



EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET
WASHINGTON, D.C. 20503

April 24, 2006

M-06-13

MEMORANDUM FOR HEADS OF EXECUTIVE DEPARTMENTS AND AGENCIES

FROM: Clay Johnson III
Acting Director

SUBJECT: Competitive Sourcing under Section 842(a) of Public Law 109-115

The purpose of this memorandum is to remind agencies of the requirements in section 842(a) of the Transportation, Treasury, Housing and Urban Development, the Judiciary, the District of Columbia, and Independent Agencies Appropriations Act, FY 2006, P.L. 109-115. Section 842(a) addresses the use of public-private competition to convert activities from government to contractor performance. A copy of the provision is provided at Attachment A.

Section 842(a) prohibits, with limited exceptions, an executive agency from converting work performed by more than 10 federal employees to private sector performance absent a showing, through competition, that performance by a contractor would be less costly to the agency by an amount that equals or exceeds the lesser of \$10 million or 10 percent of the personnel-related costs associated with performance by the agency's most efficient organization (MEO). An agency is precluded under section 842(a) from converting work to private sector performance if this differential is not met, even if the agency can demonstrate that private sector performance would provide a superior solution, when both cost and quality considerations are taken into account. The requirements of section 842(a) apply to competitions that use funds appropriated in an FY 2006 appropriations act.

Attachment B describes the applicability of section 842 and its effect on the procedures of Office of Management and Budget (OMB) Circular A-76. Agencies should carefully review both Attachments A and B to ensure that covered competitions are conducted consistent with section 842(a).

In passing section 842(a), Congress requested that OMB evaluate the effect of this section "on the Federal government's ability to obtain value for the taxpayer, both in terms of cost and quality, through the use of competitive sourcing." The Conference report accompanying P.L. 109-115 states that this information will be considered by the Conferees in deciding whether section 842(a) should be continued in FY 2007.

OMB has reviewed agency data on public-private competitions conducted over the past two years where the agency considered both cost and quality in the selection of a provider –

referred to as a cost-technical “tradeoff.” This review indicates that agencies have used tradeoff authority in a strategic and responsible manner.

OMB has concluded that the restrictions in section 842(a), which require agencies to select between the government and a private sector provider on the basis of cost alone, would likely deter private sector offerors from developing and submitting innovative proposals that could substantially improve the quality of agencies’ activities in a cost-effective manner. Over the past two years, competitions that have considered both cost and quality in the selection of a provider have encouraged private offerors to propose, and enabled agencies to achieve, transformational improvements which would not have been possible if the competitions had been narrowly restricted to considering only cost. Thus, as a result of the prohibition in section 842(a) on considering cost-technical tradeoffs, taxpayers may not receive the full benefit of public-private competition.

OMB plans to seek the repeal of section 842(a) and has prepared a report to Congress addressing the adverse impact of this provision. Agencies planning competitions to be announced in FY 2007 that may benefit from the use of cost-technical tradeoff source selections are encouraged to continue with such planning efforts and to consult with OMB.

Questions regarding this memorandum may be referred to Mathew Blum, Associate Administrator for Competitive Sourcing, Office of Federal Procurement Policy (OFPP) at (202) 395-4953. Consultations regarding potential cost-technical tradeoff competitions may also be directed either to OFPP or to your OMB contact. I appreciate your attention to this matter.

Attachments

Section 842(a) of Public Law 109-115¹

SEC. 842. (a) Requirement for Public-Private Competition-

(1) Notwithstanding any other provision of law, none of the funds appropriated by this or any other Act shall be available to convert to contractor performance an activity or function of an executive agency, that on or after the date of enactment of this Act, is performed by more than 10 Federal employees unless--

(A) the conversion is based on the result of a public-private competition that includes a most efficient and cost effective organization plan developed by such activity or function; and

(B) the Competitive Sourcing Official determines that, over all performance periods stated in the solicitation of offers for performance of the activity or function, the cost of performance of the activity or function by a contractor would be less costly to the executive agency by an amount that equals or exceeds the lesser of--

(i) 10 percent of the most efficient organization's personnel-related costs for performance of that activity or function by Federal employees; or

(ii) \$10,000,000.

(2) This paragraph shall not apply to--

(A) the Department of Defense;

(B) section 44920 of title 49, United States Code;

(C) a commercial or industrial type function that--

(i) is included on the procurement list established pursuant to section 2 of the Javits-Wagner-O'Day Act (41 U.S.C. 47); or

(ii) is planned to be converted to performance by a qualified nonprofit agency for the blind or by a qualified nonprofit agency for other severely handicapped individuals in accordance with that Act;

(D) depot contracts or contracts for depot maintenance as provided in sections 2469 and 2474 of title 10, United States Code; or

(E) activities that are the subject of an ongoing competition that was publicly announced prior to the date of enactment of this Act.

¹ Section 842(b) states that “nothing in Office of Management and Budget Circular A-76 shall prevent the head of an executive agency from conducting a public-private competition to evaluate the benefits of converting work from contract performance to performance by Federal employees in appropriate instances.” Circular A-76, as revised in May 2003, provides procedures and policies to conduct public-private competitions for work that is currently performed by the private sector. The provisions are similar to those applied to competitions for work currently performed by Federal employees that may be converted to performance by a contractor.

Effect of Section 842(a) of Public Law 109-115 on OMB Circular A-76

Section 842(a) of P.L. 109-115 prohibits, with limited exception, an executive agency from converting work performed by more than 10 federal employees to private sector performance absent a showing, through competition, that performance by a contractor would be less costly to the agency by an amount that equals or exceeds the lesser of \$10 million or 10 percent of the personnel-related costs associated with performance by the agency's most efficient organization (MEO). Section 842(a) requires several temporary adjustments to Office and Budget (OMB) Circular A-76. These adjustments and exemptions from the requirements of section 842(a) are discussed below.

1. Applicability of section 842(a).

The requirements of section 842(a) apply to competitions that: (i) are publicly announced on or after November 30, 2005 and (ii) use funds appropriated in an FY 2006 appropriations act. Exceptions to the requirements of section 842(a) are listed in paragraph 3, below.

2. Temporary adjustments to OMB Circular A-76.

Agencies shall make the adjustments described below in applying Circular A-76 to competitions that are subject to section 842(a).

a. Standard competitions. Notwithstanding paragraph D.5.b(3) of Attachment B of the Circular, agencies shall not convert work currently performed by more than 10 FTEs to private sector performance unless the conversion meets the 10 percent / \$10 million cost conversion differential provided in section 842(a). This conversion differential is reflected on line 14 of the Standard Competition Form prescribed by the Circular.

b. Streamlined competitions. For streamlined competitions that involve work performed by more than 10 FTEs, agencies shall ensure the following requirements are met.

i. The agency shall base the agency cost estimate on an MEO. Notwithstanding section C.1.a of Attachment B of the Circular, the agency shall not base the agency cost estimate on the incumbent activity.

ii. The agency shall apply a 10 percent / \$10 million conversion differential to determine the adjusted total cost of private sector performance, notwithstanding the requirement in Section C.1.c of Attachment B and section D of Attachment C of the Circular that otherwise precludes application of this differential in streamlined competitions. Application of the conversion differential must be reflected in the agency's documentation of its performance decision. (Note: COMPARE, the costing software that calculates performance costs in accordance with the costing procedures of the Circular, will automatically add the conversion differential to the cost of performance by the non-incumbent source.)

iii. The agency shall not convert work to private sector performance unless the conversion is based on the acceptance of an offer from the private sector that results in meeting the 10 percent / \$10 million conversion differential. However, the agency may choose to continue agency performance of a commercial activity through the establishment of an MEO based on market research indicating that the private sector would not meet the cost conversion differential (i.e., the agency is not be required to obtain actual offers from the private sector to make this determination).

c. Determinations. Determinations required under section 842(a) may be made by the same personnel authorized by the agency to make performance decisions required by OMB Circular A-76.

3. Exemptions from section 842.

Section 842 does not apply to the following:

- a. Activities that are the subject of an ongoing competition publicly announced prior to November 30, 2005 in accordance with Paragraph B of Attachment B of the Circular.
- b. Competitions conducted by the Department of Defense (however, see 10 U.S.C. 2461, as amended by section 341 of P.L. 109-163, the Defense Authorization Act for FY 2006).
- c. The security screening opt-out program provided under 49 U.S.C. 44920.
- d. Functions included on the procurement list established pursuant to section 2 of the Javits-Wagner-O'Day Act (41 USC 47) or planned to be converted to performance by a qualified nonprofit agency for the blind or other severely handicapped individuals in accordance with that Act.
- e. Depot contracts or contracts for depot maintenance as provided in 10 USC 2469, 2474.
- f. Activities performed by 10 or fewer FTEs.