naval Material issued its instruction on January 25, 1972. This was a rather lengthy document providing the detailed guidance for the implementation of the C/I Activities Program within the Navy. It was intended as a manual of operating procedures for use by persons at the field and major claimant levels. The overall effect of the instruction was that it tasked every shore activity commanding officer to fully implement the C/I Activities Program.⁹

6. Naval Facilities Engineering Command (NAVFAC) Instruction 4860.16 of November 28, 1972

The Naval Facilities Engineering Command (NAVFAC) published its C/I Activities Program instruction on November 28, 1972. This instruction applied only to NAVFAC field activities. These activities included Public Works Centers, Construction Battalion Centers, and Engineering Field Divisions. In this instruction, the Engineering Field Divisions were tasked with technical review of reports. Guidance for the preparation of the economic review was given with particular emphasis on the unique aspects of the Public Works Centers.¹⁰

C. Initial Program Emphasis

During the period of 1973 to 1976, the Department of Defense reported an increase in contract procurement from 23.9% to 26% of the total support in the functional areas reportable under the C/I Activities Program. Very little progress was being made and the figures indicate the lack of emphasis on the program.¹¹

1. Evolution of Base Operating Service (BOS) Contracts

Within the DOD, the Department of the Navy was trailing the Army and the Air Force in implementing the C/I Activities Program. One very significant event began to occur more frequently during the early to mid 1970's. In response to OMB Circular A-76 and because of reductions in civilian and military personnel, a number of Base Operating Service (BOS) contracts came into being, primarily in the Air Force. The Department of the Navy had dealt with manpower shortages and reductions in civilian personnel ceilings by awarding Maintenance Service Contracts on an individual function basis, never on a basewide concept.

One of the most successful BOS contracts was awarded to Northrop Worldwide Aircraft Services, Inc., a subsidiary of Northrop Corporation, by the U.S. Air Force in 1972. Northrop and the Air Force together run Vance Air Force Base. At Vance, all of the major base and aviation services are performed by a single commercial operator. Comparison of Vance with several other Air Force Bases of similar size and mission showed that costs were 20-30 percent less than the average of Bases run by military and civilian government personnel.¹² Other Air Force activities extensively contracted out include Vandenburg AFB, Patrick AFB, and the Air Defense Command in Denver. The establishment of the successful BOS concept, the lack of progress by the Navy and other Governmental departments in implementing OMB Circular A-76, and the apparent lack of support for the program by top management, all contributed to the events of 1976. During the summer of 1976, a number of Presidential initiatives began to take effect. These initiatives would revive the program and instill new heights of interest throughout the Federal Government.

D. Presidential Initiatives

On July 27, 1976, the Director of OMB, James T. Lynn, released a memorandum calling for the heads of 20 major federal agencies to submit initial plans for increasing their reliance on the private sector in accordance with OMB Circular A-76 (Revised). The agencies were to submit their plans by August 23, 1976. The source of this renewed interest was President Ford's Management Initiatives Meeting of July 23, 1976. The memorandum requested that each agency identify at least five in-house functions, with action timetables, for review by OMB. Each agency was also tasked to review and revise all implementing instructions and procedures to ensure compliance with OMB Circular A-76 (Revised) by September 21, 1976.¹³

1. Transmittal Memorandum No. 2 of October 18, 1976

Transmittal Memorandum No. 2 to OMB Circular A-76 (Revised) was first published in the Federal Register on August 23, 1976, and became effective on October 18, 1976. This revision followed the creation of the Office of Federal Procurement Policy (OFPP) in OMB. Responsibility for the Circular was subsequently passed to OFPP. This memorandum specified new factors to be used in calculating the cost of Government fringe benefits. Factors of 24.7% for civil service retirement cost and 4% for civil service insurance/compensation cost were directed for use when making analyses under the provisions of Circular A-76. The previous factors were 7% and 1.4% respectively. The higher factors were developed by Civil Service Commission actuaries on the basis of a "dynamic" versus "static" approach to reflect anticipated changes in salaries, interest rates and retirement benefits. The Transmittal

Memorandum further provided that when requested, copies of cost comparisons made under the provision of Circular A-76 were to be made available to interested parties under the provisions of the Freedom of Information Act.¹⁴

2. DOD Procedural Changes

As a result of the OMB memorandum on the Presidential Management Initiatives meeting, the Department of Defense developed several procedural changes intended to more effectively implement Circular A-76. These changes were agreed upon by the OFPP in August 1976. The more significant changes were:

- a. New factors were developed for use in all cost studies. In addition to the new retirement and insurance factors mentioned earlier, revised factors for taxes foregone, inflation projections, government wage increases and the cost of money were developed.
- b. A "firm offer" concept of securing government bids from industry was developed for use throughout DOD. Under this concept, the activity developed an in-house estimate, including factors necessary to make the estimate comparable to private industry. This estimate, after validation by an independent service agency, was then sealed and became the government estimate and the government bid in a subsequent solicitation of bids from private contractors. This concept placed the activity in direct competition with the private contractor. Guidance was also issued that encouraged contracting for a three year minimum period, to avoid the expense of advertising and bidding a C/I Activity each year.

- c. The maintenance of real property was added to the list of functional categories specified in the DOD instructions. It was further stated that the "DOD real property maintenance centralization effort of the past few years should provide ample opportunity for contracting out."
- d. The consolidation of functions to make a larger, more attractive contract solicitation was directed; an encouragement of the BOS concept. It was felt that contractor interest might be reduced if competition for small, potentially unprofitable activities was adequate.
- e. Individual service components of the DOD were encouraged to collect and analyze C/I inventory information quarterly. Inventory reports were still required annually at the DOD level.
- f. Functions subject to the C/I program no longer required a cost study prior to contracting out when adequate competition existed. This was the case unless there was substantial reason to believe that the government in-house cost was less costly, due to some unusual reason.¹⁵

3. Public Proclamation

The events of 1976 sparked the first of a series of public proclamations by the various factions affected by the C/I Activities Program. Up to this point, there had existed a long silence, although the controversy was still there. There seemed to be little point in publicly challenging a program that was receiving less than enthusiastic support within the Federal Government and that was looked on as being totally ineffective by those involved.

The American Federation of Government Employees (AFGE), an affiliate of the AFL-CIO, became a very vocal element in opposition to the renewed emphasis on the C/I Activities Program during this time frame. The AFGE estimated that 170,000 federal employees would lose their jobs if the increased factors were used in computing retirement and insurance when making cost comparisons. The AFGE stated that the new factors were meaningless unless similar factors were applied to compensate for the added unemployment compensation and social security costs which would result if the federal positions were contracted out. The AFL-CIO attacked the factors as being arbitrarily high. During this time frame, the AFGE began its consideration of legal action to halt the contracting out of functions currently performed in-house by civil service employees.¹⁶

The National Council of Technical Service Industries (NCTSI) appeared as the most vocal in support of the conversion of in-house functions to contract. The NCTSI welcomed the increased factors as appropriate and long overdue. The NCTSI also called for a similar disclosure under the Freedom of Information Act of rationale used when in-house performance is justified on the basis of a circumstance not involving a cost comparison.¹⁷

Congressional reaction to the renewed interest and proposed changes to the C/I Program was mixed. Several congressional members were in favor of proceeding slowly with the program, allowing Congress time to hold hearings and/or have the General Accounting Office study the matter more thoroughly. Others supported the change and threatened further legislation to ensure compliance with Circular A-76.¹⁸

E. Congressional Interest

1. Transmittal Memorandum No. 3 of June 13, 1977

Memorandum No. 3 dropped the standard cost factor for retirement to 14.1%, based on a different method of calculating the government's cost of retirement. The new Memorandum also called for a thorough review of the Circular and cost comparison guidelines.

2. Congressional Moratorium

While Federal employee groups celebrated their latest victory in reducing the retirement factor, private contractors were very dissatisfied. Increased political pressure led to an almost complete congressionally imposed moratorium on DOD contracting out in 1978. The moratorium was a direct result of the 1977 changes in the retirement factor and the continued difficulties in following the intent and procedures outlined in OMB Circular A-76.

One of the major areas targeted for clarification by Congress involved contracting out to overcome personnel limitations. While Circular A-76 clearly specified that agencies will not contract out solely to meet personnel ceilings, Congress did not feel that the actual distinction was clear enough.¹⁹ A congressional directive issued in 1978 called for a thorough study and report of contracting out policies and procedures.

F. Revised OMB Circular A-76

The review of OMB Circular A-76 called for by Transmittal Memorandum No. 3 resulted in a totally revised Circular. This new Circular, dated March 29, 1979 superseded all previous revisions to OMB Circular A-76.

1. Policy

The basic policy of the 1979 revision built upon three valid precepts; reliance on the private sector, retention of certain governmental functions in-house, and finally, economy via cost comparisons.²⁰

2. Government Commercial or Industrial Activity Defined

In this latest revision, a number of important areas were dealt with and discussed in detail. The Circular defines a Government commercial or industrial activity as:

"one which is operated and managed by a Federal executive agency and which provides a product or service that could be obtained from a private source."

An activity can be identified with an organization or a type of work but according to the Circular must be:

"separable from other functions so as to be suitable for performance either in-house or by contract and...a regularly needed activity of an operational nature, not a one-time activity of short duration associated with support of a particular project."

3. Governmental Functions

The Circular also specifically addressed "Governmental functions" and defined them as a function which must be performed in-house due to special relationships in executing governmental responsibilities. Three categories of governmental functions were discussed in the Circular: discretionary application of Government Authority (judicial function, national defense, foreign relations, intelligence operations, industry and commerce regulations, etc.); monetary transactions and entitlements (tax collection, treasury, money supply, administration of public trusts, etc.); and in-house core capabilities (research, development and testing). It is interesting to note that services beyond the core capability

established and justified by the agency were not considered governmental functions.²¹

4. Authorized Government Operation of C/I Activity

The overall flavor of the revised Circular was one of economy. Only three conditions were given for authorized Government operation of a commercial or industrial activity:

- a. No satisfactory commercial service available
- b. National Defense
- c. Higher cost

If a satisfactory commercial source was unavailable, the activity could be authorized for Government performance without a comparative cost analysis. The agency was required to make all reasonable efforts to identify available sources. Those efforts required at least three notices of the requirement in the Commerce Business Daily over a 90-day period. Agencies were encouraged to find satisfactory commercial sources in the small and minority owned businesses by obtaining assistance from the General Services Administration, Small Business Administration, and the Department of Commerce. A private commercial source which would cause an unacceptable delay or disruption of an essential agency program was also a reason for Government authorized performance. However, this avenue required extensive documentation in terms of cost, time and performance measures of the delay or disruption. Disruption must also be shown to be of a lasting or unacceptable nature. Possibilities of strikes, classified programs, and mission requirements were not adequate justification for in-house performance of that activity.²²

A Government commercial or industrial activity, operated by military personnel, was justified when the military personnel assigned were used in combat support roles, military skills training or in assignments pertaining to career progression or sea-shore rotations. Depot or intermediate level maintenance was justified when a ready and controlled source of technical competence and resources was needed by the Secretary of Defense to meet military contingencies. Support of mission-essential equipment was to be limited to the minimum necessary to accomplish that objective and justification required a detailed explanation on a case-by-case basis as to why the needed capability could not be supplied by either a private commercial source or by contract operation of Government-owned facilities (COGO).²³

Government C/I Activity performance was authorized if a comparative cost analysis, prepared in accordance with details in the Circular, indicated that the Government could provide or was providing a product or service at a lower total cost than if obtained from a private commercial source.²⁴

5. Common Ground Rules

The cost comparison portion of the revised Circular dealt with common ground rules for carrying out cost comparisons, the calculation of contract costs, and the calculation of the costs of government operation.

Under common ground rules, the Circular stated that both Government and commercial cost figures were to be based on the same scope of work and the same level of performance. This required a precise work statement with performance standards that could be monitored. The standard cost factors prescribed in the Cost Comparison Handbook were referenced for use in cost comparisons. Cost comparisons were to be aimed at full cost.

All significant government costs, including overhead and indirect costs, were to be considered for both direct Government performance and for contract administration. In order to guard against "buy ins", prepriced or renewal options were encouraged for work of a continuing nature. A "buy in" occurs when a contractor bids low to gain contract award with the intent to increase future earnings through change orders, etc. Cost comparisons for products or services under \$100,000 in annual operating costs were optional unless in-house performance was justified or if there was reason to believe that commercial prices were unreasonable. A rate of 10 percent per annum was prescribed as the opportunity cost of capital investments and of the net proceeds from the potential sale of capital assets.²⁵

6. Calculating Contract Costs

The contract cost figure was to be based on a binding firm bid or proposal, solicited in accordance with pertinent acquisition regulations. Bidders were to be notified that an in-house cost estimate was being developed and that a contract may or may not result, depending on the comparative cost of the alternatives. A factor of 4 percent of the contract price or expected cost was specified for use by the Government as the cost of administering the contract.²⁶

7. Calculating Costs of Government Operation

In calculating the costs of Government operation, each agency was to assure that Government operation was organized and staffed for the most efficient performance. This reference to the "most efficient" organization is a most important one and shaped the future policies and procedures of the program. These policies and procedures will be addressed later in this report.

Government cost factors were once again revised by the new Circular. A retirement factor of 20.4% was to be used, based on a dynamic normal cost projection for the Civil Service Retirement Fund. The insurance/compensation factor was changed to 5.6% and was based on actual cost. A savings of at least 10 percent of the estimated Government personnel costs was required before an existing in-house activity could be converted to contract performance. New contracts were required to save at least 10% of Government personnel costs, plus 25% of the cost of ownership of equipment and facilities, as compared to contract performance, prior to approval. All cost comparisons required a review by an activity independent of the cost analysis preparation to ensure conformance to the Cost Comparison Handbook.²⁷

8. Other Provisions

The Circular discusses two other very important requirements which have unto themselves been sources of a great deal of controversy. With regard to personnel ceilings, the document stated:

"This Circular will not be used to justify a conversion to contract solely to meet personnel ceilings or to avoid salary limitations."

When in-house performance of a "new start" was justified under the Circular but could not be accommodated within agency personnel ceilings, the agency was encouraged to appeal to OMB for an adjustment to increase personnel ceiling to implement the Circular agency-wide.

Each agency was to ensure that contracts awarded as a result of reviews under Circular A-76 included a "right of first refusal" provision. Stated simply, the contractor was required to give Federal employees, displaced as a result of conversion to contract performance, the right of

first refusal for openings in positions for which they were qualified.²⁸

The Circular also established an appeals procedure within each agency for an informal administrative review of determinations made. The procedure was designed to resolve questions of the determination between contract and in-house performance and did not apply to questions concerning award to one contractor in preference to another.²⁹

9. Continued Controversy/Problems

The revised Circular A-76 once again received mixed reviews. Federal employee groups felt that the new Circular was contract oriented. Contractor groups complained that the complicated cost comparison methods for determining government costs were invalid and unreliable.

Implementation of the new guidelines within the Navy and the Office of the Secretary of Defense (OSD) was slowed by administrative problems. It took nearly a year for OSD to prepare and publish new directives following the March 1979 transmittal of the revised Circular A-76. After the AFGE exercised its ninety-day review option, fiscal year 1980 was more than half over before DOD activities could begin conducting studies under the new cost comparison handbook procedures. The handbook's complexity, the limited expertise and lack of standardized audit procedures further slowed study efforts.³⁰

According to CDR George A. Roberts, Jr., USN, Deputy Comptroller, Chief of Naval Education and Training:

"the directed logic applied at nearly every decision point favors contracting...but...the restrictions and approval steps, intended to ensure national defense, protect government employees and satisfy other special interests, severely restrict conversions to contract."

In fact, the acquisition of service contracts within the rules of Circular A-76, congressional legislation and in-house administrative requirements, had not resulted in the anticipated solution to personnel shortages.³¹

The policies as set forth by the revised Circular appeared to be in conflict with one another. In addition, the program conflicted with other socio-economic programs such as equal employment opportunity, affirmative action and small and minority business incentive programs. The manpower required to perform cost comparisons and the detailed procedures were in direct contrast to the stated goal of reduction of paperwork and economy in government.³² However, due to outside political influences and reductions in civilian personnel ceilings, contracting had become a necessity to provide the needed services. The military retention problems during this time further deepened the requirement for a balancing of skills via contracting.

Private contractors expressed strong discontent with certain portions of the new circular. Most of the controversy centered around the cost comparison process. Burt Hall, one time member of the Commission on Government Procurement and in 1981 a Group Director with GAO attacked the cost comparison process as a way for policy makers to avoid taking a position on our private enterprise system; in other words, a convenient crutch. Hall cited a number of problems with cost comparisons as applied by Circular A-76.

Hall stated that cost comparisons were too narrow for decision-making since they did not consider such things as quality, reliability, and flexibility. He also pointed to their lack of reliability because

of the differences between the accounting systems of Government and business which would not enable true cost comparisons with private firms. This in turn would lead to a basic lack of understanding about the specific work to be done and the required standards of performance. A lack of incentives to take risks, cut costs and innovate on the part of the Government were discussed by Hall as further limitations of the cost comparison process.³³

Other cost comparison shortcomings specifically addressed by Hall include: a lack of government accountability for customer satisfaction or financial loss, a lack of consideration for long-term occurrences, the shrinking of the tax base and shifting of the tax load coincident with in-house performance, a contribution to the longstanding Government/industry adversarial relationship and a strain on the Government's credibility. Finally, he also points to the serious drain on limited agency resources while applying the detailed 90 page cost handbook. The basic problem, as addressed by Hall, was that Federal in-house business activities did not perform as private firms in the open market place in terms of cost, responsiveness, and product improvement. He maintained that the fatal misstep by the OMB Office of Federal Procurement Policy was in the attempt to balance A-76 politically, by attempting to please both private industry and Federal Employee Unions.³⁴

Another problem discussed by Edward J. Shockley, President, Lockheed Aircraft Service Co., dealt with the apparent lack of progress in contracting out aircraft depot level services, including periodic and scheduled depot maintenance, and aircraft modification. Shockley warned that the opportunity to lower government spending and increase the industrial

preparedness of the country was being missed by not contracting out depot level aircraft services. Shockley's call for increased contracting out of depot level services came at a time of eroding industrial preparedness due to diminishing workload on the part of the aerospace industry. He further lamented that none of his company's new business was a result of A-76.³⁵

The years following the March 1979 revision to Circular A-76 saw a concerted effort within DOD to schedule and complete those cost studies identified within each agency. Formal training programs were developed as the C/I Activities Program became a viable way to meet increased responsibilities with fewer and fewer civil service employees. The "most efficient organization" (MEO) concept may well have been one of the most important and worthwhile aspects of the program. The other armed services had realized true efficiencies from the application of the MEO concept. In the Navy, there was insufficient data on which to base any statistics concerning similar improvements in management.³⁶ It was, however, to become even more important as the C/I Activities Program continued through the early 1980's.

According to William D. Russell, former Deputy Assistant at OFPP and currently Vice-President of Government Relations at RCA's Service Company Division, industry still felt that it could win most cost comparisons under the rules of the 1979 Circular and Cost Comparison Handbook. He stated that initially most cost studies (65%) resulted in contract award. Russell noted that the percentage soon dropped to 60% and then to 50% and blamed this drop on "devious schemes" by activities to discourage contractors from bidding and to inflate submitted bids. He describes Circular A-76 as the "ultimate exercise in futility."³⁷

G. Congressional Restrictions

In order to deal with some of the more controversial areas of Circular A-76, Congress began to play a more important role in the implementation of Circular A-76 during the early 1980's. Specifically with the Department of Defense, Congress took action via the Department of Defense Authorization Acts of 1980 and 1981.

In the 1979 Defense Authorization Act, Congress required that an announcement of proposed conversion studies be made before studies could commence. The "announcement" constituted notification to Congress, employees, commercial vendors and labor unions, that a conversion to contract was under consideration. It identified the C/I Activity by function, location and number of in-house personnel involved.³⁸

1. Defense Authorization Act of 1980

The 1980 Defense Authorization Act (Section 805) specifically prohibited the use of contracting to circumvent any civilian personnel ceiling. It also required various notification and reports, the most important of which was certification that the government in-house calculation was based on the "most efficient and cost effective in-house organization." In 1980, Congress established the requirements of Section 806 as permanent law. These requirements were made a part of Section 502 of Public Law 96-342, the Department of Defense Authorization Act for 1981.³⁹ Section 802 of the 1980 Act also exempted Research, Development, Test and Evaluation from the provisions of Circular A-76.

2. Defense Authorization Act of 1981

In addition to policy on personnel ceilings and the most efficient organization, the 1981 Defense Authorization Act contained additional

reporting requirements. Prior to contract award the following reports must be made to Congress by the Secretary of Defense:

- a. The potential economic impact on affected employees.
- b. If 50 or more employees are affected, report on the potential impact on the community.
- c. The affect on the military mission.
- d. The result of the cost study required by Circular A-76.

In 1982, Congress took further action with regard to Circular A-76. Section 502 of the fiscal year 1981 Defense Authorization Act was modified to allow contracting out of purely military functions. Functions containing ten civilian personnel or less were also exempted from congressional notification. During this time frame of the early 1980's, the program became known as the Commercial Activities or CA Program within the Department of Defense.

3. Congressional Moratoriums

A much more controversial action by Congress in 1982 added additional fuel to the heated debate between Government and Industry. In 1982, Congress imposed a 6 month moratorium on all DOD CA studies (from October 1, 1982 to March 31, 1983). A one year moratorium was placed on contracting out firefighting and guard functions. The General Services Administration was also prohibited from contracting for guard or custodial services throughout fiscal year 1983. Specific reasons for the moratoriums were not addressed. One possible answer involved a request by Congress for the specific costs of conducting the on-going studies. Industry's view was simply that Congress, under pressure from Federal employee and other special interest groups began to include exemptions from contracting out in authorizations and appropriation bills.⁴⁰

James Montgomery, Chief Executive Officer of Pan Am World Services, Inc., described the congressional moratorium as a "dangerous and unnecessary precedent." He further indicated that the six month moratorium on all DOD CA studies would delay programs to contract out for at least two to three additional years. Montgomery argued that few companies, especially small businesses, could cover the cost of maintaining a professionally competent work force for such a length of time with no opportunity to compete for Government service work.⁴¹

H. Second A-76 Revision

On January 12, 1983, OMB published a draft revision to OMB Circular A-76 for a 180-day public, agency and congressional comment period. Over 900 copies of the Supplement were mailed to interested parties. Written comments were received from numerous individuals and organizations, including Federal agencies, business firms, industry associations, professional groups and private citizens. Public hearings were held on March 3, 1983 and testimony was received from a number of individuals and organizations. On August 4, 1983, OMB issued the final Circular and Supplement. This new Circular, once again, superseded all previous revisions to OMB Circular A-76.⁴²

The changes in this new Circular will be discussed in a format similar to that used in discussing the 1979 revision. Changes in policy, definitions and scope will be addressed and major additions and deletions to the cost comparison process will be identified.

1. Policy

The general policy statement in the new revision to Circular A-76 continues to be one of reliance on commercial sources to supply the

products and services the Government needs. Three major areas are included in this policy statement. The first area deals with the achievement of economy and enhancement of productivity. It is stated that competition enhances quality, economy and productivity and that cost comparisons shall be performed in order to determine who will do the work. The second area covers the retention of certain Governmental functions in-house. These functions are not in competition with the private sector and therefore shall be performed by Government employees. Finally, a policy of reliance on the commercial sector is set forth with the statement that the Government:

"shall not start or carry on any activity to provide a commercial product or service if the product or service can be procured more economically from a commercial source."⁴³

It is interesting to note the subtle changes in this policy area. For instance, productivity, a very popular management subject, is discussed in the first paragraph of OMB's new policy statement. Other differences include the substitution of commercial for the word private throughout the policy section of the Circular.

2. Commercial Activity Defined

The new Circular's definition of a commercial activity differs somewhat from the previous definition. The new definition states very explicitly that a "commercial activity is not a Governmental function." The definition continues to address the type of work that is separable from other functions or activities and is suitable for performance by contract. The statement contained in the previous Circular which dealt with a one-time activity of short duration has been deleted in the revised Circular.⁴⁴ A representative listing of commercial activities is provided in Appendix A.

3. Governmental Functions

The categories of Governmental functions have been decreased to two in the revised Circular. These categories include: the act of governing (i.e., the discretionary exercise of Government authority), and monetary transactions and entitlements. In-house core capabilities such as research and development have been deleted from the definition of Governmental functions.

4. Scope

A review of the scope of the new Circular indicates that the Circular no longer applies to the conduct of research and development. However, in-house commercial activities in support of research and development, such as those listed in Appendix A are normally subject to the Circular and its Supplement. Other areas specifically addressed in the scope of the new Circular include statements that the Circular does not provide authority to enter into contracts and that the new Circular shall not be used to justify conversion to contract solely to avoid personnel ceilings or salary limitations.⁴⁵

5. Government Performance of a Commercial Activity

The new Circular lists four conditions for Government performance of a commercial activity:

- a. No satisfactory commercial source available.
- b. National Defense
- c. Patient care
- d. Lower cost.

In this section of the new Circular there is no reference to specific efforts to obtain commercial sources from the small and minority-owned

businesses via the General Services Administration, Small Business Administration and Department of Commerce. The remainder of the efforts required to obtain commercial sources are essentially the same as in the previous Circular. There is an additional provision that efforts to obtain commercial sources must be documented and made available to the public upon request. A statement is also included that specifications and requirements in the solicitation shall not be unduly restrictive and shall not exceed those required of in-house Governmental personnel or operations.⁴⁶

The new Circular gives the Secretary of Defense full authority for establishing criteria for determining when Government performance of a commercial activity is required for national defense reasons. All of the detail contained in the previous Circular under this topic has been deleted. The Secretary of Defense is also given the authority to exempt commercial activities for national defense reasons.⁴⁷

A new area dealing with patient care has been added to this portion of the new Circular. If an agency head, after consultation with the chief medical director, determines that in-house performance of a commercial activity would be in the best interests of direct patient care, then the activity will be retained in-house. This applies only to commercial activities performed at hospitals operated by the Government.⁴⁸

A change in title from higher cost to lower cost for this section constitutes the only major modification. Cost comparisons are still to be made in accordance with the new Circular and Supplement and must demonstrate that the Government is operating or can operate the activity on an on-going basis at an estimated lower cost than a qualified commercial source.

6. Supplement to Circular A-76

The August 1983 version of Circular A-76 contains a Supplement as an integral portion of the Circular. Compliance with all parts of the Supplement is mandatory. The Supplement is divided into four parts. Policy Implementation is outlined in Part One. Included in this part are detailed flow charts and narrative descriptions, inventory and review requirements, and annual reporting requirements. Part Two of the Supplement sets forth the steps needed to develop, write and administer a performance work statement and a quality assurance plan for both in-house or contractor operation of a commercial activity. The management study guide comprises Part Three of the Supplement in which the recommended procedures for conducting the management review of the in-house organization are set forth. Part Four, the Cost Comparison Handbook, provides the detailed instructions for developing a comprehensive and valid comparison of the estimated cost to the Government of acquiring a product or service by contract and of providing it with in-house personnel and resources. Part One of the Supplement will be the main topic for the remainder of this Section.

The policy implementation portion of the Supplement details the step-by-step instructions for implementing the Circular. Flow charts and flow chart narratives explain each step in the process for existing commercial activities and expansions, existing contracts and new requirements. These flow charts and flow chart narratives are included in Appendix B.

The new Circular and Supplement utilize the Full-Time Equivalent (FTE) work year in determining operating levels for inventory purposes.

An FTE work year is the "planned use of 2,080 (2,087 after fiscal year 1984) straight time paid hours in a fiscal year (to include authorized leave and paid time off for training)." In the case of full time employees with permanent appointments "one FTE" is normally comparable to "one employee."⁴⁹

In compiling the required inventory lists, each agency is required to evaluate all agency activities and functions to determine which are Governmental functions and which are commercial activities. Each agency must then complete an inventory of all Government commercial activities, including known expansions and new requirements which it operates. Activities of ten FTE's or less must be listed separately from those of more than ten FTE's. The activity inventory must describe, as a minimum, the number of FTE's, the nature and location, the date of the next and last review, and the reason for continued in-house performance. Each CA inventory must be updated annually and will be made available to other agencies and the public upon request.⁵⁰

Reviews are required for existing in-house commercial activities, expansions, existing contracts and new requirements. With respect to existing in-house commercial activities, the review should first include a determination of whether the activity must be retained in-house for reasons other than lower cost. If not applicable, then the agency must justify in-house performance on the basis of lower cost. Agencies must publish their schedules for conducting cost comparisons at least 30 days in advance in the Commerce Business Daily and the Federal Register. Activities approved for continuation in-house will be reviewed again at least once every five years. Guidance is given encouraging packaging

of commercial activities to maximize efficiency and economy and to comply with the provisions of the Small Business Act Amendments. It is recommended that solicitations be written to take advantage of the competitive structure of the local business community.⁵¹

An expansion is defined as:

"The modernization, replacement, upgrading or enlargement of a Government commercial activity involving a cost increase exceeding either 30 percent of the total capital investment or 30 percent of the annual personnel and material costs."

A consolidation of two or more activities is an expansion if the proposed total capital investment or annual personnel and material cost of the consolidation exceeds the total of the individual activities by 30 percent or more. Where expansion is anticipated the entire activity, including the proposed expansion will be reviewed in the same manner as for existing in-house commercial activities.⁵²

Continual monitoring of existing contracts is strongly encouraged to ensure satisfactory, cost effective performance. In the event of unsatisfactory performance or unreasonable contract costs, a cost comparison will be conducted if re-competition with other satisfactory commercial sources does not result in reasonable prices or if in-house performance is feasible. Existing commercial contracts for which in-house performance has been justified will be allowed to expire once in-house capability is established. If the required FTE's cannot be obtained within the agency's personnel ceiling, a request to OMB for adjustment is authorized.⁵³

New requirements are newly established needs for a commercial product or service and should normally be performed by contract. If there is

reason to believe that commercial prices may be unreasonable, an informal preliminary review is authorized to determine if the work can be performed in-house. The cost of in-house performance must be less than the contract performance by 10 percent of the Government personnel-related costs, plus 25 percent of the acquisition cost of any needed capital assets not currently owned by the Government. If in-house performance is likely, a cost comparison is required. When in-house performance is not feasible or when contract performance would be under a preferential procurement program (i.e., Federal Prison Industries [FPI], Small Business Act (Section 8[a])) a contract may be awarded without conducting a cost comparison.⁵⁴

7. Common Ground Rules

Some of the common ground rules set forth in the new Circular differ from those in the previous revision. The ten FTE threshold replaces the \$100,000 threshold outlined in the previous Chapter. Activities exceeding ten FTE's are required to conduct cost comparisons to determine the method of performance. Cost comparisons can be waived by the Assistant Secretary of the agency and the activity converted to contract. The waiver must include a written determination that effective price competition is available and the reasons why the in-house operation has no reasonable expectation of winning the competition.⁵⁵

With regard to performance work statements, the new Circular again emphasizes that both Government and commercial cost estimates must be based on the same scope of work and standard of performance. Both the performance work statements and the new quality assurance plans are to be prepared in accordance with the Supplement. Again, the standard cost factors prescribed in the "Cost Comparison Handbook" portion of the

Supplement are to be used in cost comparisons. Cost comparisons will include all significant costs of both Government and contract performance. Costs common to both in-house and contract operation need not be computed but the basis of those costs must be identified and included in the cost comparison documentation.⁵⁶ The new Circular does away with the requirement for cost comparisons aimed at full cost (including allocation of overhead and indirect costs) and returns to the incremental estimate of Government indirect costs. The effort to achieve allocation of some indirect costs in the Government estimate, primarily at the installation level, was unsuccessful and has been deleted in the new Circular. The incremental estimates include those overhead costs that will go away if the activity is converted to contract.⁵⁷

The new Circular once again emphasizes that the in-house cost estimate will be based on the most efficient and cost effective in-house operation needed to accomplish the requirements of the performance work statement. Management studies and soliciting input from the employees, are required to analyze the current method of operation and make the necessary changes to achieve the most efficient organization. If the cost comparison results in a decision to perform the work in-house, the in-house staffing plan must be initiated within one month and completed within six months.⁵⁸

8. Contract Costs

Contract costs outlined in the new Circular are to be based on firm bids or proposals competitively obtained. Bidders or offerors must be informed that an in-house cost estimate is being developed and that a contract may or may not result. To guard against "buy-in" pricing, bids or proposals from contractors will be on at least a three-year multi-year

basis or include prepriced renewal options to cover two fiscal years after the initial period. Other advantages of this arrangement include continuity of operations, possibility of lower contract prices and reduced disruption. The new Circular still requires that all contracts awarded as a result of a conversion must include a right of first refusal for employment openings under the new contract. The new Circular added a requirement for the contractor to develop a strike contingency plan in contracts for critical or sensitive services. This plan must outline how the contractor intends to provide contract services during a labor dispute. Standby costs are also discussed in the new Circular. Standby costs are not to be charged to the cost of contracting when an agency elects to hold Government equipment and facilities on standby solely to maintain performance capability.⁵⁹

9. Cost Factors

The capital investment rate of 10 percent referenced in the previous Circular is now discussed in the Cost Comparison Handbook portion of the new Supplement. The cost of contract administration is no longer taken as a percentage of the contract price or expected cost as indicated in the previous Circular. Contract administration costs are now based on the size of the function under study as determined by the in-house staffing estimate developed in the management study. Staffing requirements are indicated in FTE's and a table is provided in the Cost Comparison Handbook portion of the Supplement. For example, for a study of 15 staff years (FTE's), one contract administration staff year (FTE) is required. A savings of at least 10 percent of the in-house personnel-related cost for the performance period is still required before an existing in-house activity can be converted to contract performance.⁶⁰

Government fringe benefits remain essentially the same with Federal employee retirement benefits at 20.4%. Federal employee insurance and workmen's compensation also remain at 5.6%. For those employees covered under the Federal Insurance Contribution Act (FICA) an additional 1.3% is added for Medicare.⁶¹

10. Review/Appeal Procedure

The new Circular requires that all cost comparisons be reviewed by a qualified person from an impartial activity independent of the commercial activity being studied and the activity preparing the cost comparison. This independent review should substantiate the currency, reasonableness, accuracy and completeness of the cost comparison. The appeal procedures set forth in the previous Circular remain essentially the same in the new Circular. The new Circular adds an additional category under which the appeal procedure does not apply. This category involves Government management decisions, such as the determination of the most efficient organization or whether an activity is a commercial activity or a Governmental function.⁶²

11. Inclusion of Non-Profit Organizations

A final addition to the new Circular involves the inclusion of non-profit organizations in the definition of a commercial source. The Cost Comparison Handbook outlines the procedures to be followed if the apparent low bidder or offeror is a tax-exempt organization. Should this occur, the contract price must be adjusted by an amount equal to the Federal, state and local income taxes that would be paid by the lowest non-tax exempt bidder or offeror. This adjustment is necessary to determine which bidder or offeror has the lower overall cost to the Government.⁶³

I. Current Controversy

The latest revision to OMB Circular A-76 has once again caused a stir on the sides of both Government and industry. The August 1983 version of the Circular had been delayed for over a year when the draft of the proposed changes leaked in April 1982, causing protests by Federal employee groups. The April version called for automatic contracting of all functions employing 25 FTE's or less. In addition, all new commercial activities would have been contracted for automatically.⁶⁴ Federal employee groups are still not satisfied and generally oppose the changes saying that they will cause costly and inefficient contracts to be granted.

1. Federal Employee Concerns

Federal employee groups have questioned the wisdom of changing the cut-off of cost comparisons from a cost of \$100,000 a year to ten FTE's or employees. Their feeling is that the new policy could allow functions worth millions of dollars in equipment and manpower to be given to the private sector without a cost study. Another concern of federal employee groups is in the area of jobs that are "inherently governmental." They have requested that OMB issue more stringent guidance in this area and have criticized contracts given for maintenance, payroll and legal support which they say should be performed by federal employees.⁶⁵

Sandy Arnold, a spokeswoman for the National Federation of Federal Employees describes the criteria for waiving cost comparisons in the larger functions as "pretty flimsy." There is concern that with the pressure from the administration to contract out, there will be temptations to waive the cost comparisons on any grounds.⁶⁶ Robert Stone, Deputy Assistant Secretary of Defense for Installation, recently stated that the Pentagon

had induced "artificial pressures" to contract out by subtracting jobs from its personnel proposals in anticipation of contracting. Under orders from Congress, the Pentagon recently ceased this practice. Stone added that the administration's attempt to study all commercial jobs for possible contracting within five years has also resulted in undue pressure to contract out. Federal employees also opposed this initiative and the administration has since backed down.⁶⁷

The January 1983 version of the new Circular encouraged consolidation of functions for possible takeover by one contractor. Due to objections from small businesses, that policy has been softened. Within the Pentagon, defense managers are reluctant to subdivide their functions. Concern exists that control will be lost by having to supervise many small contracts. As a result, fewer functions are put up for bid. There has been much debate, pro and con, on this subject. The Pentagon is continuing its efforts on a new order to allow "umbrella" contracts and still encourage small businesses.⁶⁸

2. Legitimate Competition

There has recently been some concern regarding the trend toward organizing performance work statements to include certain activities and then to offer it in competition against businesses which do not now exist to perform these activities. This brings up a very important question as to the legitimacy of the competition in the CA process. A whole new group of businesses may be created to compete in the CA process. Whether this is a desirable situation is certainly a valid question. Existing businesses are simply not organized in this manner and it would be difficult to determine the nature of the product which is bought in this type of process. It would appear to make more sense to compare federal and industry employees on a more

easily quantifiable basis, i.e., plumber against plumber, mechanic against mechanic. This may involve more contracts and more management attention to monitor them if the activity actually went to contract, but the management expense would be worthwhile as a means to ensure legitimate competition. The general feeling is that industry competes best with the Government in the lower skilled crafts. However, Government has the advantage at the journeymen and higher skilled levels. Most skilled government employees would rather compete at their level of expertise rather than against an unknown cost estimator. The question of consolidation of functions continues to be a major area of controversy.

3. DOD Status

The Department of Defense with the majority of the government's 400,000 contractable jobs, plans cost comparisons for all functions *considered for contracting* regardless of the allowances in OMB's policy. The House Armed Services Committee has requested that DOD compile and make available to Congress actual performance figures of all jobs that are contracted out.⁶⁹ In its fiscal year 1984 Defense Authorization Bill, Congress has requested a wide range of "special reports" from DOD to determine if contracting out for basic services is paying off. One such report with a deadline of April 15th deals with DOD's conversion to and use of commercial civilian contractors to perform jobs previously handled by DOD civilian or defense workmen. Among the items requested by Congress for audit are the following:

- a. Estimated performance cost for use of civilian non-military labor.
- b. Contractor's estimate of contract cost at time of bid.

- c. Actual cost to fulfill the contract.
- d. Savings achieved since contracts were let.
- e. Average savings of all services provided by non-military/
non-DOD civilians since January 1, 1981.
- f. Dollar amounts of contract-awards to small businesses
- g. Number of Federal employees who lost their jobs.⁷⁰

In the Department of the Navy, the civilian workforce is expanding. This is understandable since the DOD budget is growing and the size of the Navy's fleet is increasing. H. Lee Dixon, Director of the Civilian Manpower Division in the Navy Comptroller Office, points out that increases in the civilian workforce have been primarily in shipyards, ordnance activities and in the Military Sealift Command. These areas are directly related to readiness. Fiscal year 1984 plans show much the same pattern, as the Navy has requested an additional 3500 civilian employees to bring its staff up to an estimated 334,278. This increase is targeted at supporting the expanding military efforts. The new civilian employees requested for fiscal year 1984 will be utilized to improve inventory management at supply centers, to man Military Sealift Command fleet support ships, and to improve Navy readiness. Other new jobs are located in medical and training, ordnance maintenance and Marine Corps support.⁷¹

4. Private Industry Concerns

William Russell, Vice President of Government Relations at RCA's Service Company Division, points out that private industry has seen some encouraging signs in the latest revision to Circular A-76. He states that some of the more obvious "loopholes" permitting abuses of the cost comparison process have been eliminated. The complex procedures have

been simplified, according to Russell, and efforts to manipulate the process to "protect" Government activities will be more obvious. This should result in more equitable cost comparisons and more rational decisions.⁷²

In a separate article, Russell attacks the extensive changes in the Circular and its procedures in 1979 and 1983 as serving primarily to "restrict" the authority of agencies to convert Government commercial activities to private sector contract performance. He then outlines the various steps required before an agency can convert a Government activity to contract performance (See Appendix B). Russell defends OMB's attempt to establish a sound basis for decisions and to institutionalize the process by which agencies identify and consider commercial activities for contract performance, rather than to make it more difficult to contract out.⁷³ Russell recommends that the procedure be insulated from political pressure - a most difficult task.

Private industry realizes that some of the handicaps imposed on the private sector in competing with the Government are inherent in the system. William Russell points out that the rigors of the procurement process and contractual requirements place costs and risks on the contractor that cannot be placed on a Government activity. His contention is that industry can assess these costs and that they can be offset by the efficiencies in a competitive organization. Russell discusses a number of other inequities in the new Circular which Industry will continue to seek to eliminate.⁷⁴

Indirect costs, Russell argues, must be identified and allocated by contractors under many Government regulations. He objects to the current

method of incremental estimating of Government indirect costs as being in favor of in-house performance. Civil Service retirement costs and insurance costs are described by Russell as being "grossly understated." He estimates that retirement costs are actually from 35% to 50% of payroll costs versus the 20.4% stipulated in the A-76 Supplement. Insurance cost factors used by the Government are judged as being based on incomplete data by Russell. He also attacks the allocation of one-time conversion costs over a three year period versus the old five year period as favoring in-house performance when the cost study is conducted for a period of less than five years. Government labor cost computation is identified by Russell as another area of inequity. The previous handbook required that labor costs be computed on the basis of actual salaries of assigned personnel. The new Supplement calls for the use of Government-wide average steps for each pay grade or the average step for the organization. Finally Russell questions the rationale authorizing Government performance of commercial activities performed at Government hospitals. He states that the exception denies industry an opportunity to compete for this business and denies the taxpayer the potential savings from competition.⁷⁵

The American Consulting Engineers Council approves of the recent attempts to make the Circular's application work a little smoother but suggests that a closer look is needed at some of the hidden costs of in-house contracting. According to the ACEC, those costs include reduced tax revenues, license fees and business development. The council also warns against clauses exempting contracting out as a means for an agency to shield itself from commercial competition.⁷⁶

5. Legal Perspective

Karen Hastie Williams, counsel for Crowell and Moring Company, presents some interesting observations on Circular A-76 from a lawyer's viewpoint. Her initial comments express concern that the August 1983 revisions may slow contracting-out in the short term. Williams notes that the major changes in the final revision appear to reflect the comments of government employees and their unions rather than those of private industry. She further observes that the pendulum has swung back toward support for in-house performance. Finally, she argues that political perceptions played a critical role in driving the final version of the Circular. She blames a "disgracefully low level of substantive knowledge and lack of understanding" among Congressional lawmakers with respect to the key advantages and due process protections which are provided in the contracting-out process.⁷⁷

Williams identifies several key areas in the latest revision to Circular A-76 which contain changes that will impact the administrative and judicial view of contracting-out decisions.

The first key area addressed by Williams deals with the inclusion of non-profit organizations in the definition of a commercial source. She argues that the equalization of the tax factor serves the purpose of putting non-profit and profit-making organizations on an equitable cost footing, but it also adds another complex element to the preparation of the cost comparison form. From a legal perspective, Williams feels that there is a serious prospect for challenges to the tax calculation.⁷⁸

Over the last several years the implementation of the "right of first refusal" has been a source of controversy and detailed instructions

were requested from agency and private sector commentators. OMB has requested that the Office of Personnel Management (OPM) develop policies, regulations and guidelines for the implementation of this policy by the government and by contractors. According to Williams, delays in providing this guidance may become a source of tension and may frustrate the smooth implementation of the revised Circular.⁷⁹

With regard to cost comparison elements, Williams observes that under the August 1983 procedures, the agencies will be able to complete their cost comparisons in half the time it originally took. She notes that the agency reporting requirements have also been substantially reduced. The final version of the Circular notes that the government retirement factor of 20.4% and the material overhead rates are both out of date. Again OPM has been tasked with revising the retirement factor and that revisions are forthcoming from the General Services Administration (GSA) and the Defense Logistics Agency (DLA) on material overhead rates. Williams warns that interim operation with out-of-date factors will result in confusion and may lead to problems and challenges to in-house estimates based on the existing cost factors.⁸⁰

The final version of the Circular extended the deadline for completion of reviews by three years until September 30, 1987. The January version would have required completion by September 30, 1984. Williams points out that the extension of the deadline is likely to lead to "further procrastination" in agency implementation of A-76 and put OMB in the same posture several years from now.⁸¹

The January 1983 version of the Circular contained language encouraging consolidated contracts as a means of saving the government

money. It also provided detailed guidance for utilizing small businesses as subcontractors. In the wake of heated protest from the small business community, the August 1983 version has been considerably toned down with regard to "umbrella contracts." Williams observes that in the long-run, small business has not gained any headway by this revision other than a cosmetic change in the language. Agencies that wish to pursue consolidated contracts will continue to do so. According to Williams, it would appear that small business has lost some edge with respect to putting more teeth in the Small Business Act (Public Law 95-507).⁸²

6. Legal Challenges

Williams discusses the impact of the latest procedural changes on legal challenges to A-76 decisions. By way of background, it is important to note that to date the various forums available for challenging A-76 decisions generally have resisted review of agency decisions on whether or not to contract out.

The General Accounting Office (GAO) has held that A-76 was a matter of executive policy and did not establish legal rights. In the late 1970's, GAO became concerned with erroneous cost comparisons used by agencies in determining whether or not to contract out. GAO decided to review A-76 decisions where this was alleged to have occurred. If it was found that the erroneous cost data materially affected the decision on whether to contract out, GAO would reverse that decision (Crown Laundry. B-194505, July 18, 1979). Since Crown Laundry, GAO has broadened its jurisdiction to review A-76 decisions to the following:

- a. bidders must have exhausted their administrative appeals before coming to GAO.

- b. bidders must have raised those specific issues previously in the administrative proceeding before the agency.

Additionally, a protestor could not go to GAO under the previous version of the Circular to force an agency to conduct a cost comparison. With the August 1983 version of the Circular, GAO may also find itself faced with issues involving the decision to go to contract without a cost comparison.⁸³

As a general policy, GAO has declined to hear issues raised by federal employees, their unions or taxpayers. Generally it has only reviewed protests filed by bidders. Under GAO procedures, a union is not an interested party and a union protest does not fall within the zone limiting GAO review. As a result of rulings in certain district courts, unions may be afforded greater relief in the future. According to Williams, unions are considered interested, affected parties for the purpose of appealing cost comparisons within the agency.⁸⁴

Williams points out that the protestor carries the burden of proof in challenging any A-76 determination. The bidder's burden is two-fold under GAO standards:

- a. it must be demonstrated that the agency failed to follow the required A-76 procedures.
- b. that the failure materially affected the outcome of the cost comparison.⁸⁵

In the fall of 1982, the Claims Court refused to hear a suit brought by federal employees to enjoin a Navy decision to contract out under Circular A-76 Indian Wells Valley Metal Trade Council, v. U.S. (Cl.Ct. 1982). The Court held that its jurisdiction over A-76 decisions was

limited to only hearing suits brought by bidders. Since the labor organization was not a disappointed bidder, the Court concluded it had no jurisdiction to hear its complaint. With respect to jurisdiction of the Claims Court, Williams points out that the implication in Indian Wells was that had it been a bidder challenging the government's decision, the Court would have had jurisdiction. The Court later made clear that a bidder's suit would have to be brought before an award.⁸⁶

The Circuit and district courts have generally followed the lead of GAO and rejected attempts by unions to protest A-76 cost comparison studies.

In the International Association of Firefighters, Local F-100 v. Department of the Navy, 536 Fed. Sup. 125A (D.C.R.I. 1982), however, the U.S. District Court permitted a suit by Civil Service employees to enjoin the Navy from contracting-out following a cost comparison study. The Court's rationale is that the in-house cost estimate was in effect an unsuccessful bid to perform the services. Because the employees would suffer economically should the government decide to contract out, the employees were in the zone sought to be protected by the Defense Acquisition Regulations (DAR). Thus, the court found that as a "dissappointed bidder" the union had standing to challenge the A-76 decision. According to Williams, the Rhode Island case is fairly anomalous. On the whole, disappointed contractors have been somewhat more successful than government employees in attempting to obtain federal court review of the A-76 decision.⁸⁷

Williams discusses the existence of anti-contracting out sentiments in Congress and points to the number of legislative initiatives on the

subject over the last two years. According to Williams, legislation such as The Defense Authorization Act and Veterans Compensation Act effectively prohibit certain agencies from contracting out for certain specified job functions. Congress has primarily been concerned with job security for federal workers, the quality of services rendered by contractors and military preparedness. Williams points to recent legislation introduced by Senator Rudman in support of contracting-out but feels it has little chance of passing without a major education effort on the advantages of contracting-out within Congress. She feels that the contracting community must dispel myths with respect to A-76 as they relate to the efficient and effective performance of agency programs.⁸⁸

CHAPTER THREE NAVY PUBLIC WORKS CENTER BACKGROUND

A. Introduction

In order to discuss the Commercial Activities Program and its effect on a particular Navy Public Works Center, it is necessary to provide a brief overview of the Navy Public Works Center (NPWC) concept. This overview will include the standard NPWC chain of command and standard organization as well as an introduction to the Navy Industrial Fund (NIF) concept. Navy Public Works Center Pensacola will be addressed specifically regarding mission requirements, major customers, organization and services provided.

A Public Works Center (PWC) is a major independent naval command and service organization that provides a wide range of services to fleet and shore units. These public works services include utilities, housing, maintenance, transportation, engineering support, facilities planning support and other public works required by operating forces located in the vicinity of the naval complex served by a PWC.

Experience to date indicates that the most effective way to provide public works support to the Navy is through a consolidated public works operation. Where the long range operation will support at least 650 PWC personnel, the PWC concept is the best organizational structure. PWCs enjoy the advantages of a centralized management organization, and the economics of scale coincident with that organization. The Navy

Industrial Fund (NIF) concept also provides a PWC with more flexibility as compared with other Navy PW organizations. The NIF concept will be discussed later in this chapter.

The PWC chain of command is shown in Figure 1. Note that the Office of the Navy Comptroller (NAVCOMPT) provides financial management assistance to the Naval Facilities Engineering Command (NAVFAC). The Assistant Commander for Public Works Centers (Code 15) provides the individual PWC's with corporate policy, resource and management support. The various Engineering Field Divisions provide the military chain of command link between NAVFAC and the PWC's.

There are nine PWC's located in areas of large naval shore activity concentrations. These PWC's support major naval complexes in Norfolk, Virginia; Pensacola, Florida; San Francisco, California; San Diego, California; Pearl Harbor, Hawaii; Guam; Subic Bay, Republic of the Philippines and Yokosuka, Japan. All but PWC Yokosuka operate under the NIF cost accounting system.

PWC's provide public works services to over 2000 customers of which nearly ten percent are receiving services in excess of \$150,000 annually. These major customers include naval station/bases, air stations, hospitals/dental clinics, supply centers/depots, shipyards/repair facilities, communications stations, fleet commands, training commands, systems commands, air rework facilities, research and development activities, ordnance commands, ships and other DOD and government agencies.⁸⁹

B. NPWC Standard Organization

The nine PWC's are centrally managed but decentrally operated. They have evolved as a result of the consolidation of many public works

PUBLIC WORKS CENTER
CHAIN OF COMMAND
AND
RESOURCE MANAGEMENT

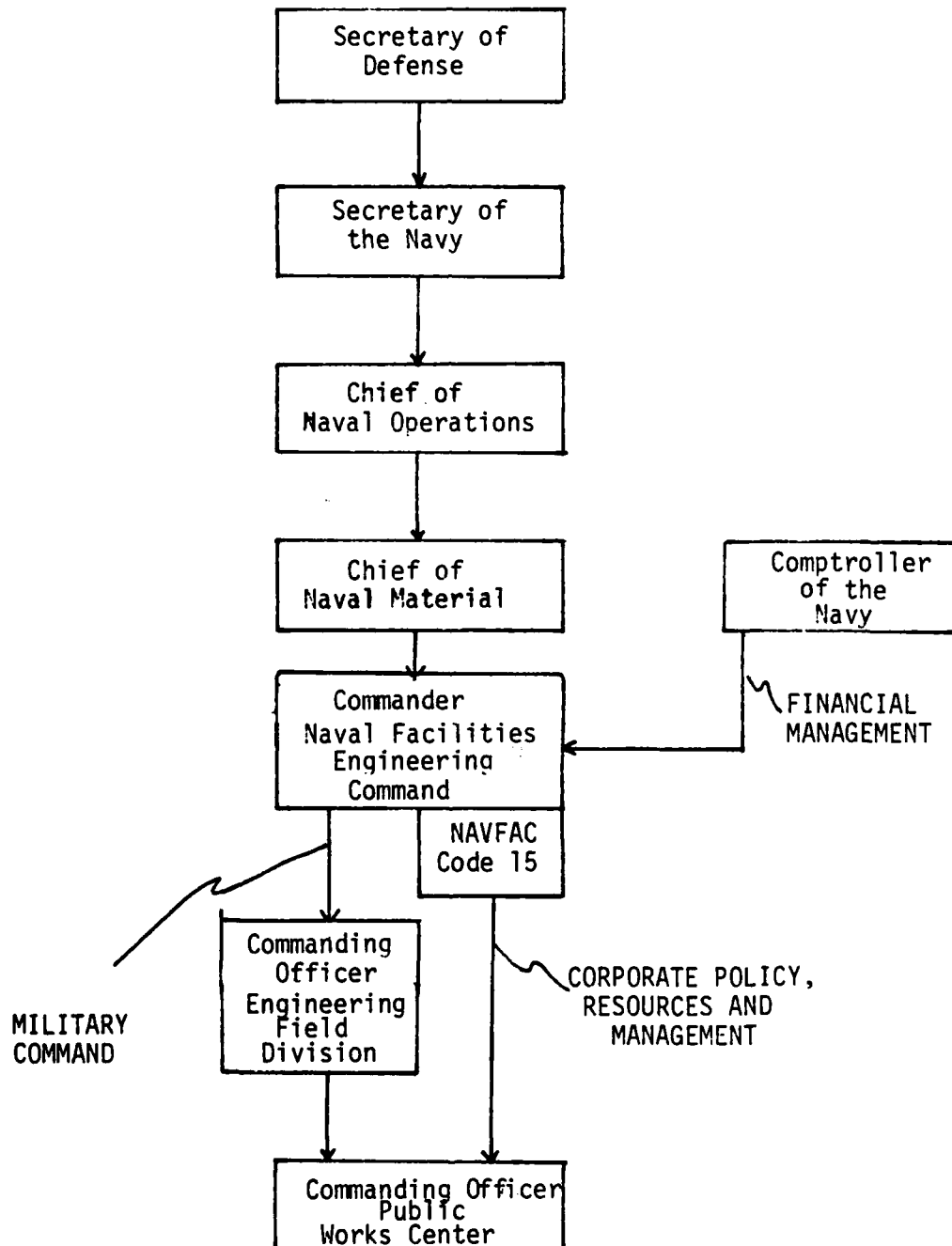
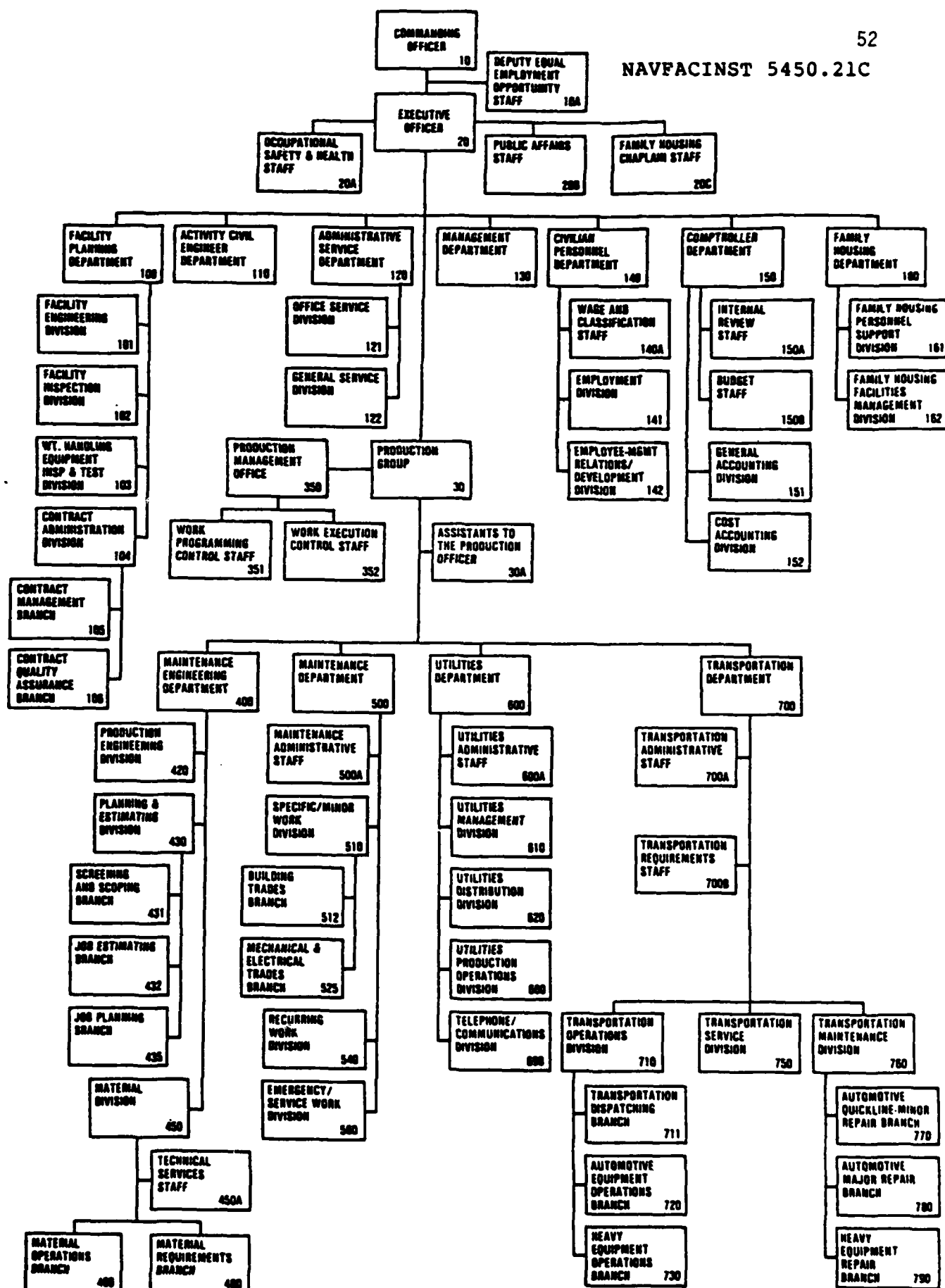


Figure 1

departments as directed by the Secretary of the Navy. Because of this there has been a high degree of management commonality and the achievement of considerable economy.⁹⁰ As a means of sustaining this "management commonality" NAVFAC published an instruction (NAVFAC INSTRUCTION 5450.21C) in April, 1980 which established the standard organization and functions for PWC's (See Figure 2). This standard organization is one of the major strengths of the PWC's. Since all PWC's are on an equal footing, competition between the Centers is encouraged by NAVFAC. The PWC's are also able to share information and obtain help from other PWC's in a more expedient manner due to the standard organization. Because of this, changes to the standard organization are not authorized without NAVFAC approval. The PWC organizations, although standard and uniform, have undergone significant organizational change during the past several years. The PWC's are anything but static organizations. In fact, the latest organizational chart for NPWC Pensacola Florida differs somewhat from this standard organization. This chart is presented later in this chapter.

The staffs of equal employment opportunity and occupational safety and health provide support to the Commanding Officer, Executive Officer and other groups within the PWC in these areas to assure compliance with all local, state and federal statutes.

The Management Department, Civilian Personnel Department and Comptroller Department each provide support in the areas of management improvement, personnel affairs and financial management respectively. This support of the command and of other PWC departments results in more efficient management of the PWC workload and resources. The Housing Department administers the DOD family housing



**PUBLIC WORKS CENTER
STANDARD ORGANIZATION**
Figure 2

policies under the jurisdiction of the PWC. The Activity Civil Engineer Department provides the critical link between the customer activities and the PWC. This close liaison is essential in the successful performance of the PWC's mission requirements. The Facility Planning Department is responsible for shore facilities planning and facilities engineering inspections.

The Production Group makes up the largest portion of the PWC in terms of personnel and consists of the Production Management Office, Maintenance Engineering Department, Maintenance Department, Utilities Department and Transportation Department.

The Maintenance Engineering Department provides professional/technical engineering consultant services to the PWC and customers. These services include production engineering, planning and estimating and material support. The Maintenance Department performs maintenance, repair and alteration services for the customers' facilities. The Utilities Department provides utilities management, distribution and production services for the PWC and customer activities. The Transportation Department provides transportation operations, dispatching, service, maintenance and repair support to the PWC and to customer activities.

C. Navy Industrial Fund

At the very heart of the Navy Public Works Center concept is the Navy Industrial Fund (NIF). The Navy Industrial Fund is made up of fifty individual activities, eight of which are PWC's. The total NIF comprises nearly twenty percent of the Navy's budget and over fifty percent of the Navy's civilian personnel and would rank in the top thirty on the "Fortune" list of 500.

Conceptually the PWC's are individual business operations within a single corporate body. The "Corporation" has a business volume approaching \$1 billion annually. A NIF PWC is the closest thing to a true business operation in the Navy and exists to provide services to other Navy commands. As a business, the individual PWC must "sell" services in order to survive. A NIF PWC is service, not profit-motivated. The financial goal is to operate in a break-even mode. The PWC's operate collectively with a permanent capitalization "corpus" of nearly \$16 million.

The NIF is a revolving fund used to provide monies for operations of designated industrial and commercial type activities. It is designed to be self-sustaining as the "corpus" is reimbursed for costs incurred from customer funds appropriated to pay for the product or service rendered. Any "profits" or "losses" sustained during the process serve to increase or decrease the capital of the fund. Rates (i.e., utilities, transportation, etc.) are then adjusted to balance the fund for future cycles. All NIF activity costs are financed from the activity's net working capital and customers pay before work is performed. Industrial accounting systems form the basis for collecting costs and billing customers. Figure 3 shows the cycle for NIF operations. A customer places work orders and establishes commitments and obligations via the Activity Civil Engineer or Staff Civil Engineer. As services are contracted for or are rendered, depending on their nature, the NIF activity recoups the cost of each service from the customer. With the collection of the bill, the NIF Activity is reimbursed for costs of services.⁹¹

The NIF concept has three important features which encourage better management and which create an environment similar to private industry:

CYCLE FOR NIF OPERATIONS

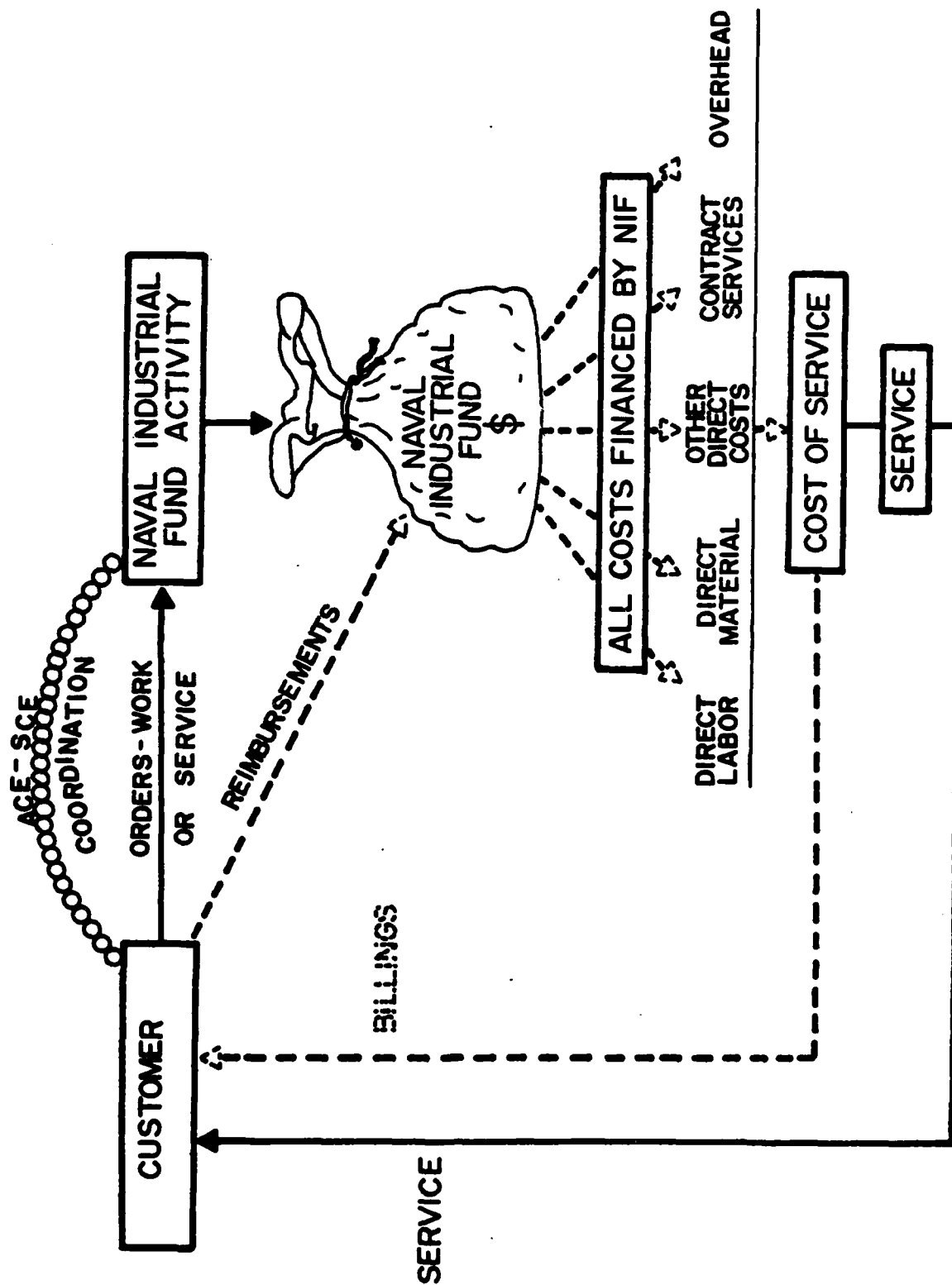


Figure 3

1. A contractual relationship is established between customer and provider whereby the provider must accurately define all tasks, forecast all costs and quote the customer a fixed price in most cases. The customer must provide the funds and thus is motivated to buy only those services truly needed. The rates for PWC services are stabilized or guaranteed throughout the budget execution year and are published prior to the customer's budget cycle needs. The PWC acts as a fiscal surge tank by softening the impact of inflation.
2. NIF enables management to identify costs to a particular job. This is essential for cost control, pricing standards, budget projections based on future workloads and measurement of efficiency.
3. A revolving fund or corpus provides flexibility in utilization of centralized dollars which are relatively free from Congressional appropriation cycles.⁹²

NIF PWC's provide approximately one-third of all Navy public works services. Recent trends of Navy shore activities indicate the consolidation and relocation into major naval complexes where PWC's are located. This trend continues to increase the requirements for services provided by PWC's.⁹³ There is no fixed annual workload for the PWC since the customer's requirements and budgetary decisions dictate the nature and amount of service which will be required from the PWC. The services provided, work performed and level of personnel employment are dependent on customer satisfaction and good business relations. Reasonable service rates, timely response and a favorable image in the eyes of the customer are keys to the success of the PWC organization.

D. PWC Pensacola Florida

Information for this section was obtained from the PWC Pensacola Command Briefing Guide as prepared by the Management Department (Code 130).

1. Mission

PWC Pensacola provides utilities, family housing, transportation services, engineering services, shore facilities planning and other public works maintenance, repair and construction services for The Pensacola Naval Complex. The goals of PWC Pensacola are to provide these services in support of customer activities at minimum cost, with required quality and in response to the customer's requirement for maximum support of their mission.

2. Customer Support

PWC Pensacola is located in Escambia County, the westernmost panhandle county in Florida. Some of the area's major PWC customers, their individual missions and annual PWC requirements (utilities, transportation, maintenance and repair, other facility support) are listed below:

<u>Activity</u>	<u>Mission</u>	<u>Annual PWC Business (Million \$)</u>
Naval Air Station Pensacola	Aviation Operations and Related Training Activities	15.7
Naval Air Rework Facility	Depot Level Maintenance of Designated Weapons Systems and Accessories	12.7
Naval Hospital	Medical and Dental Services for Military Personnel and Naval Aerospace and Flight Research Programs	3.9
Naval Education and Training Program Development Center- Saufley	Training Program, Advancement Examinations, and Other Navy Training Support	2.3

Naval Technical Training Center-Corry Station	Personnel Training in Cryptology, Electronic Warfare and Photography	5.4
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3. Organization

PWC Pensacola is organized in accordance with NAVFAC INST 5450.21. Figure 4 shows the PWC Pensacola organizational chart with some recent changes. Note the redesignation of the Facility Planning Department (Code 100) to the Facility Inspection Department. Administrative Service (Code 120) functions are accomplished within the Comptroller Department (Code 150). The Contracts Department (Code 200) carries out many of the contract management and administration functions previously performed by Code 100. Within the Production Group note the designation of the Material Department (Code 800). This function was previously performed within the Maintenance Engineering Department (Code 400).

The various functions at PWC Pensacola are performed by a total of 736 personnel, excluding military. Of these personnel, 178 are general schedule employees and 558 are wage grade. The wage grade employees (building trades, mechanics, utility operators/controllers, planners and estimators) account for over \$13 million in annual payroll costs. The general schedule employees (management, engineers, inspectors, clerical/accounting, production) account for over \$3 million in annual payroll costs.

4. Revenue/Services

The revenue of PWC Pensacola was over \$54 million in FY83. A breakdown of revenue by the type of service is presented below and shown in Figure 5:

NPWC PENSACOLA ORGANIZATION

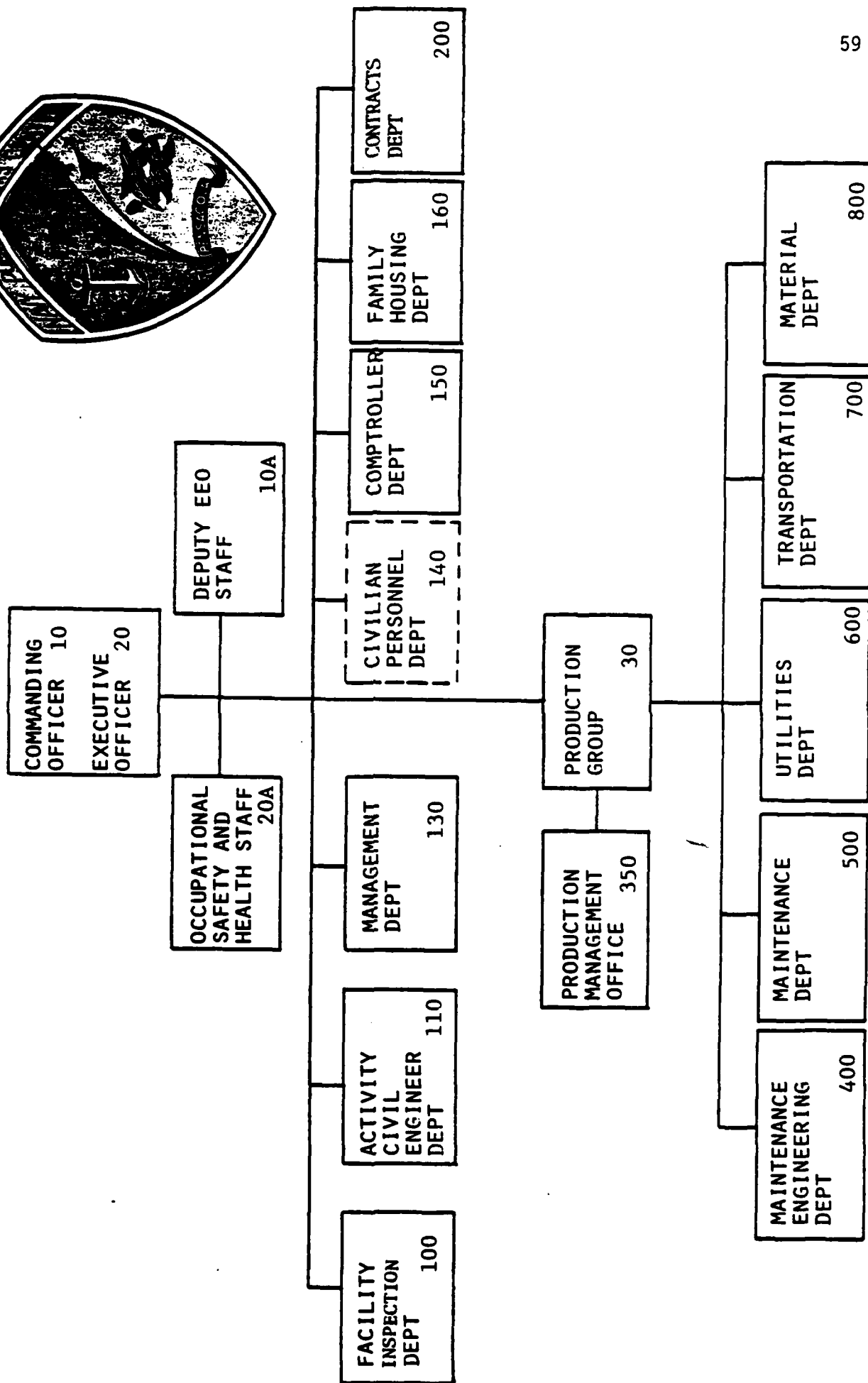
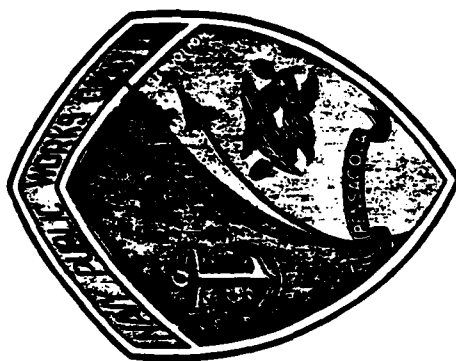
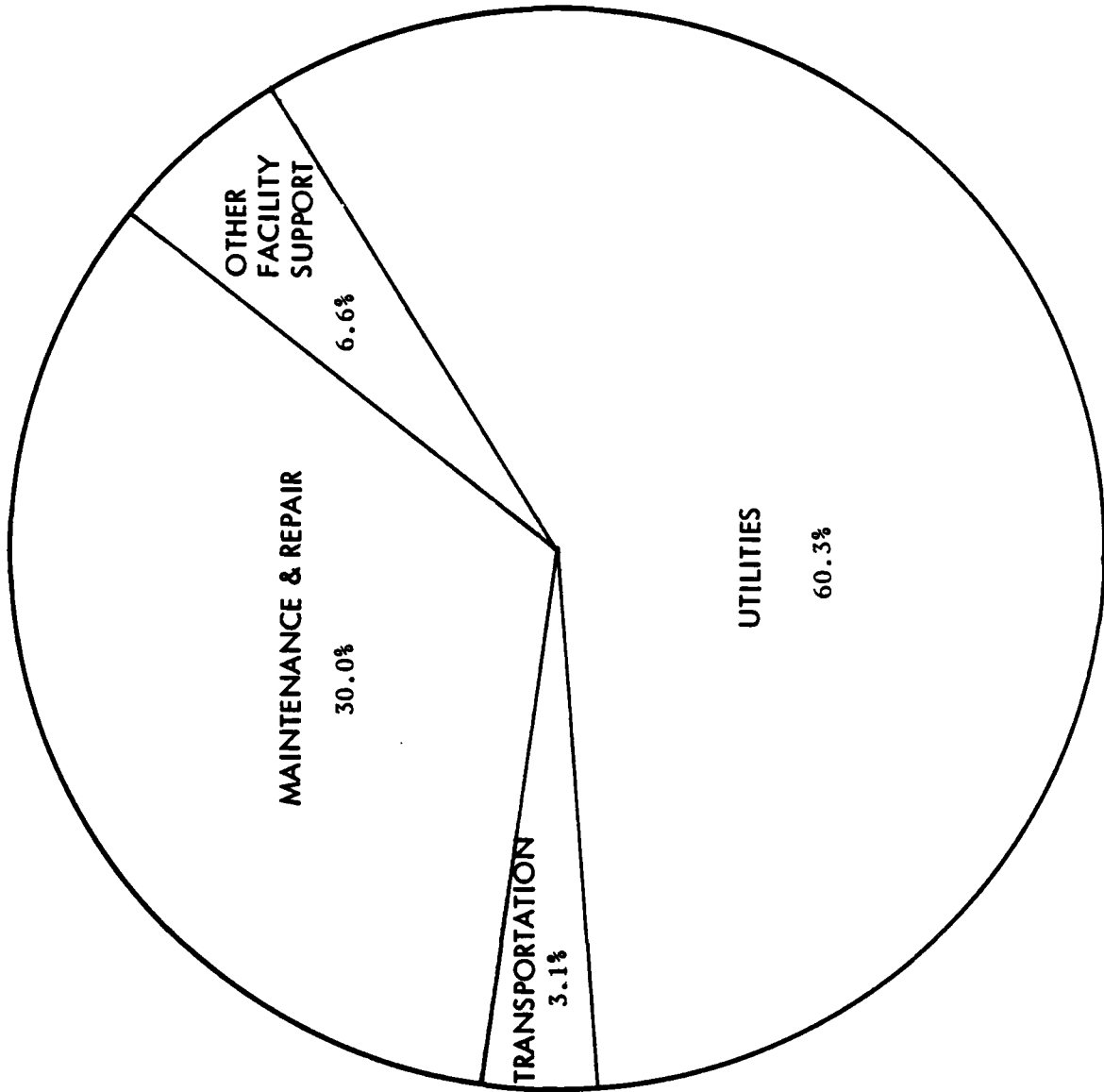


Figure 4



FY 83: REVENUE BY TYPE SERVICE

Figure 5

<u>Service</u>	<u>Functions</u>	<u>Resources</u>	<u>Revenue (Million \$)</u>
Maintenance and Repair	Maintenance, Repair, Alteration of Real Property; Minor Construction, Recurring/Preventive Maintenance	300-350 Tradesmen	16.2
Utilities	Electricity, Steam, Water Sewage/Industrial Waste, Telephone, Compressed Air	118 employees 3 Turbo Generators 17 Boilers 170 mi. of power lines 13 wells 2 Waste Treatment Plants Centrex Switchboard	32.6
Transportation	Vehicle/Equipment Rental, Maintenance Allowance; Transportation Support	738 Vehicles/Equipment 25-30 Operators 20-25 Mechanics	1.7
Other Facility Support	Plans and Specifications, Facilities, Planning, Engineering Studies, Facility Inspection	15-20 Engineers 20-25 Inspectors	3.6

5. Other Services

PWC Pensacola also provides other services in the areas of contracting and civil engineering support. In the contracts area, PWC Pensacola provides the following functions: contract advertisement/negotiation, award and administration; construction contract management/inspection; facility support contract management/quality assurance; and management of the PWC warranty program. Annual contract volume exceeds \$13 million.

Construction representatives, contract specialists and quality assurance evaluators comprise the thirty-one employees in this area.

Civil engineering support is provided to PWC customers through the assignment of active duty Navy Civil Engineer Corps officers. There are two categories in this area, Staff Civil Engineers (SCE) and Activity Civil Engineers (ACE). The SCE is assigned to a specific customer command while the ACE is assigned to the PWC in support of one or more designated customer commands. The SCE and ACE provide technical expertise regarding command operation, maintenance requirements, facility planning, maintenance planning, budget requirements, and coordination between the customer and the NPWC.

PWC Pensacola also provides family housing support to military personnel stationed in the area of the Pensacola Naval Complex. The functions of family housing includes assignment to Navy family housing; housing referral service for off-base housing; management of housing assets; annual family housing surveys; and operation of self-help stores. Resources include 783 housing units and 52 mobile home spaces.

6. Categories of Work

Work performed by the PWC for its customers is categorized as follows: emergency work, service work, minor work, recurring work, and specific work. Figure 6 details the various work categories with the manhour breakdown and funding method. Emergency service and minor work are generally performed without the benefit of a great deal of advanced planning. More detailed planning would require a greater investment of money and time than is generally warranted for this type of work.⁹⁴

CATEGORIES OF WORK

- EMERGENCY
 - IMMEDIATE ACTION TO:
 - PREVENT LOSS OR DAMAGE TO GOVERNMENT PROPERTY
 - RESTORE ESSENTIAL SERVICES
 - ELIMINATE HAZARDS
- SERVICE
 - 16 MANHOURS OR LESS REQUIRED
MINIMUM PROCESSING
FUNDED BY STANDING JOB ORDER - QUARTERLY
- MINOR
 - 17 TO 80 HOURS REQUIRED
SIMPLE - FEW TRADES
FUNDED BY STANDING JOB ORDER - QUARTERLY
- RECURRING
 - PERFORMED ON ESTABLISHED FREQUENCY
ESTIMATED FOR 1 YEAR
FUNDED BY STANDING JOB ORDER - QUARTERLY
- SPECIFIC
 - OVER 80 HOURS
ESTIMATED → FUNDED → PLANNED → SCHEDULED
OFFERED
 - FIXED PRICE
 - COST REIMBURSABLE
 - ACCOMPLISHED BY CONTRACT WHEN
 - MORE ECONOMICAL
 - NO INHOUSE CAPABILITY EXISTS
 - MORE RESPONSIVE
 - FUNDED BY SEPARATE JOB ORDER FOR EACH JOB

Figure 6

7. Response, Quality and Cost

The attributes of response, quality and cost are closely interrelated in a PWC's way of doing business. The objective of PWC Pensacola is to provide the required response and quality at the minimum cost. In determining the criteria for response to a customer's needs, typically the following questions pertain:

What does the customer want?

When does the customer want it?

How badly does the customer want it and how much will the customer pay?

How much disruption is acceptable?

Material/Equipment availability?

Influencing factors include impact on the system, negotitaion and follow-up through available channels.

The quality of work must be sufficient to fulfill customer requirements and expectations at a reasonable cost. Quality is assured via inspection of material and workmanship. Some guarantees of quality include fixed price work, maintenance service agreements and warranties.

The cost of PWC work to the various customers is designed to be the least expensive alternative. This lower cost is achieved by the consolidation of services which tends to reduce overhead costs. The use of industrial funding (NIF) also more equitably distributes the total cost to all customers. Figure 7 demonstrates some cost comparisons between PWC and commercial sources in some representative areas.

COST COMPARISON

	<u>NPWC</u>	<u>COMMERCIAL</u>
o SERVICE CALL	\$24.90/HR (INCLUDES \$25 MTL)	PLUMBING/ELEC \$22.50 - \$35/HR - MTL EXTRA
		APPLIANCES \$16 - \$25 SERVICE CHARGE PLUS \$22.50/HR PLUS MTL
o OTHER MAINTENANCE	\$17.22 TO \$26.17 (VARIES W/TRADE)	TYPICAL CONTRACTOR - \$14.47 BASE ELECTRICIAN: 2.28 FRINGES <u>16.75</u> 2.18 13% OVERHEAD 1.17 6% PROFIT <u>\$20.10</u>
o TRANSPORTATION	\$104/MO PLUS 11¢/MI	\$390 MO TO \$527 MO PLUS .10 TO .27/MI
- COMPACT SEDAN		
o UTILITIES		
- WATER	\$1.13/1000 GAL	\$1.13/1000 GAL
- SEWER	\$1.20/1000 GAL	\$1.74 - 2.78/1000 GAL
- ELECTRICITY	\$77.18 MWH	\$90.35 MWH (RESIDENTIAL)

Figure 7

CHAPTER FOUR
COMMERCIAL ACTIVITIES PROGRAM IMPLEMENTATION
AT THE PWC LEVEL

A. Purpose

The purpose of this section is to evaluate the effects of the Commercial Activities (CA) Program on a particular field activity, namely, PWC Pensacola, Florida. An overview of the current governing document which covers Navy implementation of the CA program (OPNAV INSTRUCTION 4860.6C of February 5, 1982) will be given, with a brief discussion of recent changes to the instruction. Problems encountered and productivity improvements will be addressed and the current status of the CA Program at PWC Pensacola will be outlined.

B. Governing Directives

The primary document for the Navy's implementation of the CA Program is OPNAV INSTRUCTION 4860.6C of February 5, 1982. The Instruction implements the policies established in OMB Circular A-76 of March 1979. In addition, the Instruction accommodates the changes required by the applicable SECNAV and DOD instructions. Since April 1982, there have been twenty separate changes to the OPNAV Instruction. These changes have served to keep the Instruction current by providing the necessary CA Program information to the field activities.

The Instruction provides an expanded discussion of Navy policy for the CA Program. It also specifies responsibilities and approval

authority and provides procedures for new starts and expansions. Procedures for the CA Program inventory and review are also provided. Finally, the Instruction provides an expanded discussion of all phases of the CA cost comparison procedures.

Changes to the Instruction since the August 1983 revision to Circular A-76 have not attempted to implement all of the procedures contained in the new A-76 revision. In fact, language contained in change 1-18 to the Instruction (CNO WASHINGTON DC message 171833Z Aug. 83) indicates that the new A-76 will become effective Navy-wide after release by the Office of the Secretary of Defense. Several key points discussed in the new Circular were made effective in the Instruction. The first of these deals with the Most Efficient Organization (MEO) cost of direct labor. The cost of direct labor is now based on the projected staffing requirements identified in the MEO rather than on the actual pay rates of the existing civilian employees.

The Civil Service Act permits an employee who loses his job through a Reduction in Force (RIF) to retain the same pay level for three years even though he may be occupying a lower grade position. The difference between the pay received and the pay level of the job occupied had been made a part of the CA cost study or cost comparison as a cost to the Government to be added to the contract price. The new guidance eliminates the retained pay cost entirely and is not to be computed or incorporated as part of the cost study or cost comparison.

The rules governing reestablishment of the in-house operation if the contractor defaults are discussed in change 1-20 to the Instruction (CNO WASHINGTON DC 290045Z Oct. 83). If contract performance has actually

started and the contractor defaults, the in-house organization may not be automatically permanently reestablished. A replacement contractor must be found to perform under the existing contract without a new cost study. A new CA cost study is required if the activity wants to bring the function back in-house. A temporary reestablishment of the in-house performance is permitted until a replacement contractor is found or a new cost study is performed.

The existing Instruction will probably undergo complete revision with the release of the revised Circular by the Office of the Secretary of Defense.

C. PWC Pensacola Program Status

The Commercial Activities Program at PWC Pensacola is serious business. To date, PWC Pensacola is the only Center to have won in-house all five CA functions studied. The success of PWC Pensacola is due in large part to a very strong commitment by upper management in the overall CA effort. This commitment has led to a total command awareness of the CA program and an appreciation of the potential impact of the program on the PWC organization. Key factors in the CA program at PWC Pensacola have been: The education of employees regarding CA, accurate and timely cost studies, a dedicated Management Department, and efforts to arrive at the MEO well in advance of the actual CA study. It has been an "all hands" effort and one which should be commended.

1. Background

PWC Pensacola has utilized the services of private industry since the mid 1970's for the performance of certain functions. The choice of these functions has been at the discretion of the PWC and have for the most part

involved the more labor-intensive types of work. These types of contracts are known as maintenance service contracts and generally take the form of a firm fixed price contract for a period of one, two or three years. PWC Pensacola's annual maintenance service contract costs are in the range of 3-4 million dollars.

In the early 1980's, the CA program began to affect PWC Pensacola and a number of PWC functions were identified for study under the provisions of OMB Circular A-76. Naval Facilities Engineering Command (NAVFAC) began to organize the PWC "Corporation" so that each PWC would study the same function at the same time. A study group was set up within NAVFAC to aid in the development of the performance work statements and to act as a focal point for questions. The individual PWC's were encouraged to share information and lessons learned as the program progressed. This approach to the implementation of the CA program serves to demonstrate the effectiveness of the PWC corporate structure and the importance of the standard PWC organization.

2. CA Results

The functions for study by the PWCs include pest control, surfaced areas, administrative telephone, housing maintenance, transportation (light), facilities maintenance and air conditioning, transportation (heavy), and utilities maintenance/operations. All but the last three functions have been completed and the results for PWC Pensacola are shown below:

<u>CA Function</u>	<u>PWC Bid (\$ K)</u>	<u>Contractor Low Bid (\$ K)</u>	<u>Difference</u>
Pest Control	614	707	93
Surface Areas	224	267	43
Admin. Telephone	625	1,741	1,116
Housing Maint.	1,424	1,807	383
Transportation (light)	2,732	5,233	2,501
	<u>\$5,619</u>	<u>\$9,755</u>	<u>\$4,136</u>

Overall, the PWC bids were forty-two percent lower than the contractor low bids. All of the above functions were retained for in-house performance.

The MEO for each of the functions studied at PWC Pensacola resulted in either a reduction in the number of positions or in grade reductions. The MEO results are tabulated below:

<u>CA Function</u>	<u>FY Year Studied</u>	<u>Previous Positions</u>	<u>MEO Positions</u>
Pest Control	82	8	6
Surface Areas	82	7	4
Admin. Telephone	82	7	7
Housing Maint.	83	19	10
Transportation (light)	83	33	21
		<u>74</u>	<u>48</u>

Of the 74 positions studied, 48 were retained for a 35 percent reduction in personnel required to perform the five functions. In the administrative telephone areas, there were no cuts in positions but there was one grade reduction. There were also some grade reductions in the family

housing maintenance area. The above cost and MEO data were obtained from the PWC Pensacola Management Department.

D. Problems/Concerns

There are several problems facing upper management in the implementation of the CA program at the PWC level. These concerns are being voiced at all levels within the PWC chain of command. For some there are no immediate solutions, while for others a high level of management expertise and dedication will be required to deal with the problem.

1. Level of Effort (LOE) Specifications

Firm fixed price contracting is the preferred method for CA program pricing. However, some public works requirements, such as repairs, alterations and maintenance, can be very difficult to quantify in terms of frequency or the amount of work involved. Total manyears required can be obtained but the scope and trade mix are often difficult to specify in advance for firm fixed price bidding.

Over the past year, there has been a continued effort to deal with the problem of specifying work of an indefinite scope. Early guidance specified that if it was not feasible to require unit pricing for all indefinite work, then a combination of fixed unit price and level of effort (LOE) was permitted. Level of effort requires pricing by labor hour for a specified number of hours of work. Shortly thereafter guidance was issued suspending all CA cost study efforts in which indefinite work involved level of effort.

At the root of the problem is a key conflict between statutory and regulatory requirements. Section 502 of Public Law 96-342 as amended by Section 1112 of Public Law 97-252 (Defense Authorization Act) does

not permit the contracting of positions performing commercial activities without a congressional announcement and a cost comparison demonstrating economy. At present, activities are unable to provide an accurate projection of non-recurring jobs to allow bidders to submit accurate fixed price bids for use in a multi-year comparison. Extensive use of LOE specifications greatly complicates the ability to validate the provisions of contracted services and increases the vulnerability to waste, fraud and abuse. The use of LOE specifications also serves to reduce price competition which is contrary to the goals of the CA program.

The Defense Acquisition Regulations (DAR), state that as a matter of DOD policy, construction, alteration and repair work will generally be performed by contract. This policy is reflected in DAR 18-103 dated 1 July 1976, and provides only limited exceptions for performance of this work by military or civil service personnel. Essentially civil service personnel are tasked with maintenance and repair incident to maintenance.

The Chief of Naval Operations has determined that the LOE approach is unacceptable for use in the performance work statement (PWS) for public works contracting. Work which cannot be identified in the fixed price or defined indefinite quantity part of the PWS is to be excluded from the CA cost comparison. Every effort is to be made in defining indefinite work in the fixed price portion of the PWS, along with other work that can be defined for unit price costing.

The task of defining indefinite work is a monumental one. The availability of this type of data is dependent on the organization, record-keeping, and reporting systems of a particular activity. The PWC system is more accommodating than those of the smaller Public Works

Departments but even the PWC system does not lend itself to quantifying work in anything other than manhours. The type of information needed must be retrieved manually and is a very time-consuming process.

Recent guidance from NAVFAC's Southern Division in Charleston, S.C. indicates that the work excluded from the PWS is to be accomplished by one of two methods. Long-range projects are to be performed by using competitively bid, firm fixed price contracts or open-end construction contracts for which there are definite plans and specifications. The second alternative is to maintain a number of public works craftsmen, not to exceed twenty percent of the existing public works maintenance work force. This group will perform urgent maintenance and incidental specific repair and maintenance work not covered by the PWS or where time constraints preclude the preparation of plans and specifications. The craftsmen remaining must be provided with adequate shop space, tools, equipment and supervision to ensure efficient utilization of the group.

2. Quality Control

Quality control with regard to contractor performance has always been a concern within the PWC organization. With competitively bid contracts, there is no guarantee that quality work will be performed. Past experience has certainly supported this fact. Experience with previous maintenance service-type contracts at PWC Pensacola indicates three main problem areas. First, there is usually a lack of inspectors to inspect the work. Secondly, those inspectors are sometimes not qualified to inspect in certain specific areas. Finally after a period of time with the same contractor, a friendship results between the inspector and contractor. This can often affect the judgement of the inspector in terms of contract performance.

For quality control to be effective, it must be properly applied. The contractor must be provided with the incentive to perform. This "incentive" is best handled in the contract language. The language must introduce liability making it in the contractor's best interest to keep the system running or to keep the performance at a certain level.

3. CA Savings/PW Rates

Another problem area requiring management attention is in demonstrating the benefits of the CA process (MEO, etc.) to the PWC customers. In order to provide as much advance planning and budgeting as possible to the customer, rates for PWC services are published one year in advance of the budget cycle. The customer does not see an immediate benefit resulting from the PWC's CA efforts.

The challenge for the PWC is one of customer relations. The customer must be kept apprised of CA progress and of how any changes will affect him. The stabilization resulting from CA is done to protect the customer. The command must be ready to answer questions from customers regarding the potential impact of CA on his activity. A thorough understanding of the PWC mission and organization is also an important part of this process.

4. Time/Cost to Perform Studies

One of the most difficult requirements placed on PWC Pensacola by the CA program has been in the amount of time required to perform the various CA requirements. These requirements are heaped on in addition to the normal workload of running a particular department or work center. The workload has been very unpredictable and requires a great deal of dedication and perseverance on the part of the employees.

The costs attributed to CA in terms of manhours are difficult to keep track of. Estimates of \$60,000 have been made for fiscal year 1984, to date, but these figures may not reflect the total applied effort. Costs for subsequent studies should reflect better economy and more readily identifiable applications.

E. PWC Productivity

PWC Pensacola has been the recipient of the prestigious Chief of Naval Material Productivity Excellence Award for the past two fiscal years (1982 and 1983). Competition for the award is keen, with only eight of the 200 world-wide installations under the command of the Chief of Naval Material receiving the presentation. Those commands winning the award have demonstrated creative problem-solving techniques and have found better ways of performing industrial type tasks.⁹⁵

Selected as the best in productivity, PWC Pensacola saved more than \$1.3 million during fiscal year 1983. The Center's aggressive approach to the CA Program was cited by Admiral Steven A. White, Chief of Naval Materials, as one of the "remarkable achievements" which resulted in dollar savings to the taxpayers. Captain William H. Harmon, PWC Pensacola Commanding Officer, cites a "feeling of pride and professionalism coupled with a competitive spirit, strong work ethic and hard work at all levels" that made fiscal year 1983 an outstanding year for PWC Pensacola.⁹⁶

1. MEO/Better Business

One of the biggest disadvantages of competing a government activity with a commercial activity has traditionally been the lack of a profit

motive on the part of the government. Activities such as a PWC are operated with first the customer's interest in mind, and efficiency or economy ranked second. With the renewed interest in the CA Program and the development of the MEO concept, there is now some definite motivation to perform economically, efficiently and productively to give the customer the level of service needed.

The MEO concept has forced PWC Pensacola to take a critical look at all of its functions. Many of these MEO changes have resulted in grade reductions and displaced personnel but productivity has not suffered. In fact, the intensity of the work has picked up and peer pressure to perform as required has begun to exert its influence. The workers' attitudes have improved.

While studying the transportation function, it was noted that the PWC cost per mile to maintain light vehicles was significantly higher than commercial rental companies. Upon investigation, it was determined that a great deal of the routine maintenance performed on PWC vehicles went far beyond that which is necessary to keep the vehicles running. A revamping of various maintenance procedures resulted in a significant reduction in cost per mile. Another modification in procedure was adopted for the manner in which damaged vehicles were charged for repair. Past procedure had been to repair vehicles damaged by customers and reflect the costs in future rates. The new procedure calls for the customer to pay directly for any damage which results while the customer has the vehicle in his possession. This is a far more equitable solution and results in better business.

2. Customer Satisfaction

Since the completion of the first CA study in fiscal year 1982, there have been no customer complaints in the areas affected by staffing reductions. The customers are aware of the PWC's CA status and have on the whole been very supportive. PWC workers have been instructed to perform only those tasks listed on the work order. In the past, customer requests for additional services were made directly to the workers resulting in variances in the actual times required to perform the original job. Presently any additional work desired by the customer must be processed through the normal request channels.

3. Union Relationships

Another very positive result of the CA Program at PWC Pensacola is the degree of renewed cooperation between the labor union and management. The union has worked very closely with upper management and has not inhibited any of the necessary MEO actions. The spirit is a very cooperative one with both sides doing that which is necessary to fulfill the program requirements.

CHAPTER FIVE
COMMERCIAL ACTIVITIES PROGRAM FUTURE

A. Upcoming PWC Studies

Information for this section was obtained from the Management Department at PWC Pensacola.

The CA studies to be conducted during fiscal years 1984 and 1985 will have a very significant impact on PWC Pensacola and will affect considerably more people than the previous studies. In fiscal year 1984, the PWC will be studying facilities maintenance and air conditioning, and transportation (heavy equipemnt). The fiscal year 1985 study involves utilities maintenance and operations. A breakdown of the three remaining CA functional areas is shown below:

<u>Bid Opening Dates</u>	<u>CA Function</u>	<u>Civilian Positions</u>
August 1984	Facilities Maintenance and Air Conditioning	126
September 1984	Transportation (Heavy)	29
September 1985	Utilities Maintenance/ Operations	109

The facilities maintenance function involves the emergency, service, minor, preventive and some specific maintenance of facilities, structures and dynamic equipment. The scope of the function includes the utility distribution systems excluding electrical distribution. The function does not encompass utilities production or any of the treatment plants. Emergency/service work involves approximately 1000 requests per month.

Recurring maintenance is comprised of 157 jobs per year and there are currently 62 maintenance service agreements in effect. Minor work accounts for 17 percent of the maintenance effort while specifics make up 36 percent.

The transportation functional area of heavy equipment involves the maintenance, repair and operation of construction and specialized equipment. The maintenance and repair of customer owned equipment accounts for the largest portion in this area and includes 561 pieces of various equipment types (fire/crash, materials handling, aircraft tow and crane/hoists). PWC owned equipment involves 113 pieces including cranes, materials handling, runway support, construction, and specialized equipment (compressors, welders, generators, etc.). Heavy equipment operations involve crane operators, riggers, etc.

The utilities function covers the maintenance and operation of all utility plants including electrical distribution. Other collection and distribution systems are excluded from this functional area. The utilities operated by PWC Pensacola include: 3 turbo-generators, 5 diesel generators, 17 boilers, 10 fresh water wells, 170 miles of power line, 12 air compressors, 5 potable water pumping stations, 6 reservoirs and 2 waste treatment plants.

Some of the concerns of PWC Pensacola in the upcoming studies include: customer billing and funding, determining the minimum level of planned maintenance, conflicts in customer desires and maintenance requirements and inadequate equipment maintenance history.

Another area under consideration for these upcoming studies is to introduce a contract with four option years instead of only two. This type of contract could enhance the bidding and would give the contractor a longer term contract while discouraging "buy-ins". The contract would

encourage a better PM program in lieu of breakdown maintenance and the contract could be terminated before any option year.

B. CA Strategy

PWC Pensacola has developed a winning attitude with regard to the CA Program. Captain William H. Harmon, Commanding Officer, PWC Pensacola, in a recent command newspaper article called upon the PWC employees to "take a detailed look at the way we do business and develop the methodology which will result in a more efficient and effective in-house operation." He emphasized some of the management study techniques to be used as the basis for the fiscal year 1984 CA function studies. These techniques will include work measurement, value engineering, methods improvement, position management, and systems analysis, in addition to others.⁹⁷

Rita D. Foster, Chief of the Fort Eustis Commercial Activities Division, lists six ways to develop a winning strategy:

1. Educating managers and workers in the CA program, goals and methodologies.
2. Gaining worker confidence in the CA team's efforts.
3. Achieving a positive, optimistic attitude on the part of the workforce.
4. Increasing productivity.
5. Recording all workload performed
6. Using a zero-based approach to devise a Most Efficient Organization.⁹⁸

The first three items listed above are the foundation for a successful CA Program. PWC Pensacola's program is a solid one with proven results thus far.

In the Commercial Activities Program arena, it is inevitable that some functions will be contracted out and others will remain in-house. As long as commanding officers are required to ensure that functions are performed as economically as possible, the method of performance must be left to the final cost comparison. There are no guarantees that an activity will be retained in-house. There are far too many variables. Rita D. Foster sums up the situation very well by saying:

"If we work to make an activity competitive, and and it still is defeated in a cost comparison, we (and the commander) have not failed. If we work to keep a function in-house and it is defeated in a cost comparison, we (and the commander) have failed."

Martin Lang, Vice President, Water Pollution Control Federation, and a 40 year employee of the City of New York, strongly supports a balance of contract and in-house effort in delivering public service. His main thought is that the public sector is vulnerable in both quality and cost of services, when the practices of public employees are not challenged periodically by comparison with productivity in the private sector or in other governmental agencies.⁹⁹

C. Cumulative Cost Savings/Projections

The Office of the Assistant Commander for Public Works Centers has compiled figures on the cumulative cost savings to date for the NAVFAC CA Program. These figures deal with three primary areas of savings; a contracted area, a MEO area, and a retained opportunity cost section.

For the contracted area, the savings is the difference between the government bid and the adjusted contractor's bid, or more simply the amount that the contractor won by. In the MEO area, the savings result

when the function is performed in-house. The difference between what the government was originally paying and what it would cost under the Most Efficient Organization constitutes the savings. The retained opportunity cost savings results from a comparison between the Government's MEO and the contractor's adjusted bid. It is not a true cash savings, but simply an opportunity cost that reflects going to contract without a cost comparison. The following table summarizes the NAVFAC cumulative savings to date.

<u>Area</u>	<u>Savings/(Cost) \$ Million</u>
1. Contracted	17.7
2. MEO	14.2
3. Retained Opportunity Cost Savings	32.2
4. Costs incurred to date - NAVFAC CA Program	(6.4)
5. Net Cost/Benefit (1+2+3+4)	57.7
6. Net Cash Savings (5-3)	25.5

The above figures were obtained from NAVFAC CODE 15 and reflect the entire NAVFAC CA Program including Public Works Centers and Construction Battalion Centers.

Of the 648 positions reduced in fiscal year 1983, 516 were PWC positions. Of the 516 positions reduced, 236 were reduced via MEO and the remainder were converted to contract performance. This indicates a 46 percent reduction of target through MEO. To date for 1984, there have been 102 positions studied with 26 reduced by MEO and the rest retained in-house.

The trend over the past three years has indicated an increase in MEO savings as compared to conversion to contract. Projections for 1984 point toward a higher MEO savings and reduced conversion to contract.

The following table shows NAVFAC progress with regard to positions studied and conversion rates for fiscal years 1982 and 1983. The required conversion rate for FY 1984 is also shown.

<u>FY</u>	<u>Positions Studied</u>	<u>Target Assigned</u>	<u>Target Met</u>	<u>Conversion Rate</u>
1982	503	307	293	58%
1983	1248	707	648	52%
1984	1420	588	26	(Ongoing)

To reduce the 588 positions in fiscal year 1984, a conversion rate of 41 percent is required. With past performance as indicated, NAVFAC should meet the assigned conversion rate for 1984.

CHAPTER SIX CONCLUSIONS/RECOMMENDATIONS

A. Most Efficient Organization

The MEO concept is perhaps the single most significant result of the Commercial Activities Program. A thoroughly researched MEO has proven to be both productive and economical in providing the level of service needed by PWC customers. It is recommended that the MEO's continue to reflect the proper level of manning required to perform the assigned tasks.

B. Legitimate Competition

Care must be taken to ensure that performance work statements are not organized to compete with businesses that do not exist. The nature of the product purchased in this process would be difficult to determine. Competing Federal employees on a more legitimate basis should be explored even if it requires more contracts and more management attention.

C. Management Challenges

Efforts to deal with indefinite quantity work and allocation of time to perform the CA studies must continue to obtain management attention. Methods of quantifying work performed must be integrated into the PWC data collection systems. Level of effort will continue to be a weak link until the problem is dealt with in a decisive manner.

Management must continue the efforts to keep better track of time spent in the CA effort. The time spent must be readily identifiable for audit purposes or to determine program justification at some future date.

The cooperation between management and the labor unions must be continually improved. The union must be educated as to the workings of the CA Program and consulted when necessary. This renewed cooperation has been a most welcome benefit of the CA Program.

D. Customer Relations/Satisfaction

The customer must be made aware of the potential impact of the CA Program on his command. A thorough understanding of the PWC's mission and organization is essential in this regard. Customer needs must continue to be of primary concern to the PWC and every effort must be made to continue to provide quality service, at the least cost, in a timely fashion.

E. Quality Control

Quality control must be aggressively pursued both in-house and with commercial contracts. The contract language must provide the contractor with the "incentive" to perform in a satisfactory manner. The contract must make it in the contractor's best interest to maintain the necessary performance level by introducing contractor liability.

F. Future Effort Suggestions

The following areas are considered good topics for further development:

1. Base Operating Services Contracting - history, implementation, status, cost effectiveness.
2. Effects of the CA program on smaller Navy public works activities including public works departments, lead activities, etc.

3. Application of the CA program to overhead functions.
4. Contract vs in-house at state, county and local government levels - application of CA approach.

GLOSSARY OF TERMS

ACE	-	Activity Civil Engineer
ACEC	-	American Consulting Engineers Council
AFGE	-	American Federation of Government Employees
BOB	-	Bureau of the Budget
BOS Contract	-	Base Operating Service Contract
CA Program	-	Commercial Activities Program
C/I Activity	-	Commercial/Industrial Activity
CNO	-	Chief of Naval Operations
COGO	-	Contract Operated - Government Owned
DAR	-	Defense Acquisition Regulations
DLA	-	Defense Logistics Agency
DOD	-	Department of Defense
FICA	-	Federal Insurance Contribution Act
FPI	-	Federal Prison Industries
FTE	-	Full-Time Equivalent
GAO	-	General Accounting Office
GSA	-	General Services Administration
LOE	-	Level of Effort
MEO	-	Most Efficient Organization
NAVCOMP	-	Navy Comptroller
NAVFAC	-	Naval Facilities Engineering Command
NAVMAT	-	Naval Material
NCTSI	-	National Council of Technical Service Industries
NIF	-	Navy Industrial Fund
NPWC	-	Navy Public Works Center

OFPP	-	Office of Federal Procurement Policy
OMB	-	Office of Management and Budget
OPM	-	Office of Personnel Management
OPNAV	-	Naval Operations
OSD	-	Office of the Secretary of Defense
PWC	-	Public Works Center
PWS	-	Performance Work Statement
RIF	-	Reduction In Force
SCE	-	Staff Civil Engineer
SECNAV	-	Secretary of the Navy
USN	-	United States Navy

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IMPLEMENTATION OF THE COMMERCIAL ACTIVITIES PROGRAM AT 2/2
NAVY PUBLIC WORKS CENTER PEEBECOLA (U) FLORIDA UNIV

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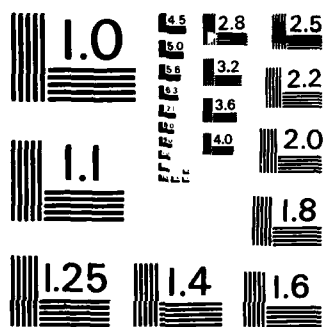
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APPENDIX A

Information for this Appendix was obtained from OMB Circular No. A-76 (Revised), dated August 4, 1983.

Attachment A
OMB Circular No. A-76EXAMPLES OF COMMERCIAL ACTIVITIES¹Audiovisual Products and Services

Photography (still, movie, aerial, etc.)
Photographic processing (developing, printing, enlarging, etc.)
Film and videotape production (script writing, direction, animation, editing, acting, etc.)
Microfilming and other microforms
Art and graphics services
Distribution of audiovisual materials
Reproduction and duplication of audiovisual products
Audiovisual facility management and operation
Maintenance of audiovisual equipment

Automatic Data Processing

ADP services -- batch processing, time-sharing, facility management, etc.
Programming and systems analysis, design, development, and simulation
Key punching, data entry, transmission, and teleprocessing services
Systems engineering and installation
Equipment installation, operation, and maintenance

Food Services

Operation of cafeterias, mess halls, kitchens, bakeries, dairies, and commissaries
Vending machines
Ice and water

Health Services

Surgical, medical, dental, and psychiatric care
Hospitalization, outpatient, and nursing care
Physical examinations
Eye and hearing examinations and manufacturing and fitting glasses and hearing aids
Medical and dental laboratories
Dispensaries
Preventive medicine
Dietary services
Veterinary services

¹ This list should be used in conjunction with the policy and procedures of the Circular to determine an agency's A-76 commercial activities inventory. It has been compiled primarily from examples of commercial activities currently contracted or operated in-house by agencies. It should not be considered exhaustive, but should be considered an aid in identifying commercial activities. For example, some Federal libraries are primarily recreational in nature and would be deemed commercial activities. However, the National Archives or certain functions within research libraries might not be considered commercial activities. Agency management must use informed judgement on a case-by-case basis in making these decisions.

8

Industrial Shops and Services

Machine, carpentry, electrical, plumbing, painting, and other shops
Industrial gas production and recharging
Equipment and instrument fabrication, repair and calibration
Plumbing, heating, electrical, and air conditioning services,
including repair
Fire protection and prevention services
Custodial and janitorial services
Refuse collection and processing

Maintenance, Overhaul, Repair, and Testing

Aircraft and aircraft components
Ships, boats, and components
Motor vehicles
Combat vehicles
Railway systems
Electronic equipment and systems
Weapons and weapon systems
Medical and dental equipment
Office furniture and equipment
Industrial plant equipment
Photographic equipment
Space systems

Management Support Services

Advertising and public relations services
Financial and payroll services
Debt collection

Manufacturing, Fabrication, Processing, Testing, and Packaging

Ordnance equipment
Clothing and fabric products
Liquid, gaseous, and chemical products
Lumber products
Communications and electronics equipment
Rubber and plastic products
Optical and related products
Sheet metal and foundry products
Machined products
Construction materials
Test and instrumentation equipment

Office and Administrative Services

- Library operations
- Stenographic recording and transcribing
- Word processing/data entry/typing services
- Mail/messenger
- Translation
- Management information systems, products and distribution
- Financial auditing and services
- Compliance auditing
- Court reporting
- Material management
- Supply services

Other Services

- Laundry and dry cleaning
- Mapping and charting
- Architect and engineer services
- Geological surveys
- Cataloging
- Training — academic, technical, vocational, and specialized
- Operation of utility systems (power, gas, water, steam, and sewage)
- Laboratory testing services

Printing and Reproduction

- Facility management and operation
- Printing and binding — where the agency or department is exempted from the provisions of Title 44 of the U.S. Code
- Reproduction, copying, and duplication
- Blueprinting

Real Property

- Design, engineering, construction, modification, repair, and maintenance of buildings and structures; building mechanical and electrical equipment and systems; elevators; escalators; moving walks
- Construction, alteration, repair, and maintenance of roads and other surfaced areas
- Landscaping, drainage, mowing and care of grounds
- Dredging of waterways

Security

- Guard and protective services
- Systems engineering, installation, and maintenance of security systems and individual privacy systems
- Forensic laboratories

Special Studies and Analyses

Cost benefit analyses
Statistical analyses
Scientific data studies
Regulatory studies
Defense, education, energy studies
Legal/litigation studies
Management studies

Systems Engineering, Installation, Operation, Maintenance, and Testing

Communications systems — voice, message, data, radio, wire,
microwave, and satellite
Missile ranges
Satellite tracking and data acquisition
Radar detection and tracking
Television systems — studio and transmission equipment,
distribution systems, receivers, antennas, etc.
Recreational areas
Bulk storage facilities

Transportation

Operation of motor pools
Bus service
Vehicle operation and maintenance
Air, water, and land transportation of people and things
Trucking and hauling

APPENDIX B

Information for this Appendix was obtained
from OMB Circular No. A-76 (Revised), dated
August 4, 1983

I-4

APPENDIX B

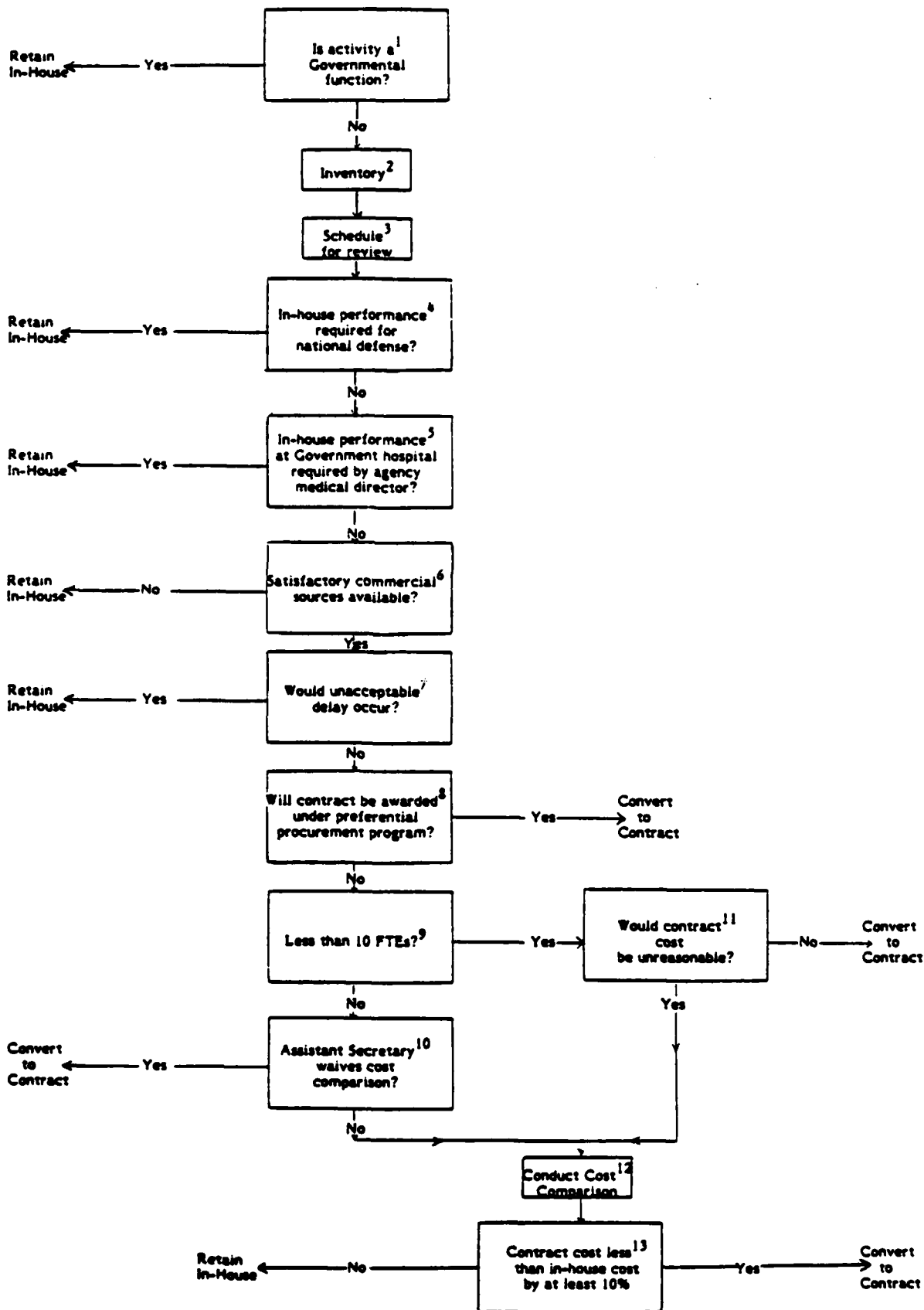
Part I
Chapter 1
Exhibit 1

FLOW CHART REFERENCES
EXISTING GOVERNMENT ACTIVITIES AND EXPANSIONS

Block
No.

- (1) Examine all activities performed by the agency to determine which activities are Governmental functions and must be performed by Government employees.
- (2) Those activities which are not Governmental functions are commercial activities and may be performed by Government employees or by contract. These activities must be inventoried. There are two inventory lists: one for activities of 10 or fewer FTEs and one for activities of more than 10 FTEs.
- (3) Schedule commercial activities on the inventory lists for review. The review, which is performed at least once every five years, determines whether the commercial activity will remain in-house to be performed by Government employees or be contracted out.
- (4) Determine if the activity must be performed by Government employees for national defense purposes. (For Department of Defense only.) If not,
- (5) Determine if it must be performed in-house because the agency's chief medical director determines it is needed to maintain the quality of direct patient care in Government-operated hospitals. If not,
- (6) Determine if performance by Government employees is necessary because there is no satisfactory commercial source to do the work,
- (7) Or an unacceptable delay would occur. If not,
- (8) Determine if function should be contracted, without a cost study, under a mandatory source program or non-competitive preferential procurement program in accordance with applicable regulations. If so, convert to contract. If not,
- (9) Determine if the activity employs 10 or fewer FTEs. If so, go to Step 11 below. If the activity is greater than 10 FTEs, then
- (10) Determine if it is appropriate to waive the requirement for a cost comparison (requires approval of persons designated per paragraph 9.a. of the Circular) and go directly to contract. If assistant secretary waiver is not obtained, go to Step 12 below.
- (11) Determine if meaningful and effective private sector competition will ensure reasonable prices. If so, award a contract. If not,
- (12) Perform a cost comparison of in-house versus contract costs in accordance with Parts II, III, and IV of this Supplement.
- (13) If the total contract costs are less than the total in-house cost estimate by 10 percent of Government personnel costs (differential), then award a contract. If not, the activity remains in-house to be performed by Government employees in accordance with the reorganization plan.

FLOW CHART
IMPLEMENTATION OF OMB CIRCULAR NO. A-76
EXISTING GOVERNMENT ACTIVITIES AND EXPANSIONS



I-6

Part I
Chapter 1
Exhibit 2

FLOW CHART NARRATIVE

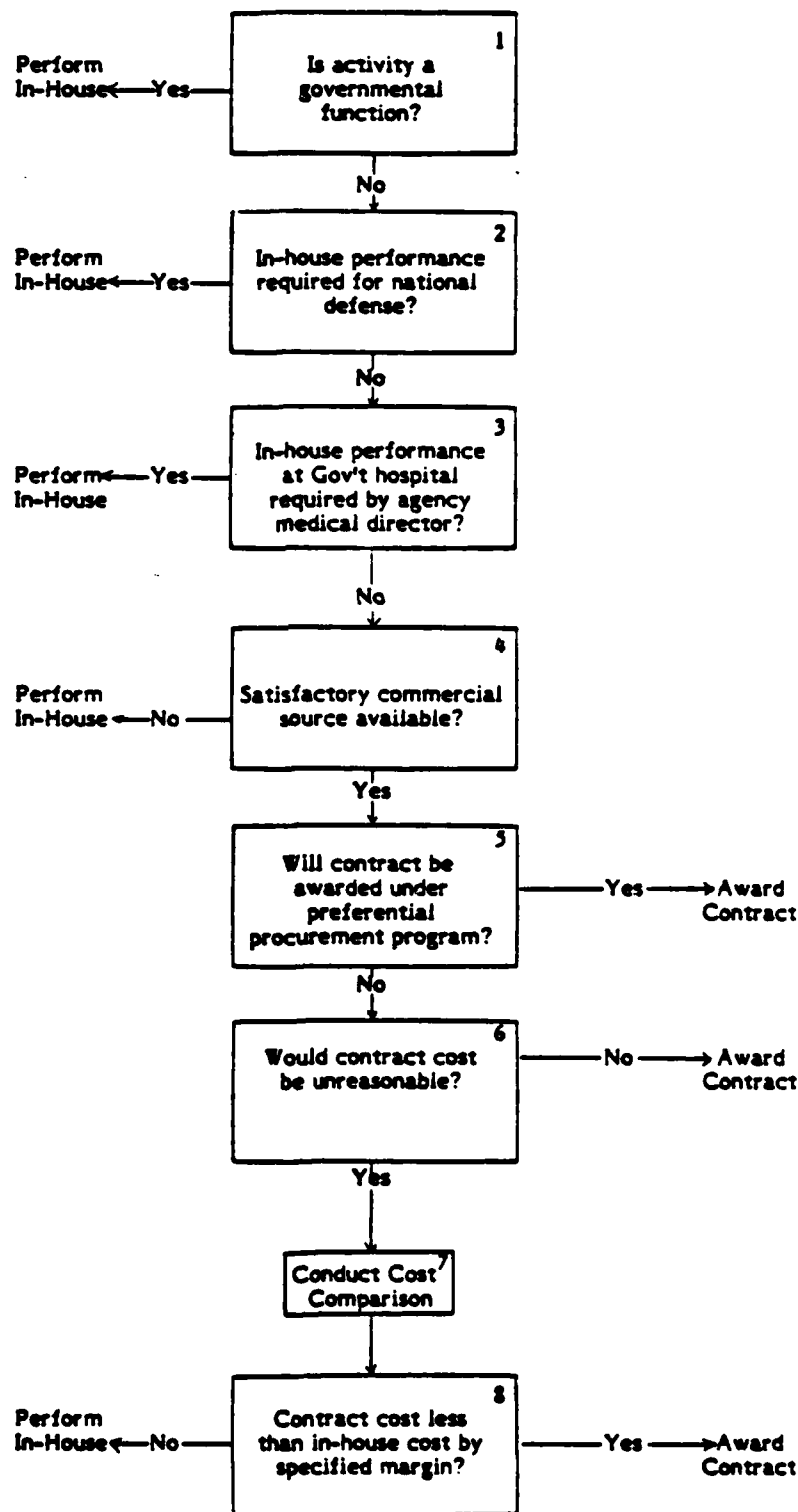
NEW REQUIREMENTS

Block
No.

- (1) Determine if the activity required is a Governmental function and must be performed in-house by Government personnel. If so, the new requirements must be satisfied in-house using Government facilities, equipment and personnel. If the requirement is not a governmental function, then
- (2) Determine if in-house performance by Government personnel is needed for national defense readiness purposes. If yes, the activity must be performed in-house. If not, then
- (3) Determine if in-house performance by Government personnel is needed to ensure the quality of direct patient care in Government-operated hospitals. If yes, the activity must be performed in-house. If not, then
- (4) Determine if satisfactory commercial sources are available to perform the work. If not, the activity must be performed in-house. If sources are available, then
- (5) Determine if a contract will be awarded to an entity under a preferential procurement program. If so, the new requirement may be satisfied by such a contract without a cost comparison. If not,
- (6) Determine if competitive contract costs would be reasonable. If so, award a contract. If not,
- (7) Conduct a cost comparison in accordance with Parts II, III and IV of this Supplement.
- (8) If total contract costs are less than the total in-house cost estimate by 10 percent of personnel-related costs (differential) and 25 percent of the estimated acquisition cost of additional equipment and facilities needed by the Government, then perform the activity by contract. If not, perform the activity in-house using Government personnel, equipment and facilities.

FLOW CHART
IMPLEMENTATION OF OMB CIRCULAR NO. A-76

NEW REQUIREMENT



Part I
Chapter 1
Exhibit 3

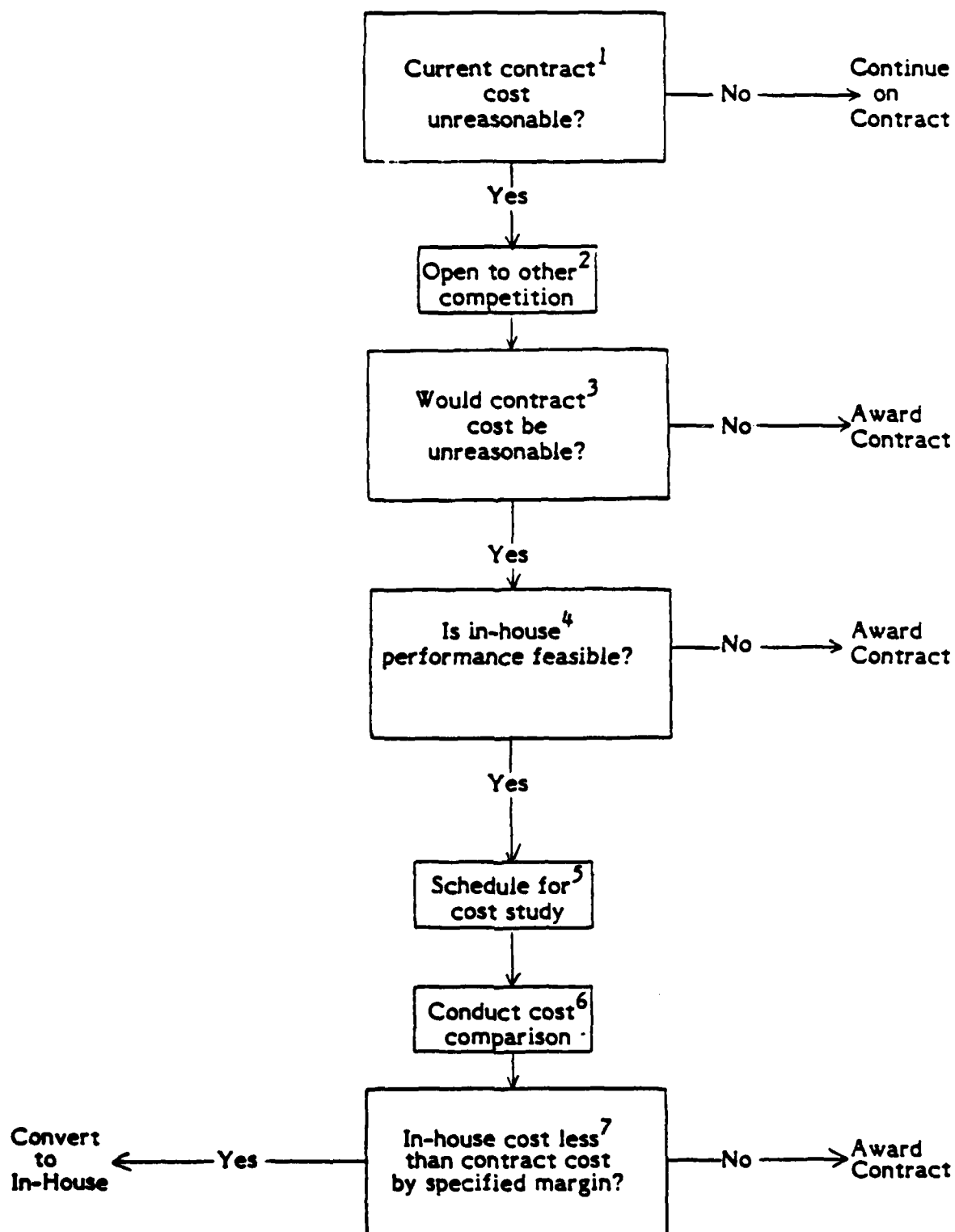
FLOW CHART NARRATIVE
EXISTING CONTRACTS

Block
No.

- (1) Determine if the current contract cost is reasonable and performance is satisfactory. If so, continue under contract. If not or at end of contract period, including options, then
- (2) Open the bid to other commercial competition through the normal procurement process.
- (3) Determine if the contract cost obtained through competitive solicitation for bids and proposals are reasonable. If so, award a contract. If not,
- (4) Determine if in-house performance by Government employees would be feasible if the activity were to be brought in-house. If not, award a contract. If in-house performance is feasible, then
- (5) Schedule the activity for a cost comparison review, and
- (6) Conduct a cost comparison of in-house and contract costs in accordance with Parts II, III, and IV of this Supplement.
- (7) If the total in-house cost estimate is less than total contract costs by 10 percent of personnel-related costs (differential) and 25 percent of the estimated acquisition cost of additional equipment and facilities needed by the Government, then perform the activity in-house using Government personnel and equipment and facilities. If not, award a contract.

FLOW CHART
IMPLEMENTATION OF OMB CIRCULAR NO. A-76

EXISTING CONTRACT



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