



Annual Privatization Report 2016

Federal Government Privatization

By John M. Palatiello

Edited by Leonard Gilroy

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A. Historical Context of Federal Privatization

Despite more than 80 years of debate, Congress has continually failed to enact legislation to codify a process to determine whether federal agencies should start and carry out commercially available activities, whether such activities should be exclusively left to the private sector, or whether a public-private cost comparison or competition should be conducted to determine the best provider.

In 1932, a special committee of the House of Representatives expressed concern over the extent to which the government engaged in activities which might be more appropriately performed by the private sector. The first and second Hoover Commissions expressed similar concern in 1947 and 1953, respectively. Formally known as the Commission on Organization of the Executive Branch of the Government, the Hoover Commissions recommended legislation to prohibit government competition with private enterprise. The closest Congress has come to enacting legislation establishing a policy and process for Executive Branch agency management of commercial activities was in 1954, when the U.S. House of Representatives passed, and a Senate committee approved, legislation to require the Executive Branch to increase its reliance on the private sector.

President Eisenhower issued Bureau of the Budget Bulletin 55-4 in January 1955 to assert Executive Branch authority and stall pending legislation. It included an administrative policy that:

... in the process of governing, the Government should not compete with its citizens. The competitive enterprise system, characterized by individual freedom and initiative, is the primary source of national economic strength. In recognition of this principle, it has been and continues to be the general policy of the Government to rely on commercial sources to supply the products and services the Government needs ... The Federal Government shall rely on commercially available sources to provide commercial products and services ... the Government shall not start or carry on any activity to provide a commercial product or service if the product or service can be procured more economically from a commercial source.

The Bureau of the Budget subsequently became the Office of Management and Budget, and “bulletins” became “Circulars.” OMB Circular A-76 succeeded Bureau of the Budget Bulletin 55-4, and the policy that the government should not compete with private enterprise remained through Democrat and Republican administrations until the provision was eliminated by George W. Bush in 2003.

The Federal Activities Inventory Reform (FAIR) Act, Public Law 105-270, was enacted in 1998, requiring each agency to inventory its activities. Lists of activities, with the number of positions associated with each, are classified as “inherently governmental” or “commercial” in nature. The law requires a “review” of the commercial activities, but neither that term, nor a process for such a review, has ever been enacted.

Today, the federal government has 2.6 million Executive Branch employees (excluding uniformed military and postal service). OMB estimates that among agencies covered by the FAIR Act, 1.12 million full-time equivalent (FTE) employees are engaged in performance of functions that are not inherently governmental. Thus, 43% of the federal workforce are in government jobs that are “commercial” in nature.

Federal employees are engaged in a wide range of commercial activities that have little to do with governing, including architecture, apparel, construction, debt and bill collections, campground operation, engineering, equipment repair and maintenance depots, film studios and theater management, food service and security, furniture, graphics, insurance, laboratories, landscaping, laundry and dry cleaning, pest management and wildlife control, manufacturing, mapping, meeting planning, marketing research, printing and chart production, public storage, recycling and waste management, surveying, tax preparation, travel planning, and zoology. The federal government is the nation’s largest banker, insurer, homeowner, landlord, utility provider, and bus, transit and passenger train operator.

In 2007—the last year for which data are available—OMB reported that 73% of public-private competitions were won by government employees. From 2003 to 2007, only 50,989 federal employee FTE positions were subject to competitive sourcing public-private competitions, out of a total federal workforce performing commercial activities of more than 1 million. Nevertheless, those competitions resulted in over \$7 billion in savings.

Only a relative handful of the 1.1 million commercial positions have been studied to determine whether government employees or private sector workers can perform these activities more effectively.

Studies on the impact of public-private competitions in the federal government have not been conducted in recent years. But historic data show OMB estimated savings from competition of 27% per full-time equivalent (FTE) studied, while the Center for Naval Analysis found average savings of 30%. A 30% savings applied to all 1.1 million commercial FTEs would amount to a total savings of as much as \$35 billion annually—regardless of whether or not a function is contracted to the private sector.

Such “competitive sourcing” requires government agencies to establish a “most efficient organization” (MEO) and compete their in-house MEO functions against the private sector. The program was *not* directed toward privatization, but to government efficiency. Historic data showed that, regardless of whether the activity stayed in-house or was contracted to the private sector, by first going through the MEO process, the taxpayer won regardless of the outcome.

The Reagan administration’s “Grace Commission,” also known as the President’s Private Sector Survey on Cost Control, recommended privatization of several federal activities and contracting out to private firms for certain support services in four separate reports, and the Clinton administration’s National Performance Review, or Reinventing Government, endorsed A-76 and urged Congress to lift restrictions on its application. In 1988, the Commission on Privatization appointed by President Reagan recommended privatization of hundreds of federal programs, activities and even complete agencies.

B. Recent Developments in Federal Privatization

Most of the potential privatization candidates are still on the government’s books today. Competitive sourcing initiatives and other efforts to utilize the private sector for functions performed by federal employees have been relatively minimal in recent years, as Congress has effectively halted competitive sourcing through earmarked restrictions. Since 2008, Congress has imposed a moratorium on the relevant administrative process, found in Office of Management and Budget (OMB) Circular A-76, which has guided this matter since 1955.

While efforts to repeal the moratorium have failed in the House of Representatives, the Senate earlier this year approved the National Defense Authorization Act (NDAA) for fiscal year 2017 (S. 2943). The bill includes a section that would repeal the temporary suspension of public-private competitions for Department of Defense functions. As this report is written, the bill is before a House-Senate conference committee to resolve differences, including this matter, as it is not included in the House-passed version. The House-passed Defense Appropriations Act for fiscal year 2017 (H.R. 5293) includes a section prohibiting funds to plan for, begin, continue, complete, process, or approve a public-private competition under the OMB Circular A-76. This, too, must be resolved in a conference committee.

Overall, privatization generated little fanfare in the federal government in 2015, but unlike so much else in Washington, some progress was quietly realized and accomplished. President Obama provided some optimism in his State of the Union address at the beginning of the year when he proposed expanding a program that encourages state and local governments to pay for infrastructure projects with public-private partnerships.

The so-called Qualified Public Infrastructure Bonds (QPIBs) would expand an existing financing tool that allows state and local governments to issue tax-exempt bonds to pay for public infrastructure projects managed primarily by private companies. However, the five-year highway and transit reauthorization bill, Fixing America's Surface Transportation Act (or "FAST Act"), was enacted in December without the QPIB proposal. Still, the FAST Act does expand the Transportation Infrastructure Finance and Innovation Act (TIFIA) program, which provides federal credit assistance in the form of direct loans, loan guarantees, and standby lines of credit to finance surface transportation projects. It authorized \$1.435 billion in capital over five years for TIFIA projects eligible for credit assistance, including passenger and freight rail, public transit, intermodal freight facilities, highways, and international bridges and tunnels.¹

In other federal government privatization news:

- The International Trade Administration (ITA) of the Department of Commerce began an outsourcing initiative affecting its information technology (IT) operations. "We are getting out of the network business entirely and out of the end user device business entirely," said Joe Paiva, ITA's chief information officer.² The use of private contractors for IT will help focus the agency's employees on its core mission, making it easier for U.S. companies to do business overseas, and to enforce trade law and policy. The private contracting includes networking and printing operations, as well as management of end-user devices such as cell phones and printers.
- While the basic allowance for housing (BAH) for military personnel was altered in 2015, the Pentagon's Military Housing Privatization Initiative, which began in 1997, continues to rely on partnerships with private developers to renovate, build, manage and maintain domestic military family housing. There are now 205,000 stateside privatized military housing units, including apartments, townhouses and single family homes. As a result, the only housing the military still owns within the United States is historic general officer quarters and small clusters of homes at small, remote bases where no private partners were attracted. It is estimated the program generated \$31 billion of private capital, leveraged by a government investment of \$3.4 billion, and the program is credited with solving the dual problems of a shortage and poor condition of base military housing.³
- The military is also realizing savings through energy savings performance contracts (ESPC). Under an ESPC, a private company pays the upfront costs of energy-saving or water-saving retrofits in exchange for making money from payments generated by energy cost savings over time. If the building doesn't save energy, the contractor doesn't get paid. This provides an incentive for the partners to make sure the technologies pay off. ESPCs are an increasingly popular tool for building

upgrades and renewable energy. In 2011 President Obama asked federal agencies to enter into \$2 billion worth of ESPCs; that amount is estimated to have doubled to almost \$4 billion in 2015.⁴

- The total federal real estate footprint has been reduced in recent years, the Office of Management and Budget reported during 2015. An Obama administration directive issued in 2013 required federal agencies to dispose of existing property before new property is acquired. “The policy was a success,” OMB Federal Controller David Mader wrote in a 2015 blog post.⁵ “Now federal agencies have frozen, reduced, or are on a path to freeze their baseline by the end of fiscal 2015.” Agencies reduced office and warehouse space by 21.4 million square feet since fiscal 2012, and in fiscal year 2014 alone the government disposed of 7,350 buildings, or about 47 million square feet of space, according to Mader.⁶ OMB reported annual federal operation and maintenance costs have been reduced by about \$17 million.⁷
- Government innovation has resulted in important technology development—the Internet being one of the most prominent. But commercialization of federal research has often been criticized as slow and cumbersome. To help this process, the Department of Energy announced the creation of an Office of Technology Transitions (OTT) to identify commercial applications for the agency’s research. The department spends more than \$10 billion annually on research through university partners and federally funded laboratories. The new OTT will work with industry and academia to expand the uses of this research and spur even more innovation in the commercial sector.
- Additionally, in early 2016 the First Responder Network Authority (FirstNet)—an agency established by Congress in 2012 to build, operate and maintain a communications network for around 60,000 public safety agencies in the United States—launched a procurement for the network, known as the Nationwide Public Safety Broadband Network. FirstNet is seeking private financing for half of this multi-billion dollar project. FirstNet plans to award a contract in November.

About the Author

John M. Palatiello is president of the Business Coalition for Fair Competition (BCFC, www.governmentcompetition.org) an organization that comprises trade associations, businesses, and organizations dedicated to free enterprise, relief from unfair government-sponsored competition, and maximum government reliance on the private sector. He is also president and owner of John M. Palatiello & Associates, Inc. (www.jmpa.us), a public affairs consulting firm located in Reston, Virginia providing government affairs and association management services to firms and organizations, with a specialization that includes the privatization market.

John has served as chairman of the Procurement and Privatization Council of the U.S. Chamber of Commerce, and currently serves on the Chamber's Small Business Council. He has also been a frequent witness before Congress on the need for reform to eliminate various forms of unfair government competition with private sector firms. He formerly served as executive director of America Moving Forward, an association of firms involved public-private partnerships ("P3s") for financing, building, and operating toll roads and other surface transportation infrastructure.

Endnotes

- ¹ U.S. Department of Transportation, "The FAST Act: Innovative Finance," <https://goo.gl/T9pvrb> (accessed August 8, 2016).
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- ⁵ David Mader, "A National Strategy for Reducing the Federal Government's Real Estate Footprint," The White House blog, March 25, 2015, <https://goo.gl/RMy9AN> (accessed August 10, 2016).
- ⁶ Ibid.
- ⁷ Ibid.