THE UNDER SECRETARY OF DEFENSE
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WASHINGTON, DC 20301-3010

ACQUISITION,
TECHNOLOGY
AND LOGISTICS

FEB 24 2004

The Honorable Duncan Hunter
Chairman
Committee on Armed Services
U. S. House of Representatives
Washington, DC 20515-0552

Dear Mr. Chairman:

The Department of Defense (DoD) is pleased to submit the report (see Enclosure) required by section 335 of the National Defense Authorization Act for Fiscal Year 2004 (Public Law 108-136). Section 335 directs the Department to delay implementation of the revised Office of Management and Budget (OMB) Circular A-76, Performance of Commercial Activities, published by OMB on May 29, 2003, until 45 days after the Department provides the report to Congress.

The Department supports OMB's revisions to the circular and, specifically, the enhancement of the public-private competition process. The changes are largely consistent with the report of the Commercial Activities Panel that was submitted to Congress on April 30, 2002, titled "Improving the Sourcing Decisions of the Government." Congress directed the formation of this panel in section 832 of the National Defense Authorization Act for Fiscal Year 2001 (Public Law 106-398). The panel recommended that OMB develop and oversee the implementation of an integrated process for public-private competition that was more in line with the Federal Acquisition Regulation (FAR).

Based on the fact that DoD continues to have the largest Competitive Sourcing Program in the Federal Government, we strongly believe that a measured, phased-in approach is essential for the successful execution of DoD's initial public-private competitions under the revised circular. This is the premise for our Transition Plan, for which OMB has approved a deviation from the revised circular to permit the use of the previous circular to complete the majority of our current competitive sourcing initiatives. The enclosed report addresses the six issues identified in Section 335 of Public Law 108-136 regarding DoD's implementation of the revised circular.

A similar letter has been sent to the President of the Senate, Speaker of the House of Representatives and the chairman and ranking members of the congressional defense committees. If you have further questions regarding matters that we have addressed in this report, please contact the DoD Competitive Sourcing Official, Mr. Raymond F. DuBois, Deputy Under Secretary of Defense (Installations and Environment).

Sincerely,

Michael W. Wynne
Acting

Enclosure:
As stated

cc:
The Honorable Ike Skelton
Ranking Member

DEPARTMENT OF DEFENSE

REPORT TO CONGRESS

DELAYED IMPLEMENTATION OF THE REVISED OFFICE OF MANAGEMENT AND BUDGET CIRCULAR A-76

The Department of Defense submits this report as required by section 335 of the National Defense Authorization Act for Fiscal Year 2004, Public Law No. 108-136.

FEBRUARY 2004

SECTION 335

Section 335 of the National Defense Authorization Act for Fiscal Year 2004, Public Law No. 108-136, directs the Department of Defense (DoD) to delay implementation of the revised Office of Management and Budget (OMB) Circular A-76, Performance of Commercial Activities, published by OMB on May 29, 2003, until 45 days after the Department provides the report to Congress. Section 335 states:

> **SEC. 335. DELAYED IMPLEMENTATION OF REVISED OFFICE OF MANAGEMENT AND BUDGET CIRCULAR A-76 BY DEPARTMENT OF DEFENSE PENDING REPORT.**
>
> (a) LIMITATION PENDING REPORT. No studies or competitions may be conducted under the policies and procedures contained in the revised Office of Management and Budget Circular A-76 dated May 29, 2003 (68 Fed. Reg. 32134), relating to the possible contracting out of commercial activities being performed, as of such date, by employees of the Department of Defense, until the end of the 45-day period beginning on the date on which the Secretary of Defense submits to Congress a report on the effects of the revisions.
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> (b) CONTENT OF REPORT. The report required by subsection (a) shall contain, at a minimum, specific information regarding the following:
>
> (1) The extent to which the revised circular will ensure that employees of the Department of Defense have the opportunity to compete to retain their jobs.
>
> (2) The extent to which the revised circular will provide appeal and protest rights to employees of the Department of Defense.
>
> (3) Identify safeguards in the revised circular to ensure that all public-private competitions are fair, appropriate, and comply with requirements of full and open competition.
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> (4) The plans of the Department to ensure an appropriate phase-in period for the revised circular, as recommended by the Commercial Activities Panel of the Government Accounting Office in its April 2002 report to Congress, including recommendations for any legislative changes that may be required to ensure a smooth and efficient phase-in period.
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> (5) The plans of the Department to provide training to employees of the Department of Defense regarding the revised circular, including how the training will be funded, how employees will be selected to receive the training, and the number of employees likely to receive the training.
>
> (6) The plans of the Department to collect and analyze data on the costs and quality of work contracted out or retained in-house as a result of a sourcing process conducted under the revised circular.

BACKGROUND

The changes made to the revised circular are largely consistent with the report of the Commercial Activities Panel that was submitted to Congress on April 30, 2002, titled "Improving the Sourcing Decisions of the Government." Congress directed the formation of this panel in section 832 of the National Defense Authorization Act for Fiscal Year 2001, Public Law No. 106-398. The panel, chaired by the Comptroller General of the United States, recommended that OMB develop and oversee the implementation of an integrated process for public-private competition that was more consistent with the Federal Acquisition Regulation (FAR). The panel also recommended that ongoing public-private competitions continue under the existing circular and that agencies conduct subsequent competitions under the revised process.

DoD POSITION

DoD supports OMB's revisions to the circular, specifically, the enhancement of the public-private competition process that is more in line with the FAR.

DoD TRANSITION

Based on the fact that DoD continues to have the largest Competitive Sourcing Program in the Federal Government, DoD has placed great importance on developing an appropriate, measured phase-in period. This is the premise for the Department's proposed Transition Plan, which was forwarded to OMB. To support the Transition Plan, OMB approved a deviation from the revised circular permitting the Department to use the previous circular to complete the majority of DoD's competitive sourcing initiatives in progress when the revised circular went into effect on May 29, 2003. (See DoD response to Issue #4 on page 6). The Department strongly believes that a measured approach also is essential for the successful execution of the Department's initial public-private competitions under the revised circular.

DoD RESPONSE

DoD responses to the six congressional issues follow.

CONGRESSIONAL ISSUE #1

The extent to which the revised circular will ensure that employees of the Department of Defense have the opportunity to compete to retain their jobs.

DoD RESPONSE. Under the revised circular, any commercial activity performed by government personnel is subject to a public-private competition before an agency may convert the activity to performance by the private sector. The revised circular does not limit the participation of employees whose jobs are directly affected by a public-private competition[1] in the development of either the agency tender[2] or performance work statement (PWS). To avoid any appearance of a conflict of interest, members of the PWS team (including, but not limited to, advisors and consultants) are not permitted to be members of the team that develops the agency tender. These restrictions are necessary to maintain the integrity of the competitive process. The Department takes special precautions to make the appropriate congressional notifications and public announcements of our public-private competitions in order to identify and notify the civilian employees who will be directly affected by these competitions.

[1] Employees whose jobs are directly affected by a public-private competition are referred to as "directly affected employees."
[2] The agency tender is the government's formal response to a solicitation in a public-private competition performed in accordance with OMB Circular A-76. This response is often informally referred to as the "government's offer."

CONGRESSIONAL ISSUE #2

The extent to which the revised circular will provide appeal and protest rights to employees of the Department of Defense.

DoD RESPONSE. Pursuant to the procedures of FAR 33.103, Protests to the Agency, directly affected employees may contest the agency's conduct of a public-private competition through an individual whom they appoint as their agent. In that respect, OMB has granted a right of review to federal employees that is not available to the employees of offerors in the private sector. The agency tender official (ATO)[3] also may advance the interests of government employees by submitting a contest in his official capacity as the ATO.

The previous circular permitted appeals only after a tentative cost comparison decision, but the revised circular allows employees to submit contests at any point during the competition, on grounds essentially identical to those available to interested parties in conventional procurements. The Department recommended this approach in its comments regarding the draft circular of November 14, 2002. We believe that the provisions of the FAR for consideration of protests to the agency are familiar to contracting officers and other acquisition officials, and will facilitate fair and thorough consideration of contests. Given that public-private competitions are now largely based upon the FAR, we believe that it is especially appropriate to model the process for the administrative resolution of contests on the process in the FAR for review of protests to the agency.

[3] The ATO is the DoD official with decision-making authority who is responsible for the agency tender.

CONGRESSIONAL ISSUE #3

Identify safeguards in the revised circular to ensure that all public-private competitions are fair, appropriate, and comply with requirements of full and open competition.

DoD RESPONSE. We believe that the revised circular establishes a public-private competition process that is significantly fairer and more transparent than the cost comparison process required by the previous circular. Some of these safeguards include the following:

1. The materials that constitute the agency tender will be available only to legal agents of directly interested parties during the course of a contest. Under the previous circular, the agency tender was publicly available upon tentative decision, which was then subject to the administrative appeal process. This arrangement called into question the fairness of any further proceedings to complete the cost comparison. The revision to the circular is designed specifically to preserve the competitive viability of the agency tender.

2. The revised circular (unlike its predecessor) requires that an agency publicly identify specific competition officials for each public-private competition. These competition officials have defined roles in, and are accountable throughout, the competition process.

3. The revised circular establishes "firewalls" to prevent conflicts of interest, or even the appearance of conflicts of interests. Unlike the previous circular, the revised circular provides specific guidelines for these firewalls by not permitting (a) a member of the team that prepares the PWS to participate on the team that develops the agency tender[4]; (b) a member of the team that develops the agency tender to serve on the team that prepares the PWS or the team that evaluates offers and tenders submitted by prospective providers; and (c) a directly affected employee to participate on the team that evaluates offers and tenders submitted by prospective providers.

4. Other critical safeguards include, but are not limited to, the following: (a) a requirement that an agency make a formal public announcement to start and end each public-private competition; (b) a provision allowing the agency tender to exceed performance standards set forth in the solicitation; (c) a one-step process for evaluating the agency tender with private sector offers, including criteria for the conduct of evaluations, exchanges, deficiencies, and cost analyses in these source selections; and (d) a requirement to enter into a binding performance agreement with the service provider selected in a public-private competition regardless of the source (e.g., contractor, DoD).

[4] The agency tender is prepared in accordance with instructions in the solicitation as well as Circular A-76 and includes the government's most efficient organization (MEO), agency cost estimate, etc.

CONGRESSIONAL ISSUE #4

The plans of the Department to ensure an appropriate phase-in period for the revised circular, as recommended by the Commercial Activities Panel of the Government Accounting Office in its April 2002 report to Congress, including recommendations for any legislative changes that may be required to ensure a smooth and efficient phase-in period.

DoD RESPONSE. When OMB issued the revised circular on May 29, 2003, the Department had 216 competitive sourcing initiatives in progress worldwide, affecting over 25,000 government personnel. The following DoD Transition Plan (included in the Department's deviation request to OMB) demonstrates DoD's measured approach.

DEPARTMENT OF DEFENSE COMPETITIVE SOURCING TRANSITION PLAN					
DoD COMPETITIVE SOURCING INITIATIVES	TOTALS	COST COMPARISONS WITH SOLICITATIONS	COST COMPARISONS WITHOUT SOLICITATIONS	STREAMLINED COST COMPARISONS	DIRECT CONVERSIONS
In-Progress on 29 May 2003	216	55	107	1	53
Proposed to OMB to Continue Under Previous Circular	205	55	97	1	52
Proposed to OMB to Transition to the Revised Circular	11	0	10 Transition to Standard Competitions	0	1 Transitions to a Streamlined Competition

Since the OMB deviation provided certain parameters regarding the Department's use of the previous circular, the Department will complete fewer than the 205 initiatives under the previous circular. To implement our measured approach, the Department will closely monitor the remaining 11 in-progress competitive sourcing initiatives that will transition to the revised circular, in addition to a limited number of initial competitions. Our transition plan, coupled with oversight at a high level, is necessary to set a standard for compliance with the revised circular. We believe our cautious and deliberate approach provides for a smooth and efficient transition to the public-private competition procedures in the revised circular. We anticipate a relatively quick learning curve, given our experience in competitive sourcing, and expect to comply with our competitive sourcing plan approved by the Business Initiatives Council and contained in our budget submission for Fiscal Year 2005.

CONGRESSIONAL ISSUE #5

The plans of the Department to provide training to employees of the Department of Defense regarding the revised circular, including how the training will be funded, how employees will be selected to receive the training, and the number of employees likely to receive the training.

DoD RESPONSE. The Department's Competitive Sourcing Office and the Defense Acquisition University are working on several initiatives to improve the Department's Competitive Sourcing Program, including standardized training regarding the public-private competition procedures required by OMB Circular A-76. Specifically, the Air Force has taken the lead to develop standardized training by signing an agreement with the Defense Acquisition University to develop approximately seven different classroom courses related to OMB Circular A-76. Eventually, instructors from Defense Acquisition University will teach the courses at various locations. Other Components are supporting this effort by providing subject matter experts and additional funding. When the courses are institutionalized at Defense Acquisition University, DoD Components will be required to budget for A-76 training just as they include funding in their budgets for any DoD training requirement.

CONGRESSIONAL ISSUE #6

The plans of the Department to collect and analyze data on the costs and quality of work contracted out or retained in-house as a result of a sourcing process conducted under the revised circular.

DoD RESPONSE. The Department has managed the execution of initiatives performed under Circular A-76 (e.g., cost comparisons, direct conversions) via the Commercial Activities Management Information System (CAMIS) since 1979. During Fiscal Year 2001, the Department updated and improved CAMIS by developing and implementing policy for a single, DoD-wide web-based system in lieu of the multi-system approach of the past. The Department's revised CAMIS refines and improves the tracking of execution data for each DoD initiative performed under Circular A-76. The Department uses the resulting CAMIS data to analyze various aspects of the Competitive Sourcing Program, and to respond to inquiries from the Congress, General Accounting Office, OMB, and many other organizations (internal and external to DoD). We identify each DoD initiative performed under Circular A-76 as a separate and unique record in CAMIS, and use an individual execution record to track the competition. These CAMIS records reflect quantifiable data such as key milestone dates (e.g., start date, end date) for each competition; geographic locations; commercial activities included in the competition; number of directly affected government personnel; acquisition-related requirements; performance decision information, such as the selected service provider and rationale for selection; cost data from the cost comparison form; personnel actions impacting the directly affected government personnel; and post-competition actions, such as the results of post-MEO reviews and the actual contract cost. The Department tracks the cost of performance provided by a service provider that is selected in a public-private competition performed under Circular A-76.

As a practical matter, quality is not easily quantifiable. Currently, we cannot effectively gauge quality from the quantitative data that we use to track hundreds of commercial activities in the CAMIS data base. While the Department continues efforts to develop such metrics, we periodically review the quality of performance based on a selected sample of public-private competitions. For example, the Center for Naval Analysis published a report in 2001, concluding that the quality of performance improved or remained the same as a result of public-private competitions.[5]

In addition to these efforts, the Department plans to expand DoD's post-competition procedures in order to add the accountability requirements of the revised circular. We are evaluating procedures to identify best practices and monitor performance, which will be incorporated in DoD's implementing guidance for the revised circular.

[5] CNA Report, Long-Run Costs and Performance Effects of Competitive Sourcing, February 2001 (see DoD Reports on the SHARE A-76! website at http://emissary.acq.osd.mil/inst/share.nsf/).