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OMB Circular A-76: Explanation and Discussion of the Recently Revised Federal Outsourcing Policy

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Summary

The Office of Management and Budget has recently modified its Circular A-76, which governs the executive policy for the competition of commercial activities. This report provides a brief history of OMB Cir. A-76, a discussion of its place in the legal implementation of the Federal procurement policy, and a review of the main components of the Circular. Important for understanding the Circular is an understanding of the concepts of "commercial activity" and "inherently governmental activity." These two concepts will be emphasized in the discussion.

There are several bills pending in the 108th Congress which could affect the implementation of Circular A-76 generally, or as it would apply to a specific Department. These are: H.R. 2691, H.R. 2650 and S. 1363, placing limitations on the Secretary of Interior; H.R. 2658, placing restrictions on the Department of Defense; H.R. 2673, placing restrictions on the Secretary of Agriculture; and H.R. 2989, placing restrictions on the appropriations for the Departments of Transportation and Treasury and independent agencies (OMB is one of these independent agencies).

Background

Since the 1950's, it has been the stated policy of the Federal Government that Federal departments and/or agencies should not be in competition with the private sector. Since 1966 this policy has been expressed in the Office of Management and Budget's (OMB) Circular A-76. This Circular was substantially revised in 1967, 1979, 1983, 1991, 1999, and, most recently and most extensively, in May of 2003.[1] The 1999 amendment was

[1] This policy was first officially stated by the Bureau of the Budget in a directive issued in 1955. BOB Bulletin 55-4, January 15, 1955. This directive was subsequently amended in 1957 and 1960. The authority cited for issuing the Circular is the Budget and Accounting Act of 1921, 31 U.S.C. §§ 501 and 502, the Office of Federal Procurement Policy Act, 41 U.S.C. § 401 et seq, (continued...)

issued to bring the Circular into conformance with, and assist implementation of, the Federal Activities Inventory Reform Act of 1998 (FAIR Act).[2] In the early 1990's much of A-76 was incorporated into the Federal Acquisition Regulations (FAR).[3]

More particularly, OMB Circular A-76, along with its four attachments, sets forth guidelines and procedures for determining whether an activity should be performed in-house by the agency with Government personnel or whether it should be contracted-out to the private sector. OMB Circular A-76 establishes the Executive policy regarding the performance of "commercial activities" to be that the Federal Government should not be in competition with the private sector. The Government should rely on the private sector to supply the products and services the Government needs.[4] Attachment A contains the inventory process for categorizing all activities as commercial or inherently governmental. Attachment B sets out the process to be used for public-private competitions. Attachment C gives the rules for calculating the cost of these competitions. Attachment D supplies the definitions for the circular.

Generally the Circular applies to all executive departments and independent establishments. There are activities which are excepted as a class and there are situations where an activity which is not excepted as a class may be excepted by the Competitive Sourcing Official (CSO) because of the particular circumstances.[5] The two primary classes of activities to which the Circular does not apply are: activities specifically exempted by law; and activities which are inherently governmental in nature.

Inherently Governmental Activity and Commercial Activity

The primary exception to the policy of contracting-out pertains to an activity which is "inherently governmental." Past definitions have been quite general in nature and were accompanied by numerous examples.[6] The new A-76 takes a more specific approach in definition, but leaves out the lists of examples. The general approach to inherently

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[1] (...continued)
and Federal Activities Inventory Reform Act of 1998, Pub. L. 105-270. See CRS Report RL31024, *The Federal Activities Inventory Reform Act and Circular A-76*, and CRS Report RL32017, *Circular A-76 Revision 2003: Selected Issues*.

[2] Pub. L. 105-270, 112 Stat. 2382 (1998). The FAIR Act generally requires each executive agency to annually inventory its activities that are not inherently governmental and submit this inventory to OMB.

[3] *See*, 48 C.F.R. § 7.3. It should be noted that not all of the subsequent amendments to A-76 have been incorporated into the FAR. Therefore, A-76 and the FAR provisions are not identical. The current proposed modifications are to A-76, not the FAR.

[4] OMB Circular A-76, § 4.

[5] OMB Circular A-76, § 5a. The Department of Defense CSO is given discretion as to the applicability of the Circular to the Department in times of declared war or military mobilization.

[6] *See*, for example, the FAIR Act, Office of Federal Procurement Policy Letter 92-1, and OMB Cir. A-76, § 6 (1999).

governmental activities is, also, significantly altered under the revision.[7] The level of discretion required to make a function inherently governmental has been significantly raised. Under the modified circular only activities requiring " **substantial** official discretion in the application of governmental authority and/or in making decisions for the government" would be considered inherently governmental.[8] The revised Circular A-76 states:

> An inherently Governmental activity is an activity that is so intimately related to the public interest as to mandate performance by Government personnel. These activities require the exercise of substantial discretion in applying Government authority and/or in making decisions for the Government. Inherently Governmental activities normally fall into two categories: the exercise of sovereign Government authority or the establishment of procedures and process related to the oversight of monetary transactions or entitlements. An inherently governmental activity involves:
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> (1) Binding the United States to take or not take some action by contract, policy, regulation, authorization, order, or otherwise;
>
> (2) Determining, protecting, and advancing economic, political, territorial, property, or other interests by military or diplomatic action, civil or criminal judicial proceeding, contract management, or otherwise;
>
> (3) Significantly affecting the life liberty, or property of private persons; or
>
> (4) Exerting ultimate control over the acquisition, use, or disposition of United States property (real or personal, tangible or intangible), including establishing policies or procedures for collection, control, or disbursement of appropriated and other Federal funds.[9]

Congress has specifically, by statute, declared certain activities or functions to be "inherently governmental" in the context of OMB Circular A-76.[10] In making these

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[7] Although, the biggest change, the proposed requirement that Agencies would presume that all activities are commercial in nature unless an activity is justified as being inherently governmental, was dropped from the final version of the Circular. *See*, 67 Fed. Reg. 69769 (Nov. 19, 2002).

[8] OMB Circular A-76, Attachment A, § B(1)(a). (Emphasis added.).

[9] *Id*.

[10] *See*, e.g. The Volunteers in the Parks Act of 1969, Amendments, Pub. L. No. 98-540, 98 Stat. 2718, 98th Cong., 2nd Sess. (1984), which declared that regulation and management of natural resources on Federal lands are inherently Government functions and should be performed by Federal employees; the Water Resources Development Act of 1990, Pub. L. 101-640, § 314, 104 Stat. 4605, 4641, 101st Cong., 2nd Sess. (1990), codified at 33 U.S.C. § 2321, which declared the operation and maintenance of hydroelectric power generating facilities at Corps of Engineers water resources projects are to be considered inherently governmental; and the Government Performance and Results Act of 1993, Pub. L. 103-62, 107 Stat.285, 103rd Cong., 1st Sess. (continued...)

declarations, Congress does not appear to have expanded the scope of "inherently governmental" beyond that of the Circular. These declarations are not inconsistent with OMB Circular A-76. For instance, the regulation and management of natural resources was one of the Circular's examples of the act of governing under the old Circular.[11] The intention of these provisions appears to be to require that a greater emphasis be placed on the purpose of the function or activity being performed as opposed to cost savings to the Government in making the decision as what should or should not be contracted-out and to give Congress more direct control of contracting-out in this area.

The revised Circular defines "commercial activity" as "a recurring service that could be performed by the private sector and is resourced, performed, and controlled by the agency through a contract or a fee-for-service agreement."[12]

The Legal Effect of OMB Cir. A-76

First it should be stated what this Circular is and what it is not. It is a statement of Executive policy. It is not a law or regulation, in the usual sense of the word.[13] The Executive Branch has cause to issue many types of regulations or, for lack of a better word, directives. These directives may be substantive in nature or they may be interpretive rules, general statements of policy, or rules of agency organization, procedure, or practice. In order to be found to have the force and effect of law, executive directives, be they executive orders, regulations, or OMB Circulars, must meet a two-pronged test. First, the directive must be the product of a Congressional grant of legislative authority, promulgated in conformity with any procedural requirements imposed by Congress. Second, it must be a "substantive" or "legislative type" rule affecting individual rights and obligations.[14]

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[10] (...continued)
(1993), which required the head of each Federal agency and the U.S. Post Office to develop and submit certain strategic plans, performance plans, and performance reports, declared the preparation and drafting of these plans and reports to be inherently governmental function only to be performed by Federal employees.

[11] OMB Circular A-76, § 6(e)(1) (1999).

[12] OMB Circular A-76, Attachment A, § B(2).

[13] There is no general statute which establishes the general policy for contracting-out by the Federal government in the civilian procurement sector. There is a statutory statement of policy in this area for defense procurement, 10 U.S.C. § 2462(a), which states:

> (a) In general. Except as otherwise provided by law, the Secretary of Defense shall procure each supply or service necessary for or beneficial to the accomplishment of the functions of the Department of Defense (other than functions which the Secretary of Defense determines must be performed by military or Governmental personal) from a source in the private sector if such a source can provide such supply or service to the Department at a cost that is lower (after including any cost differential required by law, Executive order, or regulation) than the cost at which the Department can provide the same supply or service.

[14] *Chrysler Corp.* v. *Brown*, 441 U.S. 281, 295-302 (1979). *See also*, *Morton* v. *Ruiz*, 415 U.S. (continued...)

The first prong of the test is based in the constitutional grant of all legislative power to Congress. The Supreme Court has stated;

> The legislative power of the United States is vested in Congress, and the exercise of quasi-legislative authority by governmental departments and agencies must be rooted in a grant of such power by Congress and subject to limitations which that body imposes.[15]

Therefore, if a directive is to have the force and effect of law, the underlying authority for the directive must have come from Congress.

For a directive to meet the second prong requirement, that the directive be "substantive" or "legislative type," it must be one which affects individual rights and obligations and it must provide meaningful standards susceptible to third party review. The Supreme Court has called the requirement for the creation of rights and obligations "an important touchstone for distinguishing those rules that may be 'binding' or have the 'force of law'."[16] If the directive does not create a right or obligation, the courts have nothing to enforce. If the directive is premised upon discretionary standards it provides no basis for, nor is it amenable to, judicial review.[17]

Although it is possible to imagine a situation where Congress authorizes the OMB to issue regulations to carry out specific legislation and OMB doing so in a substantive or legislative manner, this is not the usual background to an OMB circular. OMB is the President's principal arm for the exercise of his managerial functions.[18] It was intended as "a managerial tool for implementing the President's personnel . . . policies and not as a legal framework enforceable by private litigation."[19] This is to say that in the usual circumstance OMB circulars are issued upon executive authority, not legislative.

Courts have specifically held that OMB Circular A-76 does not have the force and effect of law.[20] The authority for this circular came from the President, not Congress.

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[14] (...continued)
199 (1974).

[15] *Id*. at 302. *See also*, *Youngstown Sheet & Tube Co.* v. *Sawyer*, 343 U.S. 579, 587-88 (1952)

[16] *Id*. at 302, citing, *Morton* v. *Ruiz*, 415 U.S. 199, at 235-36 (1974).

[17] *U.S. Dept. of Health and Human Services* v. *Federal Labor Relations Authority*, 844 F.2d 1087 (4th Cir. 1988). *See also*, *Defense Language Institute* v. *FLRA*, 767 F.2d 1398, 1401 (9th Cir. 1985), *cert. dis.*, 476 U.S. 1110 (1986).

[18] Reorganization Plan No. 2 of 1970, Message of the President, *reprinted in* 1970 U.S. Code Cong. & Ad. News 6315, 6316.

[19] *U.S. Dept. of Health and Human Services* v. *FLRA*, 844 F.2d 1087 at 1096 (4th Cir. 1988), citing, *Independent Meat Packers Ass.* v. *Butz*, 526 F.2d 228 at 236 (8th Cir. 1975), *cert. den.*, 424 U.S. 966 (1976).

[20] *See, U.S. Dept. of Health and Human Services*, v. *FLRA*, 844 F.2d 1087 (4th Cir. 1988) and *Defense Language Institute* v. *FLRA*, 767 F.2d 1398 (9th Cir. 1985), *cert. dis.*, 476 U.S. 1110
(continued...)

OMB Circular A-76 is a managerial document.[21] Even if A-76 could be found to pass the first part of the test, it has been consistently found not to be a "substantive" directive.[22] By its own terms A-76 does not create any enforceable rights in third parties.[23] The Circular is not amenable to third party review because it fails to provide justiciable standards. In short, it provides no "law" to apply.[24]

Current Legislation

There are several bills pending in the 108th Congress which could affect the implementation of the revised Circular A-76 generally, or as it would apply to a specific Department. Section 335 of H.R. 2691(Making appropriations for the Department of the Interior and related agencies for the fiscal year ending September 30, 2004) would prohibit the use of any funds appropriated by the bill to initiate any new public/private competitions. H.R. 2650 and S. 1363 would, also place limitations on the Secretary of Interior, prohibiting the study or implementation of any plan that would privatize, divest or transfer any activities associated with the mission, function or responsibility of the National Park Service. Section 8014 of H.R. 2658 (DOD fiscal year 2004 appropriation) would prohibit the use of funds appropriated under the bill for conversion of a function employing more than ten civilians to the private sector unless a most efficient organization plan has been developed. Title I of H.R. 2673,(Department of Agriculture fiscal year 2004 appropriation)states that no funds made available by this appropriation may be obligated for FAIR Act or Circular A-76 activities until the Secretary has submitted to the Committees on Appropriations of both Houses of Congress a report on the Department's contracting out policies, including agency budgets for contracting out. On September 10, 2003, the House passed H.R. 2989 (fiscal year 2004 appropriation for the Departments of Transportation and Treasury and independent agencies) with an amendment which prohibits the use of funds appropriated by the bill to implement the May 29, 2003 revision of OMB Circular A-76. The OMB is one of these independent agencies. Therefore, OMB could not spend funds to enforce the Circular if this legislation is enacted.

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[20] (...continued)
(1986).

[21] *U.S. Dept. of Health and Human Services,* at 1092.

[22] *Id.* The Third Circuit has found that some aspects of existing practice and procedure under OMB A-76 have been elevated to the status of law by statute. Even so, questions regarding its application involved managerial choices inherently unsuitable for the judiciary to consider. *American Federation of Governmental Employees, Local 2017* v. *Brown,* 680 F.2d 722 (3rd Cir. 1982).

[23] OMB Circular A-76 at § 7(c)(8), which states that it "shall not be construed to create any substantive or procedural basis for anyone to challenge any agency action or inaction on the basis that such action or inaction was not in accordance with" A-76. There are certain appeals authorized under the FAIR Act of A-76 cost comparisons.

[24] *U.S. Dept. of Health and Human Services,* v. *FLRA,* 844 F.2d 1087, 1096 (4th Cir. 1988), *Defense Language Institute* v. *FLRA,* 767 F.2d 1398, 1401 (9th Cir. 1985), *cert. dis.*, 476 U.S. 1110 (1986), and *American Federation of Governmental Employees, Local 2017* v. *Brown,* 680 F.2d 722 (3rd Cir. 1982). *But see, CC Distributors, Inc.* v. *United States,* 883 F.2d 146 (D.C. Cir. 1989).