CONTRACTING-OUT: A CASE FOR REALISTIC CONTRACT VS. IN-HOUSE DECISION-MAKING

A THESIS

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The opinions and conclusions expressed herein are those of the individual student author and do not necessarily represent the views of either the Judge Advocate General's School, U.S. Army, or any other governmental agency. References to this study should include the foregoing statement.

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SCOPE

An analysis of the legal and practical limits of the Government's policy in favor of contracting-out to private industry for goods and services, with special emphasis on contracting-out for support services.

TABLE OF CONTENTS

I. INTRODUCTION

The Government of the United States currently spends an estimated $20 billion annually for support services.[1] Support services are those operations ancillary to the function of a Government agency which do not involve a product and can be performed either by "in-house" personnel (active duty military and civil service employees) or by civilian personnel furnished by private contractors.[2] Expenditures by all Government agencies for support services obtained by contract approach $8 1/4 billion annually, $7 3/4 billion of which are accounted for by the Department of Defense.[3]

Contracting-out, as the Government practice of obtaining goods and services from private industry has often been labeled, is based primarily on a permissive policy declaration by the President to the effect that the Government will rely primarily upon the private enterprise system to supply its needs.[4]

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1. Hearings on A Cost Profile For Support Services Before a Subcomm. of the House Comm. on Government Operations, 90th Cong., 2d Sess. 1 (1968) [hereinafter cited as 1968 Hearings]

2. H. R. Rep. No. 1850, 90th Cong., 2d Sess. 1 (1968).

3. 1968 Hearings. 2.

4. Bureau of the Budget, Circ. No. A-76, Policies for acquiring commercial or industrial products and services for Government use, para. 2 (Revised 1967) [hereinafter cited as Circ. A-76 (Revised)].

Restrictive of this espoused policy in favor of the private-enterprise system in the area of support services, and often in conflict with it, are administrative interpretations by the General Accounting Office and Civil Service Commission of various contracting-out activities. Decision-making organs of these agencies have interpreted existing federal personnel statutes to mean that certain services-- "personal services" -- may be performed only by Government employees and have often struck down contracts for such services as having effectively violated those laws.[5]

Intermeshed between the initial policy in favor of contracting-out and decisions by the Comptroller General and the General Counsel of the Civil Service Commission restricting that policy is the current requirement for a cost analysis of in-house vs. contracted-out alternatives.[6]

Frequent conflicts between the policy, administrative decisions and cost analysis procedures have created a number of problems, not the least of which is the difficulty operational-level personnel have performing their mission under existing regulations. Such personnel are faced with "real time" mission performance requirements and are often presented with decision-making sit-

5. See note 126 infra, and accompanying text.

6. Circ. No. A-76 (Revised), supra note 4, at para. 6.

uations in which the relative procedural ease of contracting-out forces them to do so in obvious disregard of interpretive and regulatory restrictions. In addition, the policy decision whether or not to contract-out or to develop in-house capabilities is forced upon the contracting officer, a person whose resources may possibly not permit him to make a sound decision.

It shall be the purpose of this study to analyze the apparent conflict between policy and practice in the area of contracting-out in general, with special emphasis on contracting-out for support services, to determine:

1. Whether there still exists, in fact, a policy in favor of contracting-out to private industry and, if so, what the legal and practical limits of that policy are; and

2. What corrective action, if any, is necessary, either under existing law or in the form of additional legislation: to resolve the problem of ambiguity and lack of definitive guidance in this area of policy vs. practice; and to permit realistic "contract vs. in-house" decision-making, either at the operational or higher level.

II. DEVELOPMENT OF THE POLICY

A. General

Since the early 1950's, the Government has initiated and

pursued a policy which encourages the use of private enterprise to satisfy government requirements for goods and services. The policy, as first expressed, was grounded primarily on Executive concern about Government competition with private enterprise.[7] Congressional support for the policy has been manifested by numerous committee hearings in both houses and various proposals of legislation.[8] Also, the various Government agencies, including the important Department of Defense, have expressed their interpretive affirmance of the policy since its inception.[9]

An examination of the development of the policy will show that it exists now in much weaker form, having fallen victim to considerations of cost and those forces who desire to perpetuate Government

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7. See note 11, infra, and accompanying text.

8. Staff of Senate Comm. on Government Operations, 88th Cong., 1st Sess., Committee Print on Government Competition With Private Enterprise 14, 19 (1963) [hereinafter cited as 1963 Committee Print]. Congressional committees have studied numerous aspects of the problem of Government competition with private enterprise in various hearings begun in an extensive study in 1932 by a Special Committee of the House of Representatives, and have not since abated. During the referenced period, investigations were made by the Senate and House Appropriations Committees, the House Armed Services Committee, the Senate and House Committees on Government Operations, and the Senate Select Committee on Small Business. Id., 14-24.

9. Dep't. of Defense Directive No. 4100.15, Commercial or Industrial Activities sec. IV (1966).

in business.[10]

B. The Bureau of the Budget

The public first became aware of the Government's pro-private enterprise policy in 1954 when, in his first budget message to Congress after taking office, President Eisenhower stated: "This budget marks the beginning of a movement to shift to . . . private enterprise Federal activities which can be more appropriately and more efficiently carried on that way."[11] Several months later, in an appearance before the House Committee on Government Operations Percival F. Brundage, Deputy Director of the Bureau of the Budget, indicated in his testimony that the program to give preference to private enterprise would be coordinated on a government-wide basis.[12]

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10. Despite the evident weakening of the initial policy, there have been continued protestations that it was not changing. For example, subsequent to a Department of Defense decision in 1965 to convert some 10,500 contract technical service positions to civil service, the Hon. Paul R. Ignatius, Assistant Secretary of Defense (Installations and Logistics) spoke at the Annual Meeting of the National Aerospace Services Association on 2 May 1967, stating: ". . . it seems hardly necessary to emphasize that neither the Defense Department nor the Government as a whole has abandoned the general policy of obtaining the products and services we need from commercial sources to the maximum extent consistent with effective and efficient accomplishment of our programs."

11. 100 Cong. Rec. 567 (1954).

12. 1963 Committee Print, supra note 8, at 24.

Then, in January, 1955, the Bureau of the Budget published the first in a series of bulletins and circulars dealing with the subject of contracting-out to private industry. It should be noted that the first of these bulletins and those immediately following, both in policy statements and in delineation of implementing procedures, described a very broad, nearly all-inclusive purpose to give up many long-established Government-based activities into the hands of civilian contractors.[13] Thus, in this first official publication of the Government concerning the policy, B.O.B. Bulletin No. 55-4 stated under the heading "Policy :"

> It is the general policy of the administration that the Federal Government will not start or carry on any commercial activity to provide a service or product for its own use if such product or service can be produced from private enterprise through ordinary business channels. Exceptions to this policy shall be made by the head of an agency 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. 14

In order to implement the pronounced policy, each agency

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13. This, we shall see, furnished the basis for the continuing attack, especially in the last five years, against this policy, and perhaps gave added character and strength to "legal" arguments of dissenters from the theory and practice of the policy.

14. Bureau of the Budget, Bull. No. 55-4, Commercial-Industrial activities of the Government providing products or services for governmental use, para. 2 (1955) [hereinafter cited as Bull. No. 55-4].

head was required to inventory and evaluate all commercial-industrial type activities performed by his agency which fell within the scope of the bulletin. The purpose of the evaluation was to determine whether such activities should be continued by the Government in light of the change in policy. It was to be conducted in several phases, the first to cover manufacturing activities and the second to examine services.[15]

Interestingly, the relative cost of in-house vs. contracted-out activities was de-emphasized in early directives. Cost was only one factor to be considered in the using agency's evaluation and not the primary concern with regard to the final decision. B.O.B. Bulletin No. 55-4 provided, in its explanation of the required agency evaluation: "The relative costs of Government operation compared to purchase from private sources will be a factor in the determination in those cases where the agency head concludes that the product or services cannot be purchased on a competitive basis and cannot be obtained at reasonable prices from private industry. In those cases it will be necessary to develop detailed data on such costs."[16] In emphasizing that decisions should not rest on cost alone, the first bulletin stated:

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15. Id. para. 4.

16. Id. para. 6.

> Since cost should not usually be the deciding factor in determining whether to continue the operation as a direct Government operation, this statement should show both the results of the comparative cost analysis and the elements which have been used in determining the Government cost, both as a direct operation and if the product is secured from private industry. 17 (emphasis added)

Guidance as to the specific methods of cost analysis was lacking.

Each agency head was told simply that:

> . . . the costs of Government operation should be fairly computed and complete, covering both direct and indirect costs, including elements not usually chargeable to current appropriations such as depreciation, interest on the Government's investment, the cost of self-insurance (even though it is unfunded); there shall also be added an allowance for Federal State and local taxes to the extent necessary to put the costs on a comparable basis. Care must also be exercised to see that costs of procuring material /later directives included services /from private sources are fairly computed and complete, being truly representative of the lowest price the Government would pay for the quantity and

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17. Id. Attachment B. para. 26. In a memorandum to the President in October, 1956, the Bureau of the Budget discussed the progress of the administration's program concerning the elimination of Government from competition with private enterprise, and stated that the reasons for adopting the policy that "cost should not usually be the deciding factor" were:

> 1. The cost of Government operations are not comparable with corresponding business costs. The Government, for example pays no income taxes and operates its own tax-free facilities, thereby keeping costs down.
> 2. Government accounts are not kept in the same manner as business accounts, so that a comparison of the operating costs of Government versus business, for example, is not only difficult but often misleading.
> 3. Above all, the decision whether to continue or discontinue a Government activity solely on an apparent cost basis runs

quality needed, and taking account of any applicable indirect costs of the Government for such procurement. 18

As if to emphasize the strength and backing of this new policy, the bulletin required each evaluation to include review of legal authorization for each government commercial and industrial activity to determine whether new legislation was necessary to permit the agency to continue the activity. If new legislation were necessary, the agency was required to draft it and submit it promptly. Absent the need for additional legislation, the agency was required to discontinue the activity within a reasonable time. 19

Initial successes under the first B.O.B. Bulletin were measured in terms of numbers of Government activities terminated or converted to civilian contract; support services were scarcely mentioned. In a press release accompanying the May 15, 1956 publication by the Bureau of the Budget entitled "Inventory of Certain Commercial-Industrial Activities of the Government," the initial inventory evaluation required by B.O.B. Bulletin 55-4, it was stated that the inventory report:

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17. (Cont.)
counter to our concept that the Government has ordinarily no right to compete in a private enterprise economy (emphasis added) 1963 Committee Print, supra note 8, at 28.

18 Bull. No. 55-4, supra note 14, at para. 6.

19. Id.

> . . . is another step in the administration's long-term program to eliminate unnecessary Government competition with our free enterprise system. . .; that since its inauguration the program has prevented the starting of additional commercial-industrial activities. 20.

Listed among the "accomplishments" of the program was the termination of 32 types of commercial-industrial activities within the Department of Defense at 246 installations.[21] A subsequent memorandum from the Bureau of the Budget to the President in October, 1956, listed the discontinuance or curtailment of 492 Federal commercial-type activities which could be handled competitively by private business.[22]

B. O. B. Bulletin 57-7 was published in February, 1957, giving further instructions concerning the evaluation of commercial activities classified as services, the termination of commercial activities, and the starting of new commercial activities. This second bulletin expressed a policy identical to that of its predecessor. Evidence of the future struggle over relative costs may be detected, however, by the absence of the previous bulletin's provision that ". . . cost should not usually be the deciding factor in determining whether to continue the operation as a direct Govern-

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20. 1963 Committee Print, supra note 8, at 26.

21. Id.

22. Id. 2.

ment operation. . . ."[23] An important addition to the previous policy statement was included in this second document by way of delineation of those instances in which agency heads could make exceptions to the policy in favor of private enterprise-based commercial activity. Previous instructions were that such a decision might be based on a clear demonstration that contracting-out was "not in the public interest" but with no criteria specified to assist in determining what "not in the public interest" meant.[24] B.O.B. Bulletin No. 57-7 stated that the phrase included those specific situations in which the product or service was either:

1. Not available on a competitive basis or at a reasonable price (cited in the previous bulletin but not specified as public interest criteria); or,

2. Should not be procured due to overriding considerations of law, national security, or national policy.[25]

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23. Bull. No. 55-4, supra note 14, at para. 26, Attachment B.

24. Bull. No. 55-4, supra note 14.

25. Bureau of the Budget, Bull. No. 57-7, Commercial-industrial activities of the Government providing products or services for governmental use, para. 10 (1957) [hereinafter cited as Bull. No. 57-7]. Para. 10 states, in referring to those actions which must be taken before establishing new activities: "No new commercial activity shall be started until, as a minimum, the head of the agency has:
   a. Ascertained that the product or service is necessary to the conduct of a governmental function.

Government's experience with the initial contracting-out policy indicated that more emphasis could be placed on the accurate comparison of government and industry costs. In testimony before the Senate Select Committe on Small Business in 1960, the Deputy Director of the Bureau of the Budget, Elmer B. Staats, stated with regard to this cost comparison issue:

> We found [in reviewing agency reports and discussing the program with agency officials] that the costs of Government operation and private procurement could be compared provided they were both fairly computed and complete. Costs assigned to government operation, in order to be comparable, would have to cover all direct and indirect outlays as well as elements not usually chargeable to current appropriations. Costs attributed to procurement from private sources would also have to be computed on an equally fair and complete basis. We realized that some cost items could only be estimated; therefore, the principle

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25. (Cont.)

b. Provided a reasonable opportunity for private enterprise to indicate its ability to furnish the product or service.

c. Determined, on the basis of the response from private enterprise, that the product or service cannot be supplied on a competitive basis or at a reasonable price through ordinary business channels.

d. Determined that it is not in the public interest to procure the product or service from private enterprise, either because it is not available on a competitive basis or at a reasonable price (as found under step (c) above), or because of overriding considerations of law, national security, or national policy.

Steps "b" and "c" may be omitted in those cases where overriding considerations of law, national security, or national policy require that the activity be conducted as a Government operation, but in such cases the head of the agency shall make an appropriate record of his findings and conclusions to that effect."

> was developed that procurement should be from commercial sources unless the difference in comparable cost was relatively large and disproportionate. [26]

This evaluation of previous experience with the contracting-out program was articulated in B.O.B. Bulletin No. 60-2, published in September, 1959, in which it was specified: "Continuation of Government operation on the ground that procurement through commercial sources would involve higher costs may be justified only if the costs are analyzed on a comparable basis and the differences are found to be substantial and disproportionately large" [27] (emphasis added)

Under B.O.B. Bulletin 60-2, the policy expression of earlier publications was changed in form. The document stated clearly: "It is the general policy of the administration that the Federal Government will not start or carry on any commercial-industrial activity to provide a service or product for its own use if such product or service can be procured from private enterprise through ordinary business channels." [28] In explaining that the policy, which established a presumption in favor of contracted-out activities, bene-

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26. 1963 Committee Print, supra note 8, at 30.

27. Bureau of the Budget, Bull. No. 60-2, Commercial-industrial activities of the Government providing products or services for Governmental use, subpara. 3B (1959) /hereinafter cited as Bull. No. 60-2/

28. Id. para. 2.

fitted the free enterprise system as well as permitted each Government agency to concentrate on its primary objective, the bulletin went on to state three exceptions to this policy in which in-house operation became necessary. Those three exceptions, termed "compelling reasons" by the bulletin, were:

1. National security (this exception included those instances in which an activity could not be turned over to private industry for security reasons, including those functions which must be performed by Government personnel in order to provide them with vital training and experience for maintaining combat units in readiness);

2. Relatively large and disproportionately higher costs;[29]

3. Clear unfeasibility; e.g., the product or service was

a. "An intergral function of the basic mission of the agency, or

b. "Not available in the particular instance, nor likely to become available commercially in the foreseeable future because of the Government's unique or highly specialized requirements or geographic isolation of the installation, or

c. administratively impractical to contract for commercially."[30]

29. No definition of this term was provided.

30. Bull. No. 60-2, supra note 27, at para. 3.

Although comparative cost analysis of in-house vs. contracted out activities attained some prominence in B.O.B. Bulletin 60-2, it remained relatively insignificant for several reasons. First, there was still no mistaking the over-all tenor of the document as to what was expected of each agency: "Contract-out if at all possible!" Even the relative cost provision was de-emphasized by subsequent explanation: "The admissibility of relatively large and disproportionately higher costs as a possible compelling reason for continued Government operation does not alter the general policy which establishes a presumption in favor of Government procurement from commercial sources and does not prohibit procurement from more costly commercial sources."[31] Secondly, this reference to "relatively large and disproportionately higher" was not in any way defined, leaving a great deal of room for loose interpretation, if not operational rejection, of the provision.[32] Finally, formal agency findings based

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31. Id. subpara. 3B.

32. Indeed, later Bureau of the Budget publications which have attempted to define and limit this or similar percentage-of-cost terms have been equally ambiguous. One Congressional Committee report recently observed, in referring to testimony dealing with a similar provision in a later Bureau of the Budget publication, Circular No. A-76: "There seems to have been confusion in the minds of different witnesses about the real meaning of "substantial savings" referred to in paragraph 7 b (3) of Circular A-76 and particularly with respect to the 10 percent differential set forth in that paragraph." H. R. Rep. No. 1850, supra note 2, at 3.

on one of the three cited "compelling reasons" were required to be made only where "new starts" of commercial activities or the continuation of existing activities were desired.[33] No such finding was required before decision to contract-out for goods or services could be made.

To date, the Bureau of the Budget has spoken twice more on the government's contracting-out policy.[34] The time period between B.O.B. Bulletin No. 60-2 and its successor, B.O.B. Circular No. A-76,[35] produced landmark decisions by the General Counsel of the Civil Service Commission and the Comptroller General[36] and a large-scale conversion from Department of Defense contracted technical services to in-house operation.[37] Voices could

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33. The Bulletin states: "Proposed starts should be subjected to the same review outlined in this Bulletin for the evaluation of existing activities." Bull. No. 60-2, supra note 27, at para. 6. The Bulletin indicates that the establishment of new activities includes ". . . the establishment, acquisition, or reactivation of any commercial-industrial activity, regardless of the annual estimated cost or value of the product or service." Id. n. 4.

34. Bureau of the Budget, Circ. No. A-76, Policies for acquiring Commercial or industrial products and services for Government use (1966) [hereinafter cited as Circ. No. A-76], and Circ. No. A-76 (revised), supra, note 4.

35. 1959 to 1966.

36. To be discussed infra, note 123, and accompanying text.

37. In June, 1966, the Department of the Army terminated a contract with the RCA Company which had been awarded two years earlier for 5,372 man-months of services at White Sands Missile

be heard during this period speaking both for and against that policy. Thus, in 1963, the Deputy Director of the Bureau of the Budget, Elmer B. Staats, in testimony before the Joint Economic Committee, revealed that the earlier strong position of President Eisenhower's policy was weakening in favor of strict cost analysis. In that testimony, Mr. Staats stated:

> . . . We have placed increased emphasis on using Government installations and staffs rather than commercial or contractual arrangements when commercial operations are clearly more costly. Most of the goods and services needed by the Government will continue to be obtained from commercial or other private sources, but when it is clear that a direct operation by the Government will save money when all pertinent factors are considered, we believe an operation by the Government is warranted. 39 (emphasis added)

Similarly, in hearings conducted during 1964 by the Subcommittee on Manpower of the Committee on Post Office and Civil Service

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37. (Cont).
Range, and converted the operation to in-house (civil service), primarily based on "legal" considerations. Senate Comm. on Government Operations, 90th Cong., 1st Sess., Staff Memo 90-1 8 (1967).

38. One group of private service companies, the National Council of Technical Service Industries, formed in 1965, has been quite active in representing the interests of member companies which contract with the Government through publication of numerous pamphlets dealing with the Bureau of the Budget publications, testimony before Congressional Committees, etc.

39. 1963 Committee Print, supra note 8, at 9.

of the House of Representatives[40] and in the subsequent Committee Report,[41] Committee members expressed their concern with administration policy in those situations where contracting-out for services was more costly than having the same services performed by government employees. In determining that the Secretary of Defense should obtain more complete labor data, including information on the procurement, year after year, of more expensive personnel from contractors to work alongside Government employees, the report concludes: "The subcommittee does not believe that the true cost comparison is being carried on today as it could or should be."[42] Correspondingly, the subcommittee recommended:

(1) The Bureau of the Budget revise its policies re-

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40. Hearings on Control of Labor Cost in the Department of Defense Before the Subcomm. on Manpower Utilization of the House Comm. on Post Office and Civil Service, 88th Cong., 2d Sess. (1964).

41. H. R. Rep. No. 129, 89th Cong. 1st Sess. (1965).

42. Id. XIII. Note that although the House Committee of Post Office and Civil Service expresses concern over relative costs, a recurring theme in its hearings and reports, and in opinions of the General Counsel of the Civil Service Commission, to be discussed infra, is protection of the security of the civil service worker "because he has traditionally done this job with success and is doing so now." For example, in the letter of submittal attached to House Report 129, from subcomm. chairman Henderson to Comm. Chairman Murray, the Honorable Mr. Henderson states:"... it is not good business for the Federal Government to contract with private interests to furnish to the Government 'people' to perform work that currently is and historically has been successfully handled by Government personnel." Id. V.

lating to the procurement of services and products especially as presently found in Bureau of the Budget Bulletin 60-2 to reflect the current administration's program of increased efficiency and economy in the Federal Government.

(2) The Secretary of Defense establish procedures to insure the flow of information into the major commands and the Pentagon on the total labor force throughout the Defense Establishment. Such information should reveal the extent and cost of each type of labor currently used to support military forces, the impact of personnel ceilings, and the effects of personnel changes on the labor force and on the community.

(3) The Secretary of Defense develop definitive comparative cost data relating to contractual operations and to in-house performance. 43

B.O.B. Circular A-76 represents a major change in the previous policy pronouncements concerning contracting-out and signifies the nearly complete eradication of that policy as initially expressed in the 1950's. In stating that its purpose is to ". . . replace the statement of policy which was set forth in Bureau of Budget Bulletin No. 60-2. . .," 44 it provides that: "The guidelines in this Circular are in furtherance of the Government's general policy of relying on the private enterprise system to supply its needs." 45 In promising, however, that it ". . . restates (emphasis added) the guidelines and procedures to be applied. . . in determining whether commercial and industrial products and services used by the Govern-

43. Id. XIV.

44. Circ. No. A-76, supra note 34, at para. 1.

45. Id. para. 2.

ment are to be provided by private suppliers or by the Government itself,"[46] the circular makes an unfortunate choice of words. "Restate" is a misnomer, for not only are the new guidelines and procedures different from previous pronouncements but also their promulgation signifies a basic change in the policy itself. Thus, in specifying those instances in which the Government may perform a commercial or industrial activity,[47] emphasis is placed on effectiveness and efficiency of agency programs rather than on reliance on private enterprise. The mood of Circular A-76 is that each agency must perform its mission efficiently and effectively; if it can do so in concert with the basic "presumption" if favor of private enterprise, so much the better; if not, it must be done in-house.

B.O.B. Circular No. A-76 lists the following instances in which the Government would be justified in providing products or services for its own use:

> 1. Procurement of a product or service from a commercial source would disrupt or materially delay an agency's program.
> 2. It is necessary for the Government to conduct a commercial or industrial activity for purposes of

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46. Id. para. 1.

47. The circular defines the phrase "commercial or industrial activity to be one which"... is operated and managed by an executive agency and which provides for the Government's own use a product or service that is obtainable from a private source." Id. para. 3.

combat support or for individual and unit retraining of military personnel or to maintain or strengthen mobilization readiness.

3. A satisfactory commercial source is not available and cannot be developed in time to provide a product or service when it is needed.

4. The product or service is available from another Federal agency.

5. Procurement of the product or service from a commercial source will result in higher cost to the Government. [48]

It is interesting to note that while B.O.B. Bulletin No. 60-2 specified that in-house operation was permissible only where the "compelling reasons" of national security, relatively large and disproportionately higher costs, and clear unfeasability could be proved by the using agency,[49] those criteria are not mentioned in Circular No. A-76.

The bulk of Ciruclar No. A-76 pertains to methods of making a comparative cost analysis between in-house and contract operations. Hence, in explaining the policy exception for costs, the circular states that in-house operation is permissible when comparative cost analysis shows that Government can do the job at lower cost than private enterprise.[50] The circular acknowledges, however, that in such situations the disadvantage of starting or continuing in-house operations should be considered.[51]

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48. Id. para. 5.

49. Bull No. 60-2, supra note 27, at para. 3.

50. Circ. No. A-76, supra note 34, at subpara. 5e.

51. Id.

Although basic considerations in Circular No. A-76 concerning cost analysis are generally the same as in the predecessor publication, a major difference in A-76 is the exclusion from the cost of Government operations of an allowance for state and local taxes. Bulletin No. 55-4,[52] Bulletin No. 57-7[53] and Bulletin No. 60-2[54] each had provided that, in determining the relative costs of Government operations compared to purchases from private sources, there should be added an allowance for Federal, State and local taxes ". . . to the extent necessary to put the costs on a comparable basis." The absence of this latter provision is disturbing to industry, which asserts that such tax expenditures (state and local) constitute a significant cost factor and that their exclusion seriously impairs the opportunity for equitable cost comparison.[55] Losses of Federal tax revenue to the Federal Government due to withdrawal of property from the tax rolls when Government owns and/or operates the facility are suggested by Circular No. A-76 for consideration as a disadvantage when determining the propriety of in-house operation.[56]

52. Bull. No. 55-4, supra note 14, at para. 6.

53. Bull. No. 57-7, supra note 25, at para. 4.

54. Bull. No. 60-2, supra note 27, at subpara. 3B.

55. National Council of Technical Service Industries, The Impact of Omission of Any Consideration of State Tax Revenues from Cost Comparison Required by Bureau of the Budget Circular A-76 1 (1966).

56. Circ. No. A-76, supra note 34, at subpara. 5e.

Arguably, the comparable loss to state and local governments of corresponding taxes should be considered when Government elects to perform the task itself instead of utilizing private industry.

Another major area of change in Circular No. A-76 is the expansion of those products and services not covered by the pro-private industry policy. The circular states that it:

> 1. Will not be used as authority to enter into contracts if such authority does not otherwise exist nor will it be used to justify departure from any law or regulation, including regulations of the Civil Service Commission or other appropriate authority, nor will it be used for the purpose of avoiding established salary or personnel limitation.
> 2. Does not alter the existing requirement that executive agencies will perform for themselves those basic functions of management which they must perform in order to retain essential control over the conduct of their programs. These functions include selection and direction of Government employees, assignment of organizational responsibilities, planning of programs, establishment of performance goals and priorities, and evaluation of performance. 57

This expansion of the products and services not covered by the policy reflected the 1965 decision of the General Counsel of the Civil Service Commission, which ruled illegal forms of personnel procurement in derogation of the Civil Service laws (to be discussed infra.).[58] Earlier exclusions from the policy had been cursory.

57. Id. para. 4.

58. See note 120, infra, and accompanying text.

Eg., Bulletin No. 60-2 stated, in defining commercial-industrial activity in a footnote, "Also excluded are functions which are a part of the normal management responsibilities of a Government agency or a private firm of comparable size (such as accounting personnel work or the like.)."[59]

B.O.B. Circular No. A-76 was revised in August, 1967.[60] In the letter of transmittal of the revised circular addressed to the heads of executive departments and establishments, Acting Bureau of the Budget Director Phillip S. Hughes recited the verse heard many times before concerning Government policy, although it seemed this time to ring hollow in light of the erosion of the policy's initial character. He stated: "There is no change in the Government's general policy of relying upon the private enterprise system to supply its needs, except where it is in the national interest for the Government to provide directly the products and services it uses."[61] Accordingly, the policy statement in the revised circular recites the identical statement contained in Circular No. A-76.[62] Yet certain changes enunciated in the

59. Bull. No. 60-2, supra note 27, n. 1.

60. Circ. No. A-76 (revised), supra note 4.

61. Transmittal Memorandum No. 1 from Phillip S. Hughes, Acting Director, Bureau of the Budget, to the heads of executive departments and establishments, August 30, 1967.

62. Circ. No. A-76 (Revised), supra note 4, at para. 2.

revision move the "in-house vs. contract-out" decision closer to one based primarily on cost analysis. These changes have to do with modification of earlier requirements on the percentage cost differential for "new starts,"[63] and initiation of a requirement for cost analysis in still another situation.

Although the requirement for cost analysis has become a matter of greater importance with the publication of each successive Bureau of the Budget publication, the publications themselves have offered inadequate guidance as to how much savings is "enough" to justify the utilization or development of in-house facilities. Thus, Bulletin No. 55-4 stated: "The relative costs of Government operations compared to purchase from private sources will be a factor in the determination /as to whether or not existing manufacturing activities should be continued/ in those cases where the agency head concludes that the product or services. . . cannot be obtained at reasonable prices from private industry."[64] (emphasis added) Although the policy

63. The new circular defines a "new start" as:". . . a newly established Government commercial or industrial activity involving additional capital investment of $25,000 or more or additional annual costs of production of $50,000 or more. A reactivation, expansion, modernization, or replacement of an activity involving additional capital investment of $50,000 or more or additional annual costs of production of $100,000 or more are, for purposes of this circular, also regarded as "new starts". Consolidation of two of more activities without increasing the overall total amount of products or services provided is not a "new start." Id. para. 3.

64. Bull. No. 55-4, supra note 14, at para. 6.

statement in that first bulletin claimed that the administration's new policy in favor of private industry precluded both the starting and continuing of commercial activities when not in the public interest,[65] the cost analysis guidelines specified in the bulletin dealt only with continuation or termination of existing operations but made no mention of new starts. Bulletin No. 57-7 did envision that its provisions concerning cost analysis should cover both new start and continuation of in-house situations, but was not more specific than the previous bulletin in defining what cost differential would support a decision favoring in-house operation. Thus, Bulletin No. 57-7 stated:

> The relative costs of Government operation compared to purchase from private sources will be a factor in determining whether to start or carry on a commercial activity in those cases where the agency head concludes that the product or service. . . cannot be obtained at reasonable prices from private industry. (emphasis added).
>
> Prices may be considered reasonable when the price to the Government is not greater than the lowest price obtained by other purchasers, taking into consideration volume of purchases and quality of the products or services. 66

This latter provision would seem to indicate that if the price is reasonable (not more than that charged to other purchasers) Government will continue to obtain the service by contract, even though it might be less expensive to perform the service in-house. Bulletin No. 60-2 shed some light

65. Id. para. 2.

66. Bull. No. 57-7, supra note 25, at para. 4.

on the amount of cost savings which would justify an in-house operation when it stated: "Continuation of Government operation on the ground that procurement through commercial sources would involve higher costs may be justified only if the costs are analyzed on a comparable basis and the differences are found to be substantial and disproportionately large."[67] This reference to "substantial and disproportionately large" speaks rather clearly in favor of contracts for private enterprise. As noted earlier,[68] the overall tone of Bulletin No. 60-2 was still pro-contractor, despite the rumblings in the distance of requirements for consideration of cost. Circular No. A-76 was the result of that distant rumbling. It cited a specific cost savings differential in terms of percentage of cost of obtaining the product or service from commercial sources in an attempt to eliminate the guesswork produced by previous documents. Referring to in-house operation in general, including both "new starts" and continuation of existing operations, the circular stated: "A Government commercial activity may be authorized if a comparative cost analysis prepared as provided in this Circular indicates that the Government can provide or is providing a product or service at a cost lower than if the product or service were obtained from commer-

67. Bull. No. 60-2, supra note 27, at subpara. 3B.

68. See note 31, supra and accompanying text.

cial sources."[69] The circular then defined cost criteria for use in the referenced analysis, but for some unstated reason discriminated between new starts and continuation of existing operations, specifying percentage guidelines in the former but not in the latter case.[70]

Thus, the circular stated, with regard to "new starts":

> A 'new start' should not be proposed for reasons involving comparative costs unless savings are sufficient to outweigh uncertainties and risks of unanticipated losses involved in Government activities.
>
> The amount of savings required as justification for a 'new start' will vary depending on individual circumstances. Substantial savings should be required as justification if a large new or additional capital investment is involved. . . . Justification may be based on small anticipated savings if little or no capital investment is involved, if chances for obsolesence are minimal, and if reliable information is available concerning production costs, commercial prices and Government requirements. While no precise standard is prescribed in view of these varying circumstances a 'new start' ordinarily should not be approved unless costs of a Government activity will be at least 10 persent less than costs of obtaining the product or service from commercial sources.[71] (emphasis added)

Yet the provision governing existing Government activities stated:

> An activity should be continued for reasons of comparative costs only if a comparative

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69. Circ. No. A-76, supra note 34, at para. 5e.

70. Id. subpara. 7b(3).

71. Id.

> cost analysis indicates that savings resulting from continuation of the activity are at least sufficient to outweigh the disadvantages of Government commercial and industrial activities. No specific standard or guideline is prescribed for deciding whether savings are sufficient to justify continuation of an existing Government commercial activity and each activity should be evaluated on the basis of the applicable circumstances. [72] (emphasis added)

Circular A-76, as revised, attempts to clarify the ten precent cost differential in "new starts" authorization by indicating that the referenced percentage should be used only as a guide, and may be more or less, depending on the circumstances.[73] Such an "explanation" serves only to compound the ambiguity of previous instructions, and leaves the operational level decision-maker ample room in which to choose the "path of least resistance," even when confronted with a cost analysis situation.

Edging closer toward primary cost-analysis-based decisions, revised Circular No. A-76 requires that a cost analysis be conducted not only prior to starting or continuing a Government activity but also when it is otherwise deemed advisable. Hence, this discretionary pro-

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72. Id. subpara. 7c(3).

73. Circ. No. A-76 (Revised), supra note 4, at subpara. 7b(3), adds the sentence that: "It is emphasized that 10 percent is not intended to be a fixed figure."

vision states: "Cost comparison studies should also be made in other cases if there is reason to believe that savings can be realized by the Government providing for its own needs."[74]

Each of the Bureau of the Budget publications has suffered a common malady. Although purporting to deal with administration policy concerning procurement both of products and services, each bulletin or circular has been concerned almost exclusively with products.[75] As a result, application of the specified criteria to evaluation and cost analysis of in-house vs. contracted out support

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74. Id. para. 6.

75. Although the Bureau of the Budget admits to difficulty in arriving at a valid definition of "support services," it maintains that Circ. No. A-76 applies across the board to all forms of procurement. Thus, in recent testimony before a Congressional subcommittee, Deputy Director of the Bureau of the Budget Phillip S. Hughes stated: ". . . we have encountered a practical difficulty in defining the term 'service contract' so that it will be uniformly understood and interpreted by all the Government agencies. As A-76 is now written, its provisions apply, across the board, to all types of procurement and there is no necessity for determining whether a particular procurement fits within a prescribed segment of the procurement spectrum. It is the responsibility of the agencies to apply the provisions of Circular A-76 to all types of procurement, taking into consideration the facts and circumstances that prevail in each individual case, irrespective of whether the procurement may be regarded by them as falling within a service-contract category, or some other category which they may establish for purposes of implementing the provisions of the circular." 1968 Hearings, supra note 3, at 34.

services is difficult.[76] For example, in defining "new starts," Revised Circular No. A-76 uses such terms as "reactivation, expansion, modernization or replacement of a commercial or industrial activity," "capital investment", and "annual costs of production." Also, in its explanation of the relative cost advantage of in-house operation vis a vis contracting-out, the latest circular refers mainly to facilities, not services. Thus, the circular speaks of "removal or withholding of property from the tax rolls,"[77] "obsolescence of plant and equipment,"[78] and required cost analysis when Government stands to finance more than $50,000 "for costs of facilities and equipment."[79]

The current status of the policy in favor of contracting-out to private enterprise will be discussed more fully, infra. Yet it is important to visualize at this point how far from the initial expression

76. During testimony before a subcommittee of the House Committee on Government Operations in April, 1968, the subcommittee chairman, the Honorable Porter Hardy, Jr., observed: "Well, I have tried my best to see how you are going to fit Circular A-76 into all kinds of procurement. Maybe it is just because I look at the thing from a different standpoint /from the witness, Deputy Director of the Bureau of the Budget, Phillip S. Hughes/, but I have a hard time finding out how to apply a good many of the provisions in it to a service contract. It seems to me that A-76. . . is designed primarily for the procurement of things, of commercial-type items, and not of service particularly." Id. 37.

77. Circ. No. A-76, supra note 34, at subpara. 5e.

78. Id.

79. Id. para. 6.

of the policy we have come, at least within the Bureau of the Budget. Passing from the initial pronouncement, which indicated that it would be the unusual situation where cost was the deciding factor in determining whether to utilize in-house or contracted-out activities,[80] we have reached a temporary plateau on which each agency within the Government is required to justify "in-house" alternatives by cost-analysis but may, as a discretionary matter, use cost analysis in other instances when deemed advisable.[81] As will be seen in subsequent discussion, other Government agencies, specifically the Department of Defense and the General Accounting Office, have advocated cost analysis as the primary basis for making all in-house vs. out-house decisions.

C. The Department of Defense

The Department of Defense has directed its attention to the problem of in-house vs. contracted-out operations since 1952. In that year, D.O.D. Directive 4000.8 indicated that Department of Defense policy opposed continued operation and retention of in-house facilities. Hence, continued in-house operation required justification, and new starts were restricted.[82]

80. Bull. No. 55-4, supra note 14, at Attachment B, para. 26.

81. Circ. No. A-76 (Revised), supra note 4, at para. 6.

82. 1963 Committee Print, supra note 8, at 33.

In testifying before the Senate Select Committee on Small Business in 1953, Mr. Charles Thomas, Assistant Secretary of Defense for Supply and Logistics, stated:

> It will be the Department of Defense policy to get out of Commercial and industrial type activities to the maximum practicable extent, and this policy with respect to commercial and industrial-type activities is stated in a Department of Defense directive dated November 17, 1952, which provides in part, as follows:
>
> Such /commercial and industrial/ facilities will not be continued in operation where the required needs can be effectively and economically served by existing facilities of any department or where private commercial facilities are available, except to the extent that such private commercial facilities are not reasonably available or their use will be demonstrably more expensive or except where the operation of such facilities is essential for training purposes. No facilities, not in operation, shall be retained unless necessary for mobilization reserve. Cost accounting methods will be employed to assist in formulation of decisions concerning cross-servicing, establishment or continuance of such activities in or under the Department of Defense. 83

Numerous other directives and instructions were published in 1953 and 1954 which provided more specific guidance to the various military departments for the conduct of systematic review of existing commercial and industrial-type activities.[84]

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83. Id. 34.

84. Id.

The Department of Defense's program favoring private enterprise preceded that of the Bureau of the Budget (the B.O.B. program was not established until the publication of B.O.B. Bull. No. 55-4 in 1955).[85] But in 1955, after announcement of the Bureau of the Budget policy, there was evidence that the Department of Defense and Bureau of the Budget programs would be merged. Commenting to that effect before a hearing conducted by the Senate Select Committee on Small Business in April, 1955, a Department of Defense representative, Mr. O.H. Dersheimer, testified: ". . . the Defense Department has been pushing forward a program to take the Department of Defense out of competition with private business so far as this objective can possibly be accomplished without weakening our defense position."[86] Noting Bureau of the Budget Bulletin No. 55-4, he stated: ". . . we are merging our program with that of the Bureau of Budget."[87]

Initial progress under the Department of Defense policy favoring private enterprise was measured in terms of the number of Government operations discontinued or curtailed. Thus, Mr. Perkins McGuire, Assistant Secretary of Defense, Supply and

85. Bull. No. 55-4 was published on January 15, 1955.

86. 1963 Committee Print, supra note 8, at 34.

87. Id.

Logistics, testified before the Senate Select Committee on Small Business in April, 1957, that as of April 1, 1957, 548 Government commercial or industrial-type operations had been scheduled for discontinuance or curtailment.[88] The review of Government operations was continuous. Thus, Department of Defense representative Mr. Russell A. Crist testified before the same committee in May, 1960:

> The Department of Defense in implementing... [B.O.B. Bull. No. 60-2]... has endeavored to insure that all commercial and industrial activities are inventoried and reviewed. Special emphasis has been placed upon major items, such as arsenals, shipyards, aircraft, ship and vehicle maintenance and repair; transportation on a worldwide basis; communication, and warehousing and storage. 89.

In response to studies, hearings and recommendations of the Subcommittee on Manpower of the Committee on Post Office and Civil Service,[90] a special project was established in 1964 by Secretary of Defense McNamara to examine the use of contract support services within that agency. In a memorandum dated September 11, 1964, he indicated to the three service secretaries:

> Studies by congressional committees, the General Accounting Office and the Department of Defense have raised questions concerning our policies and

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88. Id. 36.

89. Id.

90. H. R. Rep. No. 129, 89th Cong., 1st Sess. (1965).

> practices in deciding when to accomplish the performance of support-type activities by military personnel, direct-hire civilian personnel, or by contract. These studies indicated that there are varying practices among the Department which, in some cases, may result in uneconomic practices or be inconsistent with Civil Service laws and regulations. . . . It is our objective to assure that the Defense Department is equipped and staffed to perform efficiently and effectively all of those functions which are essential to military readiness. After having made this determination, it is our objective in regard to other activities to select that arrangement consistent with Civil Service laws and regulations, which will produce the lowest overall cost. . . .(91)

The study group was directed to concern itself specifically with situations in which greater use of contract support services would be more economical and situations in which contract support services should be terminated for excessive costs.[92] In a memorandum dated January 8, 1965 the Assistant Secretary of Defense, Paul Ignatius announced an interim report which recommended the conversion to direct-hire civilian or military positions or replacement of contract technical personnel.[93] When the final report and recommendations

91. Senate Comm. on Government Operations, 90th Cong., 1st Sess., Staff Memo 90-1-8, Appendix B (1967).

92. Id.

93. Id. The Armed Services Procurement Regulation (31 Mar. 1969, Rev. No. 1) defines contract technical personnel in section 22-301:

> Definition of Contractor Engineering and Technical Services. Contractor engineering and technical services consist of the furnishing of advice, instruction,

of the special project group, headed by Mr. Robert C. Moot, Deputy Assistant Secretary of Defense (Logistics Services), were approved by Secretary McNamara in 1965, it became clear that the Department of Defense had again antedated the Bureau of the Budget (in Circular A-76) in effecting an administration policy change. Primary emphasis in the new policy was placed on military readiness and efficiency, as opposed to the earlier Department of Defense policy that "...the Department of Defense... /will/... get out of commercial and industrial type activities to the maximum practicable extent..."[94] The final

93. (Cont.)
and training to Department of Defense personnel, by commercial or industrial companies, in the installation, operation, and maintenance of Department of Defense weapons, equipment, and systems. This includes transmitting the knowledge necessary to develop among those Department of Defense personnel the technical skill required for installing, maintaining, and operating such equipment in a high state of military readiness. These services may be subdivided into the following categories.

(a) Contract plant services (C P S) are those engineering and technical services provided by the trained and qualified engineers and technicians of a manufacturer of military equipment or components, in the manufacturer's own plants and facilities.

(b) Contract field services (C F S) are those engineering and technical services provided on site at defense locations by the trained and qualified engineers and technicians of commercial or industrial companies.

(c) Field service representatives are those employees of a manufacturer of military equipment or components who provide a liaison or advisory service between their company and the military users of their company's equipment or components."

94. Supra, note 83, and accompanying text.

report recommended elimination of numerous contract technical positions where inconsistent with the civil service laws and regulations. In keeping with the new emphasis on military readiness and efficiency, the report also stated: "Conversion of technical... services will be... considered desirable when it is technically feasible, improves military readiness and is economical."[95]

Reflecting the change in Department of Defense policy with regard to contracting-out,[96] three new directives were published in 1965 and 1966, and are currently in effect.

1. D.O.D. Directive No. 1130.2, published on 2 October 1965, entitled "Engineering and Technical Services-Management

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95. Senate Comm. on Government Operations, 90th Cong., 1st Sess., Staff Memo 90-1-8, Appendix B (1967).

96. It has been suggested by one Congressman that the change in Department of Defense policy resulted from the following factors: "(1) a series of studies and hearings by the Subcommittee on Manpower Utilization of the House Committee on Post Office and Civil Service, beginning in November 1963 and embodied in the Henderson Report; (2)a report by the Comptroller General, dated March 19, 1964, relative to excessive costs incurred by the Department of the Air Force installation in Japan; (3)a decision by the General Counsel of the Civil Service Commission, dated February 12, 1965, concurred in, generally, by the Comptroller General; and (4) a report and recommendation by a Project Staff, appointed by the Secretary of Defense and headed by Robert C. Moot, now Deputy Assistant Secretary of Defense (Logistics Services) begun in September 1964 and completed in March 1965 (referred to as the 'Moot Report'). Sen. John L. McClellan, Chairman Sen. Comm. on Government Operations, as cited in Senate Comm. On Government Operations, 90th Cong., 1st Sess., Staff Memo 90-1-8 (1967).

and Control;"

2. D.O.D. Directive No. 4100.15, dated 9 July 1966, whose subject is "Commercial or Industrial Activities;" and

3. D.O.D. Instruction No. 4100.33, published on 22 July 1966, entitled "Commercial or Industrial Activities-Operation of."

Indicative of the new Department of Defense policy which places strong emphasis on efficient and effective performance of military readiness functions and in-house self-sufficiency is D.O.D. Directive No. 1130.2 ("Engineering and Technical Services-Management and Control"). The directive states, under the heading "policy:" "D.O.D. components will achieve in-house self-sufficiency as early as possible in the installation, operation and maintenance of their weapons, equipment and systems."[97] The directive cautions: "Contract Field Services (CFS) will be utilized only where necessary for accomplishment of a military mission, and where satisfactory provision of services by D.O.D. personnel is not practicable."[98]

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97. Dep't of Defense Directive No. 1130.2, sec. V A.1 (2Oct. 1965).

98. Id. sec. V. B. This provision is apparently based on 36 Comp. Gen. 338, 339 (1956), in which the Comptroller General stated: ". . . when the services required would ordinarily fall within the scope of work generally performed by officers and employees of the agency or of other Government agencies, the determination to invoke such contracting authority should be based on cogent considerations of the necessity, efficiency, and economy of the contract procurement." (emphasis added).

D.O.D. Directive 4100.15 implements Bureau of the Budget Circular No. A-76. In stating that the Department of Defense, in conformity with the principle espoused in the referenced circular of relying on private enterprise for products or services"... to the maximum extent consistent with effective and efficient accomplishment ..."[99] of its programs, and that only where it is in the national interest for Government itself to provide those services will it begin or continue an existing operation, the directive states: "...the Department of Defense depends upon both Private and Government commercial or industrial sources for the provision of products and services, with the objective of meeting its military readiness requirements with maximum cost effectiveness."[100] The directive then specifies under the title "Policy" that in-house commercial or industrial activities may be continued or initiated as new starts only when one or more of certain criteria exist (citing the five criteria specified in para. 5, B.O.B. Circular No. A-76).[101] The directive proscribes

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98. (Cont.)
The provision in the D.O.D. Directive does not recognize subsequent rulings by the General Counsel of the Civil Service Commission and the Comptroller General which prohibit contracts for personal services (other than those permitted by statute) as a matter of law. See note 126, infra, and accompanying text.

99. Dep't. of Defense Directive No. 4100.15, sec. IV (9 July 1966).

100. Id.

101. Id. sec. V. A. See supra, note 48, and accompanying text.

contracting-out for those basic functions of management necessary to retain control over conduct of agency programs. It lists, as examples of basic functions of management: ". . . selection, training and direction of Government personnel, assignment of organizational responsibilities, planning of programs, establishment of performance goals and priorities, and evaluation of performance,"[102] as did the Bureau of the Budget publication, but then qualifies this limitation by permitting contracting-out for ". . . professional staff advisory and other support services related to. . . /the excluded/. . . internal functions, provided that the Government's fundamental responsibility for controlling and managing its program is not compromised or weakened."[103]

In explaining the requirements for implementation of D.O.D. Directive No. 4100.15 and B.O.B. Circular No. A-76, D.O.D. Instruction 4100.33 generally adheres to the specific requirements of those publications with regard to determination of when to contract-out and when to start or continue in-house. In one important regard, however, the implementing instruction goes further than the Bureau of the Budget publication by requiring a comparative cost analysis to be made not only prior to new start or continuation circumstances,

102. Id. sec. V D.

103. Id.

but also before contracting-out for the performance of the agency's operational need. Hence, the Secretary of each military department is responsible for "making a comparative cost analysis before procuring products or services from private commercial sources when the procurement will cause the Government to finance directly or indirectly more than $50,000 for costs of facilities and equipment to be constructed to Government specifications."[104] The instruction provides that cost analysis is also required:

> 1. When the decision to rely upon a government in-house activity to provide the products or services is determined on the basis of relative cost. . . .
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> * * *
>
> 3. When there is a probability that products or services being procured from private enterprise could be obtained from Government sources at a lower overall total cost to the Government.[105]

It should be observed that, while the Bureau of the Budget has not adopted the requirement specified in the implementing

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104. Dep't of Defense Instruction No. 4100.33, sec. VI F (22 July 1966). Note that this is addressed primarily to products, not services, when it speaks of "cost of facilities and equipment." But it would appear to include some service contracts. For example, a contract which required the contractor to furnish a particular type of garbage truck to pick up metal garbage containers would apparently be subject to this requirement for comparative cost analysis. Contracts for services or for products and services where the Government finances less than $50,000 for cost of facilities and equipment are clearly not covered by this provision.

105. Id. Incl. 3, sec. III A.

Department of Defense directives for additional cost analysis prior to a decision to contract-out, such a position is advocated by various other elements in our Government. Thus, in a report to the Congress dated September 6, 1967, concerning the relative cost of converting approximately 10,500 contract technical service personnel from contract to civil service positions, the Comptroller General of the United States stated:

> On the basis of our rather extensive reviews performed at the National Aeronautics and Space Administration and the Department of Defense, we believe that an executive agency should make a determination on a case-by-case basis as to whether technical services could be more effectively performed by civil service personnel or by contractor-furnished personnel. If it is determined that effective performance could be achieved by either means, we believe that the agency should then make a detailed cost comparison of contractor versus in-house performance of such work. The agency's decision could then be made in full awareness of economic considerations. 106

In addition, the Senate Committee on Government Operations, after conducting numerous hearings on the subject of "Government Policy and Practice With Respect To Contracts For Technical Services," concluded in its report: "It is apparent that due consideration of the element of cost requires that some form of comparative cost studies

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106. Staff of Senate Comm. on Government Operations, 90th Cong., 2d Sess., Committee Print on Government Policy and Practice With Respect to Contracts for Technical Services 22 (1968) /hereinafter cited as 1968 Committee Print/

must be made by executive branch agencies prior to determining whether to perform a task in-house or by private contract."[107]

And finally, in its August, 1968 report entitled "Criteria For Support Service Cost Comparisons," the House Committee on Government Operations recommended that:

> 1. The Bureau of the Budget should issue a circular or sufficiently revise Circular A-76, to provide specific criteria governing cost comparisons of support services. Only in this manner can a determination be made as to whether such services can be obtained on a more economical basis by contract or by in-house performance.
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> 2. Exeept in special situations, A-76, or a new circular, should . . . require the making of a cost comparison for support services, before a "new start" or a contract is made. 108 (emphasis added)

Aside from the practical problems attaching to an across-the-board cost analysis requirement in contract-out vs. in-house determinations,[109] certain fundamental questions of concept present themselves. Granted that sound business practice requires serious

107. Id. 11.

108. H. R. Rep. 1850, supra note 2, at 4.

109. The Department of Defense's implementing directive of Bureau of the Budget Circular A-76 which requires cost studies of contractual arrangements for support services as well as in house". . . has created a very heavy burden of studies ranging over a wide field of contractual arrangements." 1968 Committee Print, supra note 105, at 41.

consideration of the relative costs of various alternatives, can that requirement for cost analysis be superimposed upon a policy favoring one of those alternatives, contracting-out for goods and services? The purpose of contracting-out, as initially conceived, was to reduce or terminate, whenever compatible with the national interest, Government competition with private enterprise. Although it has never been clear just what meaning attached to the phrase "in the national interest", it is readily apparent at this time that it means efficiency and economy; i. e., if Government can do the job more cheaply than the private sector, then Government can and must compete with private enterprise, for it is "in the national interest" to do so. Of course, this is not the whole picture, as we shall see in studying the various opinions of administrative decision-makers regarding the "legality" of contracting-out for support services. But enough of the picture is complete to explain part of the difficulty with current contracting-out practice. Although emphasis is still placed on contracting with private industry for goods and services, agencies are with increasing frequency being pushed toward cost-based decision-making as the ultimate criterion in the in-house vs. out-house question. Under the true cost analysis determination, after eliminating all the excluded criteria in the Bureau of the Budget and Department of Defense

publications, the ultimate criterion is not "will this help private industry?, but "will this cost less?" Then, the new policy muses almost as an afterthought, "if it does cost less and at the same time also happens to benefit private industry, how nice it will be!" [110]

But, as noted earlier, the picture is not yet complete. In addition to the in-house vs. out-house dilemma caused by the

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110. The subject of cost accounting is beyond the scope of this thesis. Its complexity has been the frequent subject of discussion and debate in Congress and industry. As an example of the difficulties involved, note the discussion as to whether total costs to Government to include "overhead", should be included in cost analysis. The Government Accounting office believes that overhead should not be included in Government cost analysis unless it can be shown in an individual case that such costs would be increased. 1968 Committee Print, supra note 105, at 41. Industry argues, however, that such costing unfairly weights advantage toward in-house operation. Id. 42. This is currently an important issue, and one concerning which industry has already taken the opportunity to notify the new Secretary of Commerce, Mr. Maurice Stans. In a letter dated 17 Dec. 1968, Mr. John G. Reutter, President of the Consulting Engineers Council, stated to the Secretary-designate his concern about the award to the Federal Aviation Administration of a $799,651 contract to Coast and Geodetic Survey for engineering and surveying services at 150 U.S. airports thusly:

"We are unable to understand. . . how anyone familiar with the daily conduct of an office or business could suggest that it can do this work with no overhead! We realize that the Government has inserted some elements of 'overhead' in other portions of its cost breakdown but where are such items as: rent, legal services, accounting, photogrammetric equipment, depreciation, insurance, social security, and workmen's compensation (to name a few)? If U.S.C. & G.S., together with GAO has devised a means of avoiding such expenses, they owe it to the business community of the nation to point out how." 254 Fed. Cont. Rep. E-1 (1968).

cost analysis requirement, certain important "legal" limitations which have been placed on the practice of contracting-out by the Comptroller General of the United States and the General Counsel of the Civil Service Commission add to the difficulty of determining how, when, and by whom the decision to contract-out should be made.

D. The General Accounting Office and the Civil Service Commission.

The General Accounting Office was established in 1921 by passage of the Budget and Accounting Act of 1921.[111] This office has exerted a strong influence on the development of the policy dealing with contracting-out for services. Empowered by the act to exercise the sole authority to ". . . settle and adjust all claims by and against the Government and all accounts in which the Government is concerned. . .,"[112] the Comptroller General has, among his many decisions since 1921, refused to permit payment for services rendered,[113] withheld approval of a service contract,[114] and required the earliest possible termination of a service contract,[115] based on a rule he has concomitantly developed which prohibits the acquisition by a Government agency of "personal services" by

111. Section 236, Revised Statutes, as amended (31 U.S.C. 71; M.L. 1949, sec. 1954).

112. Id.

113. 31 Comp. Gen 510 (1952).

114. 15 Comp. Gen 951 (1936).

115. Ms. Comp. Gen. B-113739, 2 Apr. 1953.

contract from private enterprise.[116] Basically, the rule is designed to preclude the establishment of an employer-employee relationship outside the existing Federal Statutory system.[117]

The current Comptroller General recently stated the rule thusly:

> The general rule. . . is that Government agencies may contract for the performance of required services including services which traditionally have been performed by Government employees if contracting out is determined to be justified on the basis of considerations of necessity, efficiency, and economy. However, contracts which are entered into in reliance on that rule must be made on an independent contract or non-personal service basis; that is, they must require the performance of a complete job or task by the contractor and not merely the furnishing of personnel who will work under the supervision and control of Government employees.[118]

Although the rule apparently finds little support in statutory law,[119]

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116. 17 Comp. Gen. 300 (1937).

117. Ms. Comp. Gen B-146824, 4 Mar. 1965 [hereinafter cited as Fuchu (1965)]. Contained in H. R. Rep. No. 188, 89th Cong., 1st Sess., Decision of the Comptroller General of the United States Regarding Contractor Technical Services 1, (1965).

118. Hearings on Government Policy and Practice with Respect to Contracts for Technical Services Before the Senate Comm. on Government Operations, 90th Cong., 1st Sess. (1967) [hereinafter cited as 1967 Hearings]

119. Fairbanks, Personal Service Contracts, 6 Mil. L. Rev. 1 (1959). The author states: "It thus seems clear that the [personal services] rule in its breadth as enunciated by the Comptroller General finds little support in the law." Id. See also, Bisson, Statutory Limitations on Contracts for Services of Government Agencies, 34 Brooklyn L. Rev. 197, 222 (1968), where the author concludes: "It is submitted that the decision whether to engage a Federal employee to perform Federal services

it is now firmly entrenched in the administrative and regulatory system controlling Goverment agency operations[120] and is thus an important consideration for the "contract-out vs. in-house" decision maker.

During the development of the rule prohibiting personal service contracting, the Comptroller General has vacillated between law and policy as the basis for the rule. Thus, in 1943, he stated that the rule was one of law.[121] In 1945,[122] however, and from then

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119 (Cont.)
or to contract such work out to bona fide independent contractors involves the exercise of discretion. . . /which/. . . should not be limited by such non-statutory restrictions as the Comptroller's policy against personal service." (emphasis added)

120. Eg., Armed Services Procurement Reg., sec. 22-102.1(a) (31 Mar. 1967, Rev. No. 1), states, under the heading Policy: "The Civil Service laws and regulations and the Classification Act lay down requirements which must be met by the Government in hiring its employees, and establish the incidents of employment. In addition, personnel ceilings have been established for the Department of Defense. Except as otherwise authorized by express statutory authority (e.g., 5 U.S.C. 3109b as implemented by the annual Department of Defense Appropriation Act- expert and consultant services. . .), these laws and regulations shall not be circumvented through the medium of 'personal services' contracting, which is the procuring of services by contract in such a manner that the contractor or his employees are in effect employees of the Government."

121. 22 Comp. Gen. 700 (1943).

122. 24 Comp. Gen 924 (1945).

until 1965[123] he maintained the position that the prohibition was a policy matter under which the services although "personal" in nature could nonetheless be approved by the Comptroller General if certain criteria were met. Thus, in 1963, in approving a proposal by the Internal Revenue Service to contract for the receipt, storage and issue of Federal Income Tax forms to points within the Los Angeles District of the Internal Revenue Service for a four and one-half month period, a proposal which he deemed a ". . . purely personal service contract. . .", he stated:

> The general rule is that purely personal services for the Government are required to be performed by Federal personnel under governmental supervision . . . However, the requirement of this rule is one of policy rather than positive law and when it is administratively determined that it would be substantially more economical, feasible, or necessary by reason of unusual circumstances to have the work performed by non-goverment parties, and that is clearly demonstrable, we would not object to the procurement of such work through proper contractual arrangements. 124 (emphasis added)

Apparently having no particular predilection toward the stare decisis concept, however, the Comptroller General again decided in 1965 to treat the rule prohibiting contracting-out for personal services as a matter of law.[125] In 1964, in response to an earlier request from the General Accounting Office, the Civil Service Commission examined

123. Fuchu (1965), supra note 117.
124. 43 Comp. Gen. 390, 392 (1963).
125. Fuchu (1965), supra note 117.

certain contracts for contractor-furnished personnel at the Pacific Region Ground Electronics Engineering Agency. Of specific importance were contracts for 104 contract technicians at Fuchu Air Force Base, Japan, as well as other contracts with industry for employment of technicians by the Department of Defense.[126] In a strongly worded opinion subsequently concurred in by the Comptroller General,[127] the General Counsel of the Civil Service Commission ruled that under circumstances where no real distinction can be drawn between positions filled by contract personnel and those filled by Federal employees the positions should be Federal positions and the employees Federal employees paid under appropriate personnel statutes. Further, personnel procured by contract to fill such positions are illegally obtained in violation and evasion of the

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126. As to the authority of the Civil Service Commission to make such an investigation, Mr. John W. Macy, Jr., Chairman, Civil Service Commission, in testimony before the Senate Comm. On Government Operations in 1967, stated: "As the central staff agency for personnel, the Commission must be constantly alert that the provisions of the civil service laws are fully observed. . . ." 1967 Hearings, supra note 118, at 247. In the legal memorandum attached to the Fuchu opinion supra note 117, at 6 it is stated: ". . . the Commission (not the agency) has the authority to determine whether or not the agency has established an employer-employee relationship when it has contracted out with a private organization to furnish personal services," citing the Classification Act of 1949, as amended, 5 U.S.C. 1071 et. seq.

127. Fuchu (1965), supra note 117, at 1.

Civil Service Act, the Veteran's Preference Act, the Classification Act, and other personnel statutes.[128] What is proscribed, noted the General Counsel, is an employer-employee relationship which is established by means other than the applicable Federal Personnel laws.[129] How determine this employer-employee relationship? In the Fuchu decision, three criteria were listed: whether a person is (1) engaged in the performance of a Federal function under authority of an act of Congress or an Executive order; (2) performing duties subject to the supervision of a Federal officer or employee; and (3) appointed in the civil service by a Federal officer or employee.[130]

In a more recent opinion, the General Accounting Office referred six contracts at the Goddard Space Flight Center for on-site technical services to the Civil Service Commission for determination of legality with respect to their terms and operations.[131] Using the same three criteria as he had in the Fuchu opinion, the General Counsel determined that the support technicians had been placed in a relationship with Government ". . . tantamount to an employer-employee relationship,"[132]

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128. Fuchu (1965), supra note 117, at 4.

129. Id. 3.

130. Id.

131. Ms. Opn. Gen. Counsel of C.S.C. 3, 18 Oct. 1967 [hereinafter cited as Opn. (1967)].

132. Id. 37.

and that the contracts effectively violated the requirements and policies of the personnel laws by their procurement of personnel in that manner.[133] Consequently, he ruled that ". . . the contracts under review and all like them are proscribed unless an agency possesses a specific exception from the personnel laws to procure personal services by contract."[134]

Clearly, the General Counsel of the Civil Service Commission treats contracts for "personal services," other than those contracts permitted by statute, as illegal without exception.[135] The Comptroller

133. Id.

134. Id. 40 The following standards were set down by the opinion:
". . . contracts which, when realistically viewed, contain all the following elements, each to any substantial degree, either in the terms of the contract or in its performance, constitute the procurement of personal services proscribed by the personnel laws.

Performance on-site.

Principal tools and equipment furnished by the Government

Services are applied directly to integral effort of agencies or an organizational subpart in furtherance of assigned function or mission

Comparable services, meeting comparable needs, are performed in the same or similar agencies using civil service personnel

The need for the type of service provided can reasonably be expected to last beyond one year.

The inherent nature of the service, or the manner in which it is provided reasonably requires directly or indirectly, Government direction or supervision of contractor employees in order:

To adequately protect the Government's interest or

To retain control of the function involved, or

To retain full personal responsibility for the function supported in a duly authorized Federal officer or employee." Id.

135. During Hearings before the Senate Comm. on Government Operations in 1967, the following colloquy occurred between the Acting

General published his concurrence with this second Civil Service Commission opinion in November, 1967. Although the concurrence is in general terms, it is obvious that the Comptroller General also treats the matter of the "personal service" prohibition as a legal, not a policy, question.[136] Thus, in an opinion subsequent to the NASA

135. (Cont.)
Committee Chairman, Senator Joseph M. Montoya, and Mr. John W. Macy, Chairman of the Civil Service Commission:

Senator Montoya: "Let us assume the factual situation of the Fuchu case in another case, Mr. Macy. But in addition there is a cost consideration which reflects that the contractor cost would be more economical than the in-house operation. What would be the attitude of the Civil Service Commission?

Mr. Macy: "Well, if the facts were the same as in the Fuchu case, the Commission's judgment would be that the contract was still illegal.

* * *

Senator Montoya: "All right. Let's assume the same facts as in the Fuchu case with the additional consideration that the particular function being handled by the contractor will better promote military readiness and at the same time be done at less cost than the in-house operation. What would the attitude of the Civil Service Commission be under those circumstances?

Mr. Macy: "There is no congressional exception in cases where a higher degree of military readiness is called for and consequently I would answer the same was as I did in the previous question" 1967 Hearings, supra note 118, at 254.

136. Ms. Comp. Gen. B-133394, 1 Nov. 1967. Although concurring in the opinion of the General Counsel of the Civil Service Commission, the Comptroller General Opinion construes it rather strictly. The opinion states: We think it is clear from the. . . /CSC Opinion/. . . that no single provision of a contract, such as the task assignment or technical direction requirement, may constitute the basis for a determination that the contract is or is not proscribed by the personnel laws. Rather, the Opinion requires, before an adverse determination, (1) a realistic consideration of the provisions of the entire contract and the overall substance of the operations thereunder, and(2) a conclusion that each of the stated elements is involved therein to a substantial degree." Id. 1.

case, the Comptroller General ruled that the General Services Administration could not enter into contracts for the procurement of services of clerks, typists, telephone operators and teletype operators on a temporary basis during peakload and emergency periods.[137] In so ruling, the Comptroller General utilized the three criteria cited by the General Counsel of the Civil Service Commission in the Fuchu opinion for identifying an employer-employee relationship.[138] and observed that the GSA". . . does not have inherent power to disregard the enactments of Congress with regard to the Classification Act and the civil service laws and 'employ' individuals through personal service contracts. . . ."[139] And in testimony before the Senate Government Operations Committee in 1967, Comptroller General Elmer B. Staats stated with regard to the Fuchu concurrence by his predecessor-in-office, Comptroller General Joseph Campbell: ". . . it was the intent of that statement to support the position taken by the General Counsel of the Civil Service Commission. In other words, we concurred with the legal position taken by counsel for the Civil Service Commission."[140] (emphasis added)

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137. 44 Comp. Gen. 761 (1965).

138. Supra, note 117, and accompanying text.

139. 44 Comp. Gen. 761, 764 (1965).

140. 1967 Hearings, supra note 118, at 264.

A curious question has arisen concerning the connotation of the words "illegal" and "legal" as used by the General Counsel of the Civil Service Commission and the Comptroller General. When these two individuals testified in Senate hearings in 1967 concerning contracting-out for services, they seemed to agree that although personal service contracts are "illegal" . . . they. . . /can be/ . . . permitted for a period of time necessary for conversion transition, as accepted practice and in the interests of good management and the continuation of necessary functions."[141] Also, Department of Defense Directive 1130.2 and the Armed Services Procurement Regulations appear to sanction the use of personal service contracts ". . . in the event unusual requirements involving essential mission accomplishment necessitate the procurement of contract field services. . ." if authorized by the Assistant Secretary of Defense for Manpower,[142] in consultation with the Civil Service Commission.[143] This may well indicate that the question of the "personal services" prohibition is closer to one of policy than either the Comptroller General or the General Counsel of the Civil Service Commission care

141. 1968 Committee Print, supra note 105, at 16.

142. Armed Services Procurement Reg. Sec. 22-302.2 (31 Mar. 1969, Rev. No. 1)

143. Dep't of Defense Directive 1130.2 sec. V C2 (2 Oct. 1965).

to admit. The answer seems to lie somewhere in the gray area between policy and law.

III. THE PRACTICAL LIMITS OF THE POLICY

Prior to determining what order can be made of the disorder that is the "policy-cost-legality" question, it is appropriate to examine the decision-making process under existing directives and regulations to expose those practical operational problems which have resulted from their interpretation.

The man on the "hot seat" in the majority of cases is the contracting officer. Assume for a moment that a commander is given a mission which includes a support-service requirement that might be performed with equal efficiency either in-house or by contract. In determining which alternative is the more appropriate, the commander's contracting officer utilizes a two step method. He must initially ask the question: is this a "personal serivce" and thus precluded from being procured by contract by current regulations which implement the decisions of the Comptroller General and the General Counsel of the Civil Service Commission?[144] This initial determination is relatively easy, as a practical matter, for guidelines exist which are sufficiently

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144. Armed Services Procurement Reg. sec. 22-1021(a)(31 Mar. 1969, Rev. No. 1).

definitive to permit him to decide the question in his own office without going elsewhere for assistance. Thus, he considers:

1. The nature of the work(his consideratinn must include an examination of whether the services represent the discharge of a Governmental function calling for the exercise of judgment or discretion by the Government[145]);

2. Those contractual provisions which concern the contractor's employees, (such as whether the Government specifies the qualifications of, or reserves the right to approve each contractor's employees[146]);

3. Other provisions of the contract (such as whether the services can properly be defined as an end product, and whether payment will be for results accomplished or based only on the amount of time worked[147]); and

4. How the contract will be administered. This provision recognizes that, although by the terms of a contract no "personal services" are provided for, the actual performance of the contract may prove the converse.[148]

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145. Id. sec. 22-102.2(i).

146. Id. sec. 22-102.2 (ii).

147. Id. sec. 22-102.2 (iii).

148. Id. sec. 22-102.2 (iv).

Of course, there are those situations in which the "personal service vs. non-personal service" portion of the decision will not be a clear case. Such situations are provided for in ASPR 22-102.1, which requires that the contracting officer obtain a legal opinion in doubtful cases.[149] This regulatory provision also requires a legal opinion to be obtained in those cases where a "personal service" permitted by statutory exception, such as for expert or consultant services under 5 U.S.C. 3109 b,[150] is sought to be procured by contract. Normally, the contracting officer is able to make this initial decision within his own resources. Clearly, at this point, if the services are "personal" in nature (and not permitted by statutory exception), the contracting officer is compelled to initiate action for a "new start;" that is, to establish the serivce activity within the Department of the Army using military or civil service resources.[151] On the other

149. Id. sec. 22-102.1.

150. Id. Procurement of such services must be authorized by an appropriation or other statute. 5 U.S.C. 3109 b.

151. Although this effectively is a "compelling reason" which requires in-house operation, it is interesting to note that it is not listed as such in Army Regulation No. 235-5 (28 Nov. 1966) which implements the commercial and industrial facilities program in the Department of the Army. That regulation's only reference to the objectionable "personal services" contract is contained in sub para. 1d(2)(e), in which it is stated: ". . . this regulation requires that applicable commanders and heads of Army agencies. . . assure that . . . the procurement of contract support services conforms to applicable laws and regulations, including regulation [sic] of the Civil

hand, if the services are determined by the contracting officer to be "non-personal" he is free to proceed to the second step in the problem-solving process: should the services by done by contractor personnel or by in-house operation?

In this second portion of the decision-making process, various factors come into play. Theoretically, under Army Regulation 235-5 and Department of Defense Directive No. 4100.33, this second step in the determination is a weighing process in which, on one side of the scale, the oft-expressed presumption in favor of private enterprise reposes, waiting to test on the other side of the scale his arch enemies, the "compelling reasons"[152] one by one. Should any of these "compelling reasons" exist, it is sufficient to sustain the contracting

151 (Cont.)
Service Commission or other appropriate authority, and is not used as the basis for contract personnel procurement not authorized by law, or as a means of avoiding Government personnel or salary limitations."

152. Army Regulation No. 235-5, para. 5b (28 Nov. 1966) /hereinafter cited as AR 235-5/. This provision states: "The policy . . . (in favor of contracting out). . . establishes a presumption in favor of Department of the Army Procurement of services and products from commercial sources." The regulation lists the following "compelling reasons" for exception to the general policy in favor of contract-out:

1. "Procurement of a product or service from a commercial source would disrupt or materially delay an agency's program.

2. It is necessary for the Government to conduct a commercial or industrial activity for the purposes of combat support for individual and unit retraining of military personnel or to maintain or strengthen mobilization readiness.

officer's decision to initiate a "new start." In practice, the referenced Army Regulation, (which, along with D.O.D. Directive No. 4000.31 goes further in implementing Bureau of the Budget Circular A-76 than the circular itself demands) effectively requires cost analysis in nearly all cases.[153] Thus a cost analysis is required prior to initating a "new start,"[154] prior to continuing an existing in-house activity or converting to contract from in-house operation,[155]

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152. (Cont.)

3. A satisfactory commercial source is not available and cannot be developed in time to provide a product or service when it is needed.

4. The product or service is not available from another Federal agency nor from commercial sources.

5. Procurement of the product or service from a commercial source will result in higher cost to the Government." Id. para. 6.

153. The regulation cautions, however, that the last of the five compelling reasons, comparative cost advantage to the Government should be used as justification either for initiating a new start or continuing an existing operation only when none of the other four compelling reasons apply, ". . .because of the difficulty in comparing Government and commercial costs." Id. para. 6e (3).

154. Id. para. 9c.

155. Although para.13a(1) of the regulation states that a cost comparison is required only when the decision to continue in-house activities rests on the basis of relative cost, para. 8 of the same regulation, which requires periodic review of all Army commercial-industrial-type activities to determine whether an existing activity should be continued, curtailed or discontinued, states, in subpara. f(2)(a): "Before a final decision is reached to convert to a contractor performance, a comparison of cost will be made in accordance with section IV and will be audited by the U.S. Army Audit Agency."

and prior to contracting-out for a new service activity.[156] This requirement for cost analysis poses a major problem for the contracting officer, if he is aware of it.[157] Faced with a limited staff and information-collection resources, he is asked to make or have made a detailed, complicated and sophisticated analysis with inadequate and indefinite guidance.[158] The evaluation of such com-

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156. Id. subpara. 13a (2) and 13a(3).

157. ASPR, Section 22-102.1, places responsibility upon the contracting officer for assuring implementation of the Government's policy that Government employees must be hired within the prescriptions of the Civil Service laws and regulations and Classification Act requirements, that Department of Defense personnel ceilings must be observed (except where statute provides an exception), and that ". . . these laws and regulations. . . /are/. . . not circumvented through the medium of 'personal service' contracting. . . ." However, the author was able to find no directive, regulation or instruction which specifies who is to make the comparative cost analysis upon which so much importance has been placed by Bureau of the Budget and Department of Defense publications. Army Regulation 235-5, which implements D.O.D. Dir. 4100.15 and D.O.D. Instruction 4100.33 (and thus, B.O.B. Circ. No. A-76), places all responsibility for decisions regarding the establishment, continuation or curtailment of commercial and industrial activities on the "applicable commanders and heads of Army agencies" (para. 1d, AR 235-5, 28 Nov. 1966). The regulation makes no further delineation, however, of in-house vs. out-house decision-making responsibility, nor do procurement regulations require that such determinations be made prior to contracting for the supply or service.

158. Note that in specifying those situations in which cost comparisons are required (subpara. 13a) and those situations in which cost comparisons are not required (subpara. 13b), the regulation fails to cover all possibilities, resulting in ambiguity and ease of skirting the requirement for cost comparison. AR 235-5, subpara. 13a and 13b. Id. 15.

plicated costs as overhead, Federal taxes, depreciation, and military and civilian personnel salaries, requires substantially more definitive guidance than the generalities now offered.[159]

In addition to the problem of a required cost analysis which in all probability goes beyond the local ability to perform with accuracy, the contracting officer is faced with the subtle influences of the "real" world in which he makes his decisions. When the commanding officer receives a mission, that mission must be performed in "real time." Hence, when that mission includes a requirement for a new services activity not previously performed by the unit or installation, the commander exerts strong pressure on the contracting officer to acquire the capability within the time

159. Thus, under the heading "Overhead Costs," the contracting officer is advised, in determining overhead cost in Department of Defense commercial or industrial activities, to include" . . additional overhead costs that are incurred or will be incurred at the installation level if commercial procurement is not utilized. An equitable share of general overhead such as finance and accounting, personnel, legal, local procurement, medical services, receipt, storage and issue of supplies, police, fire and other services should be allocated to the function under study. In addition, overhead costs at the installation level for management, direction, and administration above the organization performing the function which are specifically related to the function, should be included as part of the Government operation costs. Include also any contract termination, lease cancellation, or other costs which may become due because commercial procurement is discontinued in favor of in-house performance." Id. subpara. 15b (10).

allotted. Whether an activity might more appropriately be done in-house or not, the contracting officer is most likely to take the path of least resistance and hence the least time-consuming: contracting-out.[160] The current cost analysis procedure provided for in Army Regulation 235-5 is, by necessity, time consuming and cumbersome. If the agency required to perform the cost analysis is not properly staffed for that function, or is not able to acquire (in the case of civilian personnel) sufficient personnel spaces to fulfill the requirement based on an in-house decision, in-house starts can easily be the victim of long delays.

This discussion brings up an important question: even when the decision is made that it is either a matter of military necessity or of relatively less cost to go in-house to perform the mission, is the existing personnel system geared to handle the change? The Civil Service Commission asserts that the Civil Service system can handle this personnel flux. In his 1967 opinion on the NASA technical services contracts, the General Counsel of the Civil Service Commission stated:

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160. As to one often-cited reason for contracting-out—to avoid personnel ceilings— the following observation was made by Mr. Louis I. Freed, staff Administrator of the Special Studies Subcommittee of the House Committee on Government Operations, during questioning of the Deputy Director, Bureau of the Budget, Mr. Phillip S. Hughes in hearings before that subcommittee in 1967 concerning support service contracts: "Aren't your personnel ceilings really sort of a deception,

"Generally, we either have or could readily provide examination coverage for the kinds of positions we have been able to identify as occupied by contractor employees." And, he went on, ". . . we see no reason why the Civil Service examining system cannot supply Goddard with the kind of people now working there under contract."[161] Further, in testifying before the House Subcommittee on Government Operations in 1967, Mr. John W. Macy, Chairman of the Civil Service Commission, stated: "I have a pride and a confidence in the civil service system, and I believe that it can perform effectively to meet needs, whether they are emergency or urgent or are routine, and I feel there needs to be a very careful consideration of all of the management factors before a decision is made to contract out for a particular function."[162] But, notwithstanding the responsiveness of the Civil Service recruiting program, consideration should be given

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160. (Cont.)
a paper deception? If we had personnel ceilings, on the one hand, and no ceilings via the personal service contract route, why should agencies feel if they have their programs, and they have got to get on with them, that they have to pay attention to ceilings? They can go via the contract route, and literally thumb their noses at you anyway." Hearings on Support Service Contracts Before a Subcomm. of the House Comm. on Government Operations, 90th Cong., 1st Sess. 55 (1967).

161. Opn. (1967), supra note 131, at 39.

162. 1967 Hearings, supra note 118, at 29.

to the agency's problem of obtaining personnel spaces. A decision to pursue an in-house course of action and the hiring of additional Civil Service personnel do not mean that sufficient personnel spaces can be obtained to permit those personnel to work at the job for which they were hired. Employment ceilings, determined annually by the President, are intended to be absolute limits. Hence, although agencies may request adjustment in their particular employment ceiling, no such adjustment may be obtained merely to provide for additional employment in a particular bureau or unit. Each agency is first expected to absorb an increase through an internal adjustment in the agency's ceiling distribution.[163]

And what of short-term service requirements? Even though it may well be cheaper to go in-house under a short-term requirement for support services, this may have serious adverse effects on the in-house personnel system, such as moving newly acquired civil servants to another location when the short-term requirement is complete, discharging them, or even "bumping" other Civil Service workers at the same installation who have less seniority. Conversely, it may well be less expensive to contract-out for a short-term service requirement, yet not permitted due to the rule pre-

163. Bureau of the Budget, Circ. No. A-64 (revised), Position management systems and employment ceilings, subpara. 4d (1965).

cluding contracting-out for personal services absent statutory exception. Clearly, the manpower management aspects of this decision-making process need to be considered if a responsive answer to an in-house vs. contracting-out question is to be made.

One might certainly ask the question: why do we contract-out even in those situations in which existing guidelines technically preclude our doing so? It has been suggested that as a practical matter, contract services have been utilized in such circumstances as (1) Lack of in-house capability; (2) to handle peak loads; (3) inability to recruit talent;(4) when contract personnel were believed to be less expensive than in-house personnel; (5) lack of adequate personnel due to manpower ceiling authorizations; and (6) it was more expedient to use contract personnel.[164] The author submits that, all too often, the real reason the contracting officer obtains support services by contract is that it is procedurally easier to do so than to initiate a "new start;" controlling regulations requiring cost analysis before contracting-out in most instances are sufficiently ambiguous to permit sidestepping their purported requirements, and

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164. Letter from Senator John L. McClellan, Chairman of the Senate Committee on Government Operations, to four Members of Congress from New Mexico, dated 7 Dec. 1966, contained in 1967 Hearings, supra note 118, at 9.

the contracting officer does not want to face the problem of having to obtain personnel spaces to support an in-house decision.

IV. ISSUES AND ALTERNATIVES

The ultimate issue in the frequent conflict between policy, administrative decision on "legality," and cost analysis is, of course, the one which initiated the entire controversy: to what extent should Government compete with private enterprise? Strangely, the Congress has failed to speak definitively on this major policy issue, although some consideration has been given by various Congressional committees[165] in the past to proposed legislation. Thus, the Senate Committee on Government Operations has considered

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165. For example, H. R. 9835, 83rd Cong., would have provided, as amended, ". . . for the termination, to the maximum extent compatible with national security and the public interest, of all commercial activities engaged in by the Federal Government in the United States which compete with private enterprise." The proposed statute ". . . declared it to be the policy of the Congress to encourage private competitive enterprise to the maximum extent compatible with the national security and the public interest; and that the Federal Government should not engage in business-type operations that are in competition with private enterprise, except where it is necessary in furtherance of national programs and objectives legally established." 1963 Committee Print, supra note 8, at 19.

numerous bills on the subject in every Congress since the 83rd. That Committee has always deferred final action thereon, however, mainly, due to repeated assurances from the Bureau of the Budget that legislation was not necessary since the policy contained in proposed legislation already existed in Bureau of the Budget pronouncements; and serious efforts were being made to prevent Government competition with private enterprise already, many of which had allegedly been successful.[166] Thus, this primary issue has effectively been answered by policy directives outside the lawmaking sphere. The spirit of the initial policy remains— private industry should provide goods and services to Government absent some conflict with the national interest. The evolvement of the requirement for cost analysis reflects the practical realization that it is normally in the nation's interest to obtain those goods and services at the lowest price.

A second important issue is: who can most effectively make the required comparative cost analysis and under what criteria should it be made? The contracting officer now has the responsibility for deciding whether services are personal or non-personal. Arguably,

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166. Senate Comm. on Government Operations, 90th Cong., 1st Sess., Staff Memo. 90-1-8 Appendix A (1967).

he should also be permitted to make the initial contracting-out vs. in-house decision. Cost analusis questions could be handled by him on a summary basis,using more definitive guidelines. The need for adequate guidelines is strong if the contracting officer is to make such a decision, since his ability to make an in-depth cost analysis is normally limited by virtue of his sparsely-staffed office. Under this concept, analysis which clearly shows cost benefit in favor of either in-house or out-house operation could permit the contracting officer to make the in-house vs. out-house decision, subject to subsequent review at a higher level within his agency. Close cases, on the other hand, would be immediately forwarded to a higher level within the agency staffed to make a thorough comparative cost analysis. An important part of this plan would be a guarantee to the contracting officer that, should he make an in-house decision, sufficient personnel spaces would be available and allocated to support that decision. Forcing the contracting officer to consider the availability of personnel spaces might very well influence his ultimate decision. Personnel space guarantees could be effected at the same agency level which makes complicated cost analyses for the contracting officer and reviews his summary cost determinations. Such a system would permit relatively quick decision-making in all but

the most complicated cost analysis cases. And ASPR, already being received by each contracting officer, is a ready vehicle for distribution of information to the in-house vs. out-house decision maker.

There is an alternative answer to the issue of who should make the in-house vs. out-house decision. Consider the nature of this decision. Arguably, it is a policy decision, and one which should be made at the agency's policy level. It is a question which calls for a critical weighing of values, many of which the contracting officer does not have sufficient resources to interpret or to comprehend. To cause the local contracting officer to make what is effectively a high-level policy decision may be unrealistic as well as unfair. Severe pressure from time-mission requirements will often cause him to compromise his position by choosing contracting-out as the only acceptable solution under the circumstances. These factors seem to suggest, as a viable alternative, a higher-level in-agency decision maker to determine the in-house vs. out-house question. Such an individual or body would not suffer the disability of subtle influences faced by the contracting officer, would have within its own level those resources sufficient to accomplish cost analysis requirements in the least amount of time and with the most accuracy, and could directly allocate personnel spaces to support an in-house

decision. This is not to say that the contracting officer could not serve a useful purpose under such a relationship, for he would surely act as the primary gatherer of facts at his level to assist the decision-maker in arriving at the decision. In addition to the higher-level in-house decision-maker and to assure the responsiveness of the Government personnel system in those situations in which an in-house decision is appropriate, an inter-agency committee might be established to review immediately agency decisions on urgent requirements, those concerning a large number of personnel or involving substantial sums of money, or other special situations which might arise. Such a group might properly include a member each from the Bureau of the Budget, which establishes personnel ceilings, the Civil Service Commission, which has concern for the well-being of the system itself and the protection of the personnel laws, the General Accounting Office, which keeps surveillance on the system lest cost or legality be abused, and the Department of Defense or other agency making the personnel request. Such an inter-agency committee would hopefully be able to examine the problem quickly, and arrive at a timely solution which would be definitive to the extent that mission requirements could be completed just as quickly, efficiently and easily with in-house capabilities as with contracted-out personnel.[167]

167. Industry has advocated independent review of all decisions

The key to the problem seems to be "ease of mission accomplishment," at least in the absence of strict and specific requirements to the contrary.

Regardless of who makes the in-house vs. out-house decision, it is obvious that at least the Department of Defense decision-maker needs, under circumstances of necessity and short-time requirements, a statutory exception to the rule which prohibits contracting-out for personal services. A recent Congressional Committee Report notes:

> . . . it would appear that such agencies as DOD and NASA, often faced with manpower ceilings, difficulty or inability to recruit shortage-type technical personnel, and strict time schedules for the accomplishments of various phases of their respective missions, would require a measure of latitude and flexibility in personnel procurement. 168

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167 (Cont.)
to adopt in-house alternatives as opposed to contracting-out, but the Bureau of the Budget, the Government Accounting Office and the Department of Defense oppose this suggestion on the ground that ". . . it is not feasible, from an operating standpoint, to subject numerous day-to-day transactions to a central review by agencies not acquainted with the circumstances." 1968 Committee Print, supra note 106, at 40. The suggested inter-agency committee, however, would have neither disability claimed. Not only would it have members on the committee from all agencies acquainted with the circumstances plus those with authority to correct deficiencies, but also it would not review all decisions, but only those with special circumstances.

168. 1968 Committee Print, supra note 106, at 11.

Current Department of Defense directives also recognize the need for this provision.[169] Such an exception could be included as an amendment to 5 U.S.C. 3109 b, which now permits contracting-out for expert or consultant services.

V. CONCLUSION

Clearly, the initial policy expressed by President Eisenhower in 1954 proclaiming Government's preference for private industry and asserting Government's desire to avoid economic confrontation with private enterprise has been weakened by evolving procedures requiring cost analysis prior to making a decision to initiate or continue in-house operation and by rulings of the General Counsel of the Civil Service Commission and Comptroller General that certain services can be performed only by Government employees. During this evolution no designation of the in-house vs. out-house decision-maker has been made, nor have clear criteria upon which to base the decision-making process been specified.

Hence, the author has offered several alternative solutions to this dilemma, in the hope that some constructive progress might be made toward realistic contract vs. in-house decision making:

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169. Notes 142 and 143, supra, and accompanying text.

1. The in-house vs. out-house decision-maker should be affirmatively designated and given adequate definitive criteria upon which to base this decision.

a. The decision-maker could well be the contracting-officer, authorized to make summary cost-analyses in all but complicated cases, and backed up by personnel space guarantees by higher authority to support an in-house decision; or, in the alternative,

b. The decision-maker could be a higher-level in-agency body, equipped to handle both in-depth comparative cost analysis and agency-personnel space allocation, with the contracting officer serving primarily as a gatherer of facts for the decision-maker.

2. Congress should assist the decision-maker by providing a statutory exception to the prohibition against contracting-out for personal services in situations of necessity and short-time requirements.

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Articles