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Acquisition Reform

OFPP Issues Final Guidance on the Performance of Inherently Governmental Functions: We're on the Right Track, But Are We on the Right Train?



BY JOHN PRAIRIE

In September, the Office of Federal Procurement Policy (“OFPP”) issued its long-awaited final policy letter to provide to Executive Departments and agencies guidance on managing the performance of inherently governmental and critical functions. The guidance, which goes into effect on October 12, 2011, retains, without broadening, the existing statutory definition of an “inherently governmental function” and provides guidance to agencies regarding the circumstances under which it is appropriate to use contractors to perform functions “closely associated with inherently governmental functions” and “critical functions.”

The good news for the contracting community is that the final policy letter declined to significantly expand the list of functions that must be performed by government employees and provides agencies the flexibility to determine which functions can be performed by private industry consistent with their mission and operations. However, the policy lacks clear guidance regarding how agencies should determine which functions can, or should, be performed by government or contractor per-

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sonnel, or how to compare the costs of performance. As a result, it remains to be seen how agencies will choose to implement the OFPP’s guidance in practice and whether they will use their discretion in these areas to justify the arbitrary elimination of contractor positions to meet current budgetary realities. In short, while the OFPP’s final policy letter is a good start, the devil will be in the implementation details.

Background. The OFPP policy letter addresses direction to the Office of Management and Budget (“OMB”) in President Obama’s March 4, 2009 Memorandum on Government Contracting to clarify when governmental outsourcing of services is appropriate, consistent with section 321 of the Duncan Hunter National Defense Authorization Act (“NDAA”) for Fiscal Year 2009, Pub. L. No. 110-417. Section 321 requires OMB to: (i) create a single definition for the term “inherently governmental function” that addresses any deficiencies in the existing definition and reasonably applies to all agencies; (ii) establish criteria to be used by agencies to identify “critical” functions and positions that should be performed only by federal employees; and (iii) provide guidance to improve internal agency management of functions that are inherently governmental or critical.

The policy letter is issued against the backdrop of continuing debate over the government’s reliance on contractors. As the government’s reliance on service contractors has blossomed over the past ten years, Congress has grown increasingly uneasy with what is perceived as an “overreliance” on service contractors to

execute agencies' missions. In particular, they have expressed alarm at the prospect that private contractors may be performing "inherently governmental functions." As a result, both Congress and the Obama Administration have mandated that agencies take a closer look at the use of support contractors generally to determine whether certain contracted tasks are more properly performed by government employees. The contracting community, for its part, has raised concerns that in the rush to fulfill Congress' and the President's "in-sourcing" mandates, agencies may not carefully consider whether the government or the private sector has the best capability to perform the function and to provide the best value to the American taxpayer.

The Proposed Policy Letter. On March 31, 2010, OFPP issued a proposed policy letter, entitled "Work Reserved for Performance by Federal Government Employees," to clarify and provide guidance for Executive Branch agencies on determining what kinds of work should be performed by government employees instead of private contractors. The policy letter proposed to:

- Create a single definition of the term "inherently governmental functions" by directing agencies to adhere to the statutory definition of this term in the 1998 Federal Activities Inventory Reform ("FAIR") Act, Public Law No. 105-270, and eliminate variations of this definition found in other documents, such as the Federal Acquisition Regulation and OMB Circular A-76.

- Preserve a long-standing list of examples set out in FAR 7.503 of the most common inherently governmental functions, such as commanding military forces, determining foreign policy and awarding or administering contracts.

- Refine existing criteria (e.g., addressing the exercise of discretion) and provide new criteria (e.g., focused on the nature of the function), to help agencies decide if a particular function that is not identified on the list of examples is, nonetheless, inherently governmental.

- Require federal agencies to identify functions that are "closely associated" with inherently governmental functions and refine guidance requiring special management attention when contractors perform such functions to guard against their expansion into inherently governmental functions.

- Reiterate requirements in the 2009 Omnibus Appropriations Act (Pub. L. No. 111-8) to give special consideration to federal employee performance of functions closely associated with inherently governmental ones.

- Recognize a new category of work, "critical functions," defined as functions that are necessary to the agency being able to effectively perform and maintain control of its mission and operations.

- Require agencies to ensure that, for critical functions, they have an adequate number of positions filled by federal employees with appropriate training, experience, and expertise to understand the agency's requirements, formulate alternatives, manage work product, and monitor any contractors used to support the federal workforce.

Finally, the proposed policy letter would require agencies to take specific actions, before and after con-

tract award, to prevent contractor performance of inherently governmental functions and overreliance on contractors in the performance of closely associated and critical functions.

OFPP received public comments from more than 30,000 respondents on the proposed policy letter. Although respondents were generally supportive of the agency's efforts to clarify policies and management responsibilities with respect to the performance of inherently governmental functions, the comments reflected mixed reactions to the proposed guidance. Many respondents expressed concerns that the policy letter and the increased attention on having non-inherently governmental functions performed by federal employees would inappropriately discourage federal managers and agencies from taking full and effective advantage of the private sector and the benefits of contracting. Others cautioned against excessive outsourcing and recommended expanding the definition of an inherently governmental function to encompass critical functions and functions closely associated with inherently governmental functions.

To determine whether a function is inherently governmental, agencies must now evaluate, on a case-by-case basis, the nature of the work and the level of discretion associated with the performance of the work.

The Final Policy Letter. The final OFPP policy letter, issued on September 9, 2011, retains the definition of "inherently governmental function" that is included in the 1998 FAIR Act, which defines an activity as inherently governmental when it "is so intimately related to the public interest as to mandate performance by federal government employees." The policy letter also includes an illustrative list of 24 examples of inherently governmental functions. The list retains from the current FAR, among other things, combat and the provision of security under certain circumstances, the conduct of foreign relations, determining what supplies or services are to be acquired by the government, the awarding and termination of prime contracts, and the determination of budget policy, guidance and strategy.

To determine whether a function is inherently governmental, agencies must now evaluate, on a case-by-case basis, the nature of the work and the level of discretion associated with the performance of the work. Under the "nature of the function" test, agencies must examine whether the function "involves the exercise of sovereign powers of the United States," such as officially representing the United States in an intergovernmental forum or body, or arresting someone. If the function involves the exercise of U.S. sovereign powers, it can be deemed inherently governmental "without regard to the type or level of discretion associated with the function."

Under the "exercise of discretion" test, agencies must now evaluate whether a function: (i) requires the exercise of discretion "commits the government to a

course of action where two or more alternative courses of action exist and decision making is not already limited or guided by existing policies, procedures, directions, orders and other guidance”; (ii) can be performed by a contractor that “does not have the authority to decide on the overall course of action”; or (iii) performed by a contractor would “effectively preempt the federal official’s decision-making process, discretion or authority.” If an agency determines that a particular function is inherently governmental, it must, of course, be performed exclusively by federal employees.

The policy letter further provides that even though a function may not be considered inherently governmental, it “may approach being in that category because of the nature of the function and the risk that performance may impinge on federal officials’ performance of an inherently government function.” In such cases, the policy letter instructs agencies to give “special consideration to using federal employees to perform these functions.” If contractors are used to perform such work, agencies must give special management attention to contractors’ activities to guard against their expansion into inherently governmental functions. The policy letter, for the first time, includes examples of such closely associated functions, such as supporting budget preparation activities, providing support for development of policies, regulations or legislative proposals, and conducting market research or drafting statements of work in support of an acquisition.

The final policy letter also requires agencies to identify their “critical functions” to ensure that they have sufficient internal capability to maintain control over functions that are core to the agency’s mission and operations. Critical functions are those functions that are “necessary to the agency being able to effectively perform and maintain control of its mission and operations.” The criticality of the function depends on the mission and operations, which the policy letter acknowledges will differ between agencies and even within agencies over time. In making that determination, the officials must consider the importance that a function holds for the agency and its mission and operations. The more important the function, the more important that the agency have internal capability to maintain control of its mission and operations. The policy letter provides two examples of critical functions: (i) analyzing areas of tax law that impose significant compliance burdens on taxpayers for the Internal Revenue Service’s Office of the Taxpayer Advocate; and (ii) performing mediation services for the Federal Mediation and Conciliation Service.

Critical functions can be performed by either federal employees or contractors. When determining whether a critical function may be performed by a contractor, the agency must ensure that it has “sufficient internal capability to control its mission and operations” and that use of a contractor is cost-effective. The policy letter defines “sufficient internal capability” as generally having “an adequate number of positions filled by federal employees with appropriate training, experience, and expertise to understand the agency’s requirements, formulate alternatives, take other appropriate actions to properly manage and be accountable for the work product, and continue critical operations with in-house resources, another contractor, or a combination of the two, in the event of contractor default.”

In determining whether sufficient internal capability exists, agencies must consider, on a case-by-case basis, the: (i) agency’s mission; (ii) complexity of the function and the need for specialized skill; (iii) current strength of the agency’s in-house expertise; (iv) current size and capability of the agency’s acquisition workforce; and (v) effect of contractor default on mission performance.

While it is appropriate to provide agencies flexibility in assessing their internal capabilities and needs, the lack of clear guidance regarding what can and cannot be sourced to industry may lead to non-strategic, arbitrary insourcing.

The policy letter outlines a series of actions that contracting agencies must take both pre- and post-contract award. As part of acquisition planning, agencies must confirm that the services to be procured do not include work that must be reserved for performance by federal employees and that the agency will be able to manage the contractor consistent with its responsibility to perform all inherently governmental functions and maintain control of its mission and operations. This analysis must be included in the contract file.

Agencies must also review, on an ongoing basis, the functions being performed by their contractors, paying particular attention to the way in which contractors are performing, and agency personnel are managing, contracts involving functions that are closely associated with inherently governmental functions and contracts involving critical functions. Agencies must take prompt corrective action if they determine that a contractor is performing an inherently governmental function. If an agency determines that “internal control of its mission and operations is at risk due to overreliance on contractors to perform critical functions,” it must develop a plan to reduce reliance on contractors.

Finally, the OFPP policy letter outlines a series of steps that agencies must take to develop and maintain internal procedures to implement OFPP’s guidance. Agencies with 100 or more full-time employees must identify at least one senior official to be accountable for the development and implementation of these policies and procedures.

Impact on Contractors. The initial reaction of the contracting community to the final OFPP policy letter has been one of cautious optimism. Much to contractors’ relief, OFPP rejected calls to expand the current definition of inherently governmental functions in the final letter to include critical functions and functions closely associated with inherently governmental functions. The policy also appears to be well-balanced, at least on its face. Rather than encouraging agencies to reserve increasingly more work for performance by government employees, as the title of proposed policy suggested, the final policy largely allows agencies to decide for themselves which functions can be appropriately performed by private industry consistent with their mission and operations.

Of significance for contractors, OFPP emphasized at the outset of the policy letter that:

Nothing in this guidance is intended to discourage the appropriate use of contractors. Contractors can provide expertise, innovation, and cost-effective support to federal agencies for a wide range of services. Reliance on contractors is not, by itself, a cause for concern, provided that the work that they perform is not work that should be reserved for federal employees and that federal officials are appropriately managing and overseeing contractor performance.

Nevertheless, concerns remain regarding how agencies will implement the new OFPP policy in practice. The definitions of “critical functions” and “functions closely associated with inherently governmental functions” are not clear. While it is appropriate to provide agencies flexibility in assessing their internal capabilities and needs, the contracting community has expressed concern that the lack of clear guidance regarding what can and cannot be sourced to industry may lead to non-strategic, arbitrary insourcing of certain tasks currently being performed by contractors. In addition, though the policy letter makes clear that it is appropriate to use contractors to perform “closely associated” and “critical” functions where agencies have sufficient internal management capabilities, industry organizations, including the Professional Services Council, have cautioned that agencies may misconstrue the policy’s list of examples of closely associated functions as a “do not contract” list.

Of particular concern is the policy’s instruction that if an agency has sufficient internal capability to control its mission and operations, the agency should perform a “cost analysis” to determine if additional critical functions should be performed by federal employees or contractors. The policy letter explains that the cost analysis “should address the full costs of government and private sector performance and provide like comparisons of costs,” but provides no real guidance on how agencies should compare the actual costs of government versus contractor performance. In light of government agencies’ well-documented difficulties with performing such cost comparisons in connection with prior insourcing efforts, the lack of more concrete guidance in the final OFPP policy letter is a legitimate cause for concern for contractors. Indeed, with the new budget realities facing all Executive Branch agencies, including the Department of Defense, federal managers may use the

new OFPP policy to justify the elimination of contractor positions and tout illusory “savings” of taxpayer funds.

Another concern is the impact on small businesses, which have been particularly hard hit by the government’s recent insourcing initiatives. In an effort to “minimize the impact of these actions on small businesses,” the final policy letter instructs agencies to place a lower priority on reviewing work performed by small businesses where the work is not inherently governmental and continued contractor performance does not put the agency at risk of losing control of its mission and operations. Agencies should also consider whether they recently have failed to meet, or currently have difficulty meeting, their small business goals, including any of their socioeconomic goals. Agencies are instructed to involve their small business advocate if considering the insourcing of work currently being performed by small business. Nevertheless, it remains to be seen whether small businesses will fair any better under the OFPP’s new guidance regarding inherently performing functions than they did under the government’s prior attempts at insourcing.

In recent congressional testimony regarding the intelligence community’s use of contractors, OFPP Administrator Daniel Gordon predicted that the policy letter would not significantly diminish the federal government’s use of contractors. According to Administrator Gordon, many agencies, including the intelligence agencies, have already been informally following many of the principles laid out in the policy letter and this has not led to a significant shift away from the use of contractors. However, there is limited data available to support his claims in light of the classified nature of much of this work. Moreover, it is not clear whether agencies outside of the intelligence community have made any effort to implement the policy’s guidance.

Conclusion. By almost all accounts, the OFPP’s final policy letter regarding the performance of inherently government functions is a good start. Time will tell, however, how individual government agencies will choose to implement this policy to determine which functions can or cannot be performed appropriately by contractor personnel consistent with agencies’ missions and operations. This merits close monitoring and targeted advocacy.