



Testimony

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OMB CIRCULAR A-76

Oversight and Implementation Issues

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OMB Circular A-76: Oversight and Implementation Issues

Mr. Chairman and Members of the Subcommittee:

I am pleased to be here today to discuss the extent to which the Office of Management and Budget's (OMB) Circular A-76 is being used by executive branch agencies. As you know, A-76 provides the policy guidance and implementation procedures for government agencies to use in deciding whether to contract out for commercial activities—a product or service that could be obtained from a private sector source.

As agreed with the Subcommittee, my statement will cover three major points. First, I will discuss the purpose and usefulness of A-76 in the current federal environment. Second, I will show that A-76 is not being used extensively by civilian agencies and then will discuss the effectiveness of OMB's efforts to lead the implementation of A-76, which, in our view, could be enhanced. Finally, I will provide some observations regarding the necessary elements of a more active A-76 program. My comments today are made on the basis of recent work we have done at the request of the Subcommittee, primarily at OMB and the Departments of Commerce and the Interior, as well as other work we have done on competitive contracting.

The A-76 Process Can Be an Effective Management Tool for Improving Operational Efficiency and Reducing Costs

With the agreement between Congress and the administration to balance the federal budget and the widespread demands by the American people for a less costly government, agencies are being challenged as never before to ensure that their operations are as efficient as possible. Efforts by Congress and the administration are leading or have led to a broader focus on results, significant reductions in the size of the federal workforce, simplified administrative and management procedures, and additional mechanisms to improve efficiency. Within this context, interest has grown over the last several years in using contracting out as one of the central tools available to agencies to reduce costs in a balanced budget environment.

The executive branch's long-standing policy, spanning several administrations, has been that, to the extent it is cost-effective, agencies should rely on the private sector for needed goods and services. The federal government therefore makes extensive use of the private sector to meet federal program goals. This is particularly true for agencies created in the past 2 or 3 decades, such as the Department of Energy, the National Aeronautics and Space Administration, the Environmental Protection Agency, and the Health Care Financing Administration, which typically

have relied from the start on contracting out much of their work rather than performing it directly. Contractors also have almost completely replaced federal employees in some functions, such as cleaning services, travel management, and most recently personnel security investigations. As an indication of the degree to which the federal government uses the private sector, total civilian personnel costs for fiscal year 1997 were about \$113 billion, as compared with about \$110 billion that federal agencies spent on commercial service contracts.

The issue of whether to contract out federal functions has always been challenging. In an effort to help agencies make better decisions in this regard, OMB issued Circular A-76 in 1966 and updated it several times, most recently in 1983. A-76 provides federal policy for the government's performance of commercial activities. OMB issued a supplemental handbook to the circular in 1979 that included detailed procedures for competitively determining whether commercial activities should be performed in-house; by another federal agency, through an interservice support agreement; or by the private sector. OMB updated this handbook in 1983 and again in March 1996. This latest revision was intended to streamline the cost comparison process and reduce the A-76 administrative burden and thereby ease the use of A-76 within the executive branch.

According to OMB, the purpose of A-76 is not to convert work to or from in-house, contract, or interservice support agreement performance. Thus, a senior OMB official stressed, OMB does not view its role as requiring agencies to undertake A-76 cost comparisons. Rather, OMB encourages agencies to understand and use A-76 as one of a series of tools federal managers can employ to make sound business decisions and to enhance federal performance through competition and choice.

Circular A-76 and its supplemental guidance require agencies to evaluate their activities to determine whether they are governmental or commercial and complete an inventory of all commercial activities. A-76 requires, in certain circumstances, that agencies conduct cost comparisons to determine the most efficient means to carry out commercial activities. Under A-76, agencies are to use a three-step process to determine whether recurring commercial activities will be performed in-house or by contractors. The process consists of (1) developing a performance work statement that defines the technical, functional, and performance characteristics of the work to be performed; (2) conducting a management study to determine organizational structure, staffing, and operating

procedures for the most efficient and effective in-house performance of the commercial activity, referred to as the Most Efficient Organization or MEO; and (3) accepting formal bids and conducting a cost comparison between the private sector and the government's Most Efficient Organization in order to make a decision on whether an activity will be performed by the government or the private sector.

Agencies' experiences with A-76 suggest that competition is a key to realizing savings, whether functions are eventually performed by private sector sources or remain in-house.¹ We have found that savings achieved through the A-76 competitive process were largely personnel savings, the result of closely examining the work to be done and reengineering the activities in order to perform them with fewer personnel, whether in-house or by contractor.² OMB has reported that savings from reviewing an agency's operations and making changes to implement the Most Efficient Organization have averaged 20 percent from original costs. We have noted in past work that such reported savings must be viewed with caution because statements about savings have often been heavily premised on initial estimates that were not later updated to reflect actual amounts. However, there appears to be a clear consensus, which we share, that savings are possible when agencies undertake a disciplined approach, such as that called for under A-76, to review their operations and implement the changes to become more efficient themselves or contract with the private sector for services. In fact, in DOD's case, about half of the competitions were won by federal employees.

Stronger OMB Leadership Is Needed to Invigorate Civilian Agencies' A-76 Programs

Although the evidence suggests that the A-76 process provides the opportunity to achieve savings, A-76 does not appear to be a high priority within OMB or civilian agencies, and as a result, little effort is under way to use the A-76 process. There has been minimal A-76 activity among many agencies since the late 1980s, with some major civilian agencies, such as the Departments of Education, Housing and Urban Development, and Justice, reporting that they have not studied any positions under A-76 in the past 11 years. Moreover, despite OMB's intention that the March 1996

¹Base Operations: Challenges Confronting DOD as It Renews Emphasis on Outsourcing (GAO/NSIAD-97-86, Mar. 11, 1997); and Privatization: Lessons Learned by State and Local Governments (GAO/GGD-97-48, Mar. 14, 1997).

²Outsourcing DOD Logistics: Savings Achievable But Defense Science Board's Projections Are Overstated (GAO/NSIAD-98-48, Dec. 8, 1997); Base Operations: Challenges Confronting DOD as It Renews Emphasis on Outsourcing (GAO/NSIAD-97-86, Mar. 11, 1997); and Defense Outsourcing: Challenges Facing DOD as It Attempts to Save Billions in Infrastructure Costs (GAO/T-NSIAD-97-110, Mar. 12, 1997).

revision to the A-76 Supplemental Handbook would make A-76 a more attractive vehicle for agencies to use, no significant increase in efforts under A-76 among civilian agencies are readily evident. As shown in table 1, for fiscal year 1997, DOD was the only federal agency that reported to OMB that it had completed any A-76 studies of federal positions.³

**Table 1: Reported Number of FTEs
Staff Years Studied Under A-76 During
Each of the the Past 10 Years**

Fiscal year	Total FTEs	DOD FTEs	Civilian agencies FTEs
1988	17,249	12,000	5,249
1989	8,469	6,100	2,369
1990	9,547	6,989	2,558
1991	2,026	1,243	783
1992	564	496	68
1993	509	441	68
1994	1,691	1,623	68
1995	2,386	2,128	258
1996	5,267	5,241	26
1997	25,255	25,255	0

Note: As reported by OMB, civilian agencies data for 1992-1995 are based on annual averages for that time period. Not all agencies are included, but OMB stated that the number excluded is insignificant. We did not independently verify the accuracy of the data provided by OMB.

Source: OMB

For the future, DOD projected that it can save about \$6 billion by 2003 and \$2.5 billion each year thereafter by subjecting more of its business and support activities to competition using the A-76 process. Currently, DOD plans to subject over 220,000 positions to the A-76 process. DOD has not fully achieved estimated savings in the past, and we question DOD's ability to achieve all estimated savings in the future. However, if DOD is able to complete its ambitious A-76 plans, significant savings are likely.

To gain more perspective on A-76 activity within civilian agencies, we examined the program's use at the Departments of Commerce and the Interior. Both departments had A-76 efforts in the 1980s. For example, between 1986 and 1990, Commerce estimated that it saved \$8.6 million through these efforts. Interior reported estimated savings of about \$1.9 million during that period through its A-76 efforts. However, since

³In fiscal year 1997, the Department of the Interior completed one A-76 cost comparison regarding the an aircraft purchase that did not involve any full time equivalents (FTE). According to OMB guidance, a FTE or work year generally includes 260 compensable days or 2,080 hours. These hours include straight-time hours only and exclude overtime and holiday hours.

then, A-76 efforts at Commerce and Interior have dwindled along with those at other federal agencies.

The Department of Commerce has not done a complete update of its inventory of commercial activities since 1983 and recently completed what had been its only ongoing study. That study covered the operation and support of a National Oceanic and Atmospheric Administration (NOAA) ship. NOAA officials told us that the study was done because of pressure from Congress, OMB, and the Department's Inspector General to explore alternatives to an agency-designed, -owned, and -operated fleet for acquiring marine data. However, the study did not result in any commercial offers in response to NOAA's solicitation. In addition, the study took almost 19 months and required nearly 10 staff years to complete. It would have required even more resources if NOAA had received offers to perform the work.

The Department of the Interior has a current inventory which it updates periodically, and has identified over 5,000 FTES as devoted to commercial activities. These activities include such functions as administrative support services and automated data processing-related services. The Department reports that although it has not conducted many formal A-76 studies in recent years, it has undertaken a number of A-76 cost comparisons of its aircraft services, including examinations of aircraft maintenance and decisions on whether to lease or purchase aircraft. However, most of these studies did not involve any federal positions, and therefore are not reflected in OMB's governmentwide data on FTES studied.

Officials at the Departments of Commerce and the Interior provided similar explanations for the limited effort under A-76. They said that they perceived that the priorities in management reform initiatives had changed and that greater emphasis was being given to implementation of more fundamental, mission-based initiatives arising from the National Partnership for Reinventing Government, formerly known as the National Performance Review (NPR) and the Government Performance and Results Act (the Results Act), among others. According to the officials, these shifting management priorities, along with the significant time and money needed to do the studies under A-76 and the need for sufficient staff with the necessary technical skills, have all contributed to reduce A-76 efforts.

**OMB Leadership on A-76
Issues Has Been Limited**

As I noted, OMB's March 1996 revision of the A-76 Supplemental Handbook was intended to ease the administrative burden on agencies in doing A-76

studies. This supplement was issued subsequent to the expiration of several legislative provisions that temporarily limited agencies' A-76 efforts, particularly those of DOD. OMB's revision of the supplement had the potential to re-focus attention on A-76. However, since issuing the revision, OMB has not consistently worked with agencies to ensure that the provisions of A-76 are being effectively implemented. For example, OMB made only limited efforts to gather and use the commercial activities inventories that agencies are to develop under A-76. In June 1996, OMB requested that agencies submit not later than September 13, 1996, a summary of their updated inventory of commercial activities as required by A-76. According to OMB, it did not receive inventories from all agencies, and of those that it did receive, many were based largely on previous inventory efforts. In June 1997, after not receiving responses from several agencies, OMB followed up with another request for the commercial inventory information. Several months later, in April 1998, we found that 6 of the 24 largest agencies still had not complied with OMB's initial and follow-up requests to provide updated commercial activities inventories.

OMB also has not systematically reviewed the inventories of commercial activities that it did receive to determine whether agencies are missing opportunities to generate savings. OMB generally has not attempted to determine whether agencies have inappropriately omitted some commercial activities. OMB also does not compare commercial activities among agencies to identify inconsistent application of A-76 guidance across the federal government. As a result, some agencies may not be identifying commercial activities that are similar to those included in other agencies' commercial activities inventories, thereby missing opportunities to use the A-76 process to achieve cost savings.

Lastly, and most importantly, it is not clear how consistently OMB has raised questions about agencies' implementation of A-76 during the budget process. OMB officials told us that the primary mechanism for monitoring agencies' A-76 efforts is through the budget review process.⁴ They pointed to guidance requiring agencies to incorporate A-76 considerations into their budget submissions. However, we found that OMB's guidance to agencies was very limited. For example, the over 300-page OMB Circular A-11, which governs the preparation of agencies' budget requests to OMB, appears to contain only three paragraphs that directly concern A-76, and

⁴In 1994, OMB reorganized to integrate its budget analysis, management review, and policy development roles, in an initiative called "OMB 2000." This reorganization was the most recent of a series of attempts to bolster OMB's management capacity and influence. See *Government Management: Observations on OMB's Management Leadership Efforts* (GAO/T-GGD/AIMD-98-148, May 12, 1998).

these paragraphs instruct agencies that their savings estimates should reflect the probable results generated by cost comparisons or conversions.

OMB officials stated that they rely primarily on program examiners in the OMB Resource Management Offices (RMO) to review agencies' A-76 efforts in conjunction with the budget review and approval process. In 1996, the OMB Deputy Director for Management asked the RMOs to examine competition initiatives, such as A-76, as part of their continuing program management and budget reviews. The Deputy Director highlighted agencies' strategic plans and streamlining plans as being especially appropriate vehicles for examining agencies' efforts to compete their support service requirements. However, since then, OMB has not provided its program examiners with more recent written requirements or guidance on the need to review agencies' A-76 efforts. OMB officials said that, despite the lack of current guidance, some review has been done on an ad hoc basis in conjunction with budget reviews. According to these officials, examiners were given copies of agencies' commercial activities inventories where they existed and were instructed to keep in mind all reinvention efforts, including A-76, as they reviewed agency budget requests. However, given the absence of inventory information for several of the largest federal agencies and the absence of ongoing studies in virtually all agencies other than DOD, the effect of examiners' efforts, if any, is questionable.

Recent OMB Plans, If Implemented, Appear Promising

OMB has very recently indicated that it intends to devote more attention to the implementation of A-76. In a May 12, 1998, memorandum to the heads of executive departments and agencies, the Director of OMB asked agencies to submit updated lists of commercial activities by October 31, 1998. The Director said that OMB plans to share these lists with the President's Management Council.⁵ The Director said that OMB also plans to examine agencies' lists to seek consistency in inventories across agencies. The memorandum said OMB will seek to complete this effort by November 30, 1998, and that final lists of inventories will be made available for congressional and public review by January 1999. An OMB official said DOD's A-76 efforts over the last several years could provide a rich body of experience from which to build effective A-76 programs in civilian agencies. The official also noted that because commercial activities inventories can provide detailed information about an agency's structure

⁵The President's Management Council (PMC) was established in 1993 to advise and assist the President and the Vice President in improving overall executive branch management, coordinating management improvement-related efforts, and ensuring adoption of management practices in executive branch agencies. Agencies generally are represented on the PMC by their Deputy Secretary or equivalent.

and functions, these inventories can be valuable not only for A-76 purposes, but also for identifying other reinvention opportunities.

This plan for renewed OMB commitment, if effectively implemented, is an important and noteworthy development that could lay the groundwork for a reinvigorated A-76 program. Given OMB's past experience with requesting and using inventories of commercial activities from agencies, it is clear that sustained OMB commitment and follow-through will be vital to the success of the effort. We plan to continue to monitor OMB's and the agencies' efforts in this area.

Observations Concerning the Needed Elements for a More Active A-76 Program

Over the last couple of years, there has been interest in Congress in establishing a statutory basis for A-76 and for making other changes intended to expand the degree to which agencies compete their commercial activities. We have been pleased that Congress has turned to us for assistance as it has considered various legislative proposals.⁶ Irrespective of any decisions that Congress may make about the A-76 program, our work suggests that several elements are needed for a successful A-76 effort across federal agencies. Today, I will highlight four elements that I believe merit special attention.

Leadership Commitment to Use A-76

The sustained commitment of agency and administration leadership is a necessary element to ensure the success of any management improvement effort, including A-76. As the current level of activity suggests, consistent and forceful leadership from OMB may be needed to create incentives for agencies' managers to subject themselves to the rigors of the A-76 process. By comparison with the rest of the federal government, DOD has maintained much larger levels of activity because it has incentives to generate savings through A-76 to fund its modernization efforts.

Integration of A-76 Within a Performance-Based Approach to Management and Accountability

In recent years, Congress has put in place a statutory framework—with the Results Act as its centerpiece—for performance based management and accountability. Under the Results Act, each executive branch agency is to issue strategic plans that, among other things, lay out the long-term

⁶Competitive Contracting: Information Related to the Redrafts of the Freedom From Government Competition Act ([GAO/GGD/NSIAD-98-167R](#), Apr. 27, 1998); Privatization and Competition: Comments on H.R. 716, the Freedom From Government Competition Act ([GAO/T-GGD-97-185](#), Sep. 29, 1997); Privatization and Competition: Comments on S. 314, the Freedom From Government Competition Act ([GAO/T-GGD-97-134](#), June 18, 1997); and Federal Contracting: Comments on S. 1724, the Freedom From Government Competition Act ([GAO/T-GGD-96-169](#), Sept. 19, 1996).

goals the agency will pursue and the strategies the agency will use to achieve those goals. The first of these strategic plans were provided to Congress last fall. Each agency is then to develop annual performance plans that identify the agency's annual goals and strategies and the resources that will be used to achieve those yearly goals. The first of these plans, to cover fiscal year 1999, were submitted to Congress this spring.

An agency's efforts on its annual performance plans provides the opportunity to consider A-76 within the broader context of what the agency is trying to achieve and how best to achieve it. At the request of congressional leaders and to assist Congress in using annual performance plans for making decisions, we issued a guide in February 1998 for Congress to use in assessing annual performance plans.⁷ In that guide, we noted that Congress could examine the plans from the standpoint of whether they show evidence that various approaches, such as establishing partnerships with other organizations and contracting, were considered in determining how best to deliver products and services. More directly, the annual performance plans can provide a ready-made, annual vehicle for Congress to use to inquire about agencies' efforts to ensure that the most cost-effective strategies are in place to achieve agencies' goals. As part of this inquiry, Congress can ask agencies about the tools the agencies are using to increase effectiveness, including the status of A-76 programs, and the specific choices the agencies have made about whether to keep a commercial activity in-house or contract it out.

Improved Cost Data

The government's lack of complete cost data, particularly for indirect costs, has increased the difficulty of carrying out the A-76 competitive process, because the government is not able to accurately determine the cost of the function or activity it plans to compete. The cost data needed to develop indirect costs or standard cost factors that represent these costs, such as overhead rates, are not readily available. In our audit of the consolidated financial statements of the U.S. government for fiscal year 1997, we noted significant financial management deficiencies.⁸ We found that financial systems weaknesses; problems with fundamental recordkeeping; incomplete documentation; and weak internal controls, including computer controls; prevent the government from accurately reporting a large portion of its assets, liabilities, and costs. These

⁷Agencies' Annual Plans Under the Results Act: An Assessment Guide to Facilitate Congressional Decisionmaking (GAO/GGD/AIMD-10.1.18, Version 1, Feb. 1998).

⁸Audit of the Consolidated Financial Statements of the U.S. Government for Fiscal Year 1997 (GAO/AIMD-98-127, Mar. 31, 1998).

deficiencies affect the government's ability to accurately measure the full cost and financial performance of programs and to efficiently manage its operations. For example, in January 1998, we reported that DOD has no reliable means of accumulating actual cost data to account for and manage resources.⁹ Moreover, in a February 1998 report, we noted that it will likely be many years before DOD is capable of providing accurate and reliable cost data.¹⁰

Efforts are under way to improve government cost data and supporting systems, but for some agencies it could be several years before significant improvements are made. Continuing efforts to implement the Chief Financial Officers Act are central to ensuring that agencies resolve their long-standing problems in generating vital information for decisionmakers. In that regard, the Federal Accounting Standards Advisory Board (FASAB) has developed a new set of accounting concepts and standards that underpin OMB's guidance to agencies on the form and content of their agencywide financial statements.¹¹ As part of that effort, FASAB developed managerial cost accounting standards. These managerial cost accounting concepts and standards require that federal agencies provide reliable and timely information on the full cost of federal programs and on their activities and outputs. Specifically identified in the standards is the need for information to help guide decisions involving economic choices, such as whether to do a project in-house or contract it out. Such information would allow agencies to develop appropriate overhead rates for specific operations. These cost accounting standards became effective for fiscal year 1998. Some agencies' Chief Financial Officers have expressed concern about their agencies' ability to comply with the cost accounting standards this year.

Contract Management and Oversight

An effective contracting effort requires considerable contract management capability. An agency must have adequate capacity and expertise to successfully carry out the solicitation process and effectively administer and monitor contracts once they are awarded. We noted in our report on privatization lessons from state and local governments that, when a government's direct role in the delivery of services is reduced through

⁹Federal Management Issues ([GAO/OCG-98-1R](#), Jan. 9, 1998).

¹⁰Defense Outsourcing: Better Data Needed to Support Overhead Rates for A-76 Studies ([GAO/NSIAD-98-62](#), Feb. 27, 1998).

¹¹FASAB was created in October 1990 by the Secretary of the Treasury, the Director of OMB, and the Comptroller General to consider and recommend accounting principles for the federal government. If accepted by Treasury, OMB, and GAO, the standards are adopted and issued by OMB and GAO.

privatization, the need for aggressive monitoring and oversight grows.¹² Oversight was needed not only to evaluate compliance with the terms of the privatization agreement, but also to evaluate performance in delivering goods and services to help ensure that the government's interests were fully protected. Officials from most state and local governments said that the monitoring of contractor performance was the weakest link in their privatization processes.

Oversight and monitoring have been consistent weaknesses in federal efforts as well. In numerous past reports on governmentwide contract management, we have identified major problem areas, such as ineffective contract administration, insufficient oversight of contract auditing, and lack of high-level management attention to and accountability for contract management. For example, long-standing contractor oversight problems at several agencies, including DOD, the Department of Energy, and the National Aeronautics and Space Administration have, in our view, put these agencies at high risk for waste, fraud, abuse, and mismanagement.¹³ Although each of these agencies have taken actions to improve their contractor oversight and monitoring functions, these remain high-risk areas that we continue to monitor closely.

In summary, Mr. Chairman, A-76 has shown itself to be an effective management tool in increasing the efficiency of the federal government and saving scarce funds. However, despite its proven track record, A-76 is seldom used in civilian agencies. OMB has not consistently sent strong messages to the agencies that A-76 is a priority management initiative. While OMB's May 12, 1998, memorandum is an encouraging first step, thorough implementation and follow-through will be needed to get A-76 on track. In addition, agencies will need to continue their efforts to ensure both that they have the sound program cost data needed to make comparisons and that mechanisms are in place to monitor and oversee contracts. Finally, we believe that agencies' development and Congress' use of annual performance plans under the Results Act provide an opportunity to consider A-76 and other competition issues within the context of the most efficient means to achieve agency goals.

Mr. Chairman, this concludes my prepared statement. I would be pleased to respond to any questions you or other Members of the Subcommittee may have.

¹²Privatization: Lessons Learned by State and Local Governments ([GAO/GGD-97-48](#), Mar. 14, 1997).

¹³High-Risk Series: An Overview ([GAO/HR-97-1](#), Feb. 1997).

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