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BEFORE THE

COALITION FOR COMMON SENSE

IN GOVERNMENT PROCUREMENT

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I am pleased to be here today to discuss with you the recently issued General Accounting Office report entitled, "[Applicability of] Service Contract Act ~~Should Not Apply~~ to Service Employees of ADP and High-Technology Companies."

The Service Contract Act of 1965 (SCA) was enacted by the Congress to provide labor standards protection to employees of contractors and subcontractors furnishing services to Federal agencies. The act applies when a contract's principal purpose is to provide services in the United States using service employees. It requires that covered service employees receive wages no less than the minimum specified under the Fair Labor Standards Act--currently $3.10 an hour--and that, for contracts exceeding $2,500, the minimum wages and fringe benefits be based on rates the Secretary of Labor determines as prevailing for service employees in the locality.

LABOR'S SERVICE CONTRACT ACT DECISION

Over the years the General Services Administration (GSA) and other Federal contracting agencies have awarded numerous contracts for the purchase or rental of supplies and equipment that included maintenance and repair services. In the past, Federal agency pro-

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curement officials, including Labor's own procurement staff, considered these contracts to be subject only to the provisions of the Walsh-Healey Public Contracts Act, because their principal purpose was the furnishing of supplies or equipment. However, on June 5, 1979, Labor notified GSA that the maintenance and repair service specifications of all contracts for the purchase or rental of supplies or equipment were subject to SCA, thereby requiring that such contracts include prevailing wage determinations issued by Labor.

Soon thereafter, several major automatic data processing (ADP) manufacturers publicly announced their refusal to bid on or enter into any Government contract subject to SCA coverage. Other firms appeared ready to follow suit. Recognizing the industry concerns, congressional and Federal agency pressures were brought to bear on Labor to exercise its authority under the act and grant an administrative exemption for the ADP, telecommunications, and other high-technology commercial equipment industries. On August 10, 1979, Labor granted a 90-day temporary exemption from SCA coverage, but only for ADP and telecommunications equipment purchase or rental contracts falling within the purview of the Brooks Act (Public Law 89-306). Specific contracts for maintenance and repair services only and those involving other high-technology commercial products were not covered by the temporary exemption.

At the end of the 90-day exemption period (November 8, 1979), the Secretary of Labor decided not to further extend the Department's exemption for the ADP and telecommunications industry. Since then,

the Labor Department has required that all bid or proposal packages and all contracts having maintenance and repair specifications must contain the applicable SCA provisions, including appropriate wage and fringe benefit rate determinations.

To minimize the initial impact of its decision and to buy time while appropriate wage and fringe benefit data could be gathered from the ADP industry, on November 30, 1979, the Labor Department issued an interim, nationwide wage determination covering ADP maintenance and repair services only. This determination accepted the currently paid wages and fringe benefits as being those deemed by Labor to be prevailing for such services in the ADP industry. Nevertheless, some major manufacturers continued to reject Government contracts subject to SCA coverage.

THE COMMITTEE'S REQUEST

Recognizing that Labor's SCA decision and the computer manufacturers' refusals to contract with the Government could have seriously affected the maintenance and repair of the Government's enormous inventory of computers--more than 14,300 as of September 30, 1979--many of which are critical to our national defense and security, on November 23, 1979, the Chairman of the House Committee on Government Operations asked the General Accounting Office to review Labor's decision to apply SCA to ADP and telecommunications products.

On January 29, 1980, Congressman Frank Horton, the Committee's Ranking Minority Member, requested that we broaden our study to cover other high-technology commercial equipment industries directly affected by Labor's June 1979 notification to GSA.

OJECTIVES, SCOPE, AND METHODOLOGY

Our review objectives were to:

--Determine and assess the rationale for Labor's June 1979 decision.

--Determine the cost and other impacts, if any, of Labor's SCA decision on both Government and contractor operations.

--Assess the merits of industry arguments that they should be exempted from SCA coverage.

--Assess the need for administrative and/or legislative actions to equitably resolve the various issues involved.

To assess the impact of Labor's SCA decision on Federal agency operations, we contacted 114 Federal contracting agencies located in 26 States and the District of Columbia. Our Federal agency contacts covered a wide range of programs and missions and included 51 defense installations, 42 installations involving 8 civilian departments, and 21 installations involving 7 independent agencies. On the basis of the information gained in our initial contacts, we made followup contacts at 2 locations and we visited 42 of the 114 agency locations to interview agency officials, review contract files, and gather pertinent documentation.

We also contacted or visited 18 companies that manufacture, sell, and service ADP or other high-technology commercial equipment, including 10 major companies supplying ADP equipment to the Federal Government, and several major trade associations, including the Computer and Business Equipment Manufacturers Association (CBEMA), the Scientific Apparatus Makers Association (SAMA), and the National Micrographics Association (NMA).

In addition, we interviewed key headquarters officials and obtained pertinent documentation from the Department of Labor's Employment

Standards Administration, GSA's Automated Data and Telecommunications Service, the Department of Defense, and the National Aeronautics and Space Administration.

The data we gathered were not based on a scientific random sampling of Federal agencies and contractors, but rather a judgment sample designed to illustrate the problems and impacts involved and to give the broadest possible coverage while making the most effective use of our available staff resources. However, because of our broad coverage of agencies, equipment locations, and manufacturers, we believe that the information developed is representative of what would be found natonwide if scientific random sampling techniques were used. In this regard, our judgment sample covered Federal agencies having 98 percent of the Government's computers, States in which 72 percent of the Government's computers are located, and manufacturers who provided 81 percent of the Government's computers.

LABOR'S DECISION INAPPROPRIATE

The Department of Labor contends that the act applies to all contracts, as well as any contract specification, whose principal purpose is to provide services through use of service employees. Labor's position relies on its interpretation of the act. While acknowledging that no remedial purpose will be served by applying SCA to ADP and other high-technology industries, Labor believes none is required since the act applies to contracts for all services provided to the Government by service employees. Accordingly, Labor has not made any studies of the impact of SCA on (1) contractors' recordkeeping systems, pay practices, employee assignment practices, and the costs of compliance or (2) Government operations if agencies are unable to acquire needed services.

We believe that Labor's position is not supported by the act's language and legislative history, by Labor's own regulations, or by its administrative manual. The Service Contract Act was not intended to cover maintenance services related to commercial products acquired by the Government. ADP, high-technology, and other commercial product-support service contracts, where Government sales represent a relatively small portion of a company's total sales, do not have the same characteristics, or incentives, for contractors to deliberately pay low wages to successfully bid on Government contracts.

Accordingly, Labor's application of the act to contractor services sold primarily in the commercial sector, such as provided by ADP and other high-technology industries, in our view, is inappropriate.

LABOR'S WAGE PROTECTION UNNEEDED

The industries' central argument, that the act's application to commerical product-support services is not needed, has merit. All of the 18 corporations we contacted stressed their belief that the act's intent was not to cover industries providing commercial product-support services to the Government at established catalog prices. Of these corporations, 17 presented convincing evidence through financial statements, payroll records, price catalogs, and other documents that the act should not apply because:

--Substantial quantities of their products and services are sold commercially at established catalog prices.

--Government business represents a small portion of their total business.

--Their field service technicians receive adequate wages under merit pay systems, thereby eliminating the need for wage protection.

The most significant force behind the act was the Congress' desire to eliminate "wage busting" and prevent payment of substandard wages to persons whose employment either totally or substantially depended upon Government contracts awarded solely on the basis of price competition. Industry contends, Labor officials acknowledge, and our review has confirmed, that wage busting is not a problem in these industries.

INDUSTRY COMPLIANCE WOULD BE COUNTERPRODUCTIVE AND COSTLY

The most serious concerns presented by the 18 corporations we contacted were that Labor's decision would eventually:

--increase the administrative burdens and operating cost of each corporation and

--hinder employee productivity and morale by disrupting merit pay systems and staff assignment practices.

In addition, several corporations stressed the inflationary impact Labor's wage determinations could have on the industries' wage rates.

One corporation said a new system estimated to cost almost $1 million would be needed to track data on employees servicing approximately 700,000 machines within the Government. This corporation also stated that, to maintain its merit pay system and still comply with the act, a separate work force would have to be created to service its Federal contracts. To do this, the corporation estimated it would incur developmental and implementation costs of more than $9 million--including the $1 million for a new data system--and annual recurring costs of $3.3 million.

Another corporation estimated that the cost to develop and implement new data processing systems and modify existing systems would be $1.5 to $2 million. A third corporation estimated the cost to design, develop, and install its system at over $1 million, with annual maintenance costs of $250,000.

Regarding inflationary impact, one corporation said the first-year impact on its field service technician wages would be $648,000. Another corporation estimated the impact at $12 million. A third and much larger corporation said the inflationary impact on technician wages would be $100 million the first year.

One major high-technology corporation uses varying salary groups, each with salary ranges for merit promotion, to provide geographic area differentials in salaries based on the cost of living in those areas. Corporate officials estimated the inflationary impact of SCA to be between $50 million and $100 million if their employees were paid at least the median salary rate reflected in two of their geographic areas.

Since issuance of our report, a fifth corporation has advised us that SCA prevailing wage determinations would produce a first-year inflationary impact on its service technician wages of almost $20 million.

Such increases in service technicians' wages would undoubtedly be reflected in future prices to customers for equipment maintenance and repair services.

IMPACT ON FEDERAL AGENCY OPERATIONS

As I mentioned earlier, to obtain information on the act's impact on Federal agency operations, we contacted 114 Federal installations. At 42 of these installations, contracting difficulties developed

because contractors refused to accept contracts subject to the act.

To minimize impact or avoid shutdown of programs and activities, agency contracting officials either awarded contracts during Labor's 90-day exemption period or circumvented the act by:

--Issuing numerous purchase orders valued under $2,500.

--Designating service technicians as exempt professionals.

--Exercising contract options, extending terms, or adding to the scope of existing exempt contracts, sometimes due to misinterpretation of instructions.

Some agencies that had previously contracted directly with vendors for maintenance services began issuing delivery orders against GSA's exempt fiscal year 1980 ADP schedule contracts.

Not all of these efforts were successful in minimizing the impact. For example, the Army Corps of Engineers in Vicksburg, Mississippi, had to shut down its $12 million computer system because the sole-source contractor would not accept a follow-on maintenance contract containing SCA provisions. The system is expected to be scrapped, and replacement computer services are being obtained from sources at much higher cost and considerable inconvenience.

Various Federal officials cited other impacts they believed would occur if maintenance and repair services under expiring contracts were discontinued and could not be renewed. Presently, however, many of the major corporations that have strongly objected to coverage under the act in any form appear willing to accept contracts containing Labor's interim wage determination, including GSA's proposed fiscal year 1981 ADP schedule contracts.

LABOR'S RECOGNITION OF INDUSTRY CONCERNS

The Department of Labor recognizes that (1) SCA prevailing wage determination rates, by their very nature, affect merit pay practices, (2) legitimate merit pay systems do exist in the industry, and (3) to the extent feasible, Labor should not permit its normal administrative practices under SCA to destroy those systems. Labor's November 30, 1979, interim wage determination, allowing the ADP industry to continue paying their service employees the wage rates and fringe benefits currently being paid, was a tangible recognition of Labor's desire not to disrupt or destroy industry merit pay practices.

Between December 1, 1979, and mid-June 1980, Labor attempted to issue a specific wage rate for entry-level field service technicians, based on the Bureau of Labor Statistics' reported median wage of Class C electronic technicians. Labor had hoped that this variance from its normal SCA wage determination practices would meet industry concerns while allowing Labor to carry out its SCA enforcement responsibilities. However, the industry opposed this effort. Moreover, industry data obtained during our review showed that application of Labor's proposed entry-level rate would have disrupted the merit pay and staff assignment practices of a large segment of the industry.

On June 17, 1980, Labor abandoned, at least temporarily, its proposed entry-level wage determination in favor of issuing a revised expanded version of the earlier interim wage determination covering maintenance services not only for ADP equipment but also for scientific and other high-technology equipment. Labor also issued a separate wage determination, also patterned after the interim determination, to cover

maintenance and repair specifications under GSA's Federal Supply Service schedule contracts for purchase or rental of automated office and business machines and related equipment. These latest actions, in our view, are a further indication of the difficulty of satisfactorily resolving the problem.

If the Labor/industry basic disagreement on the act's coverage is not permanently resolved, we believe the future impact on Federal agency programs and operations and on the affected industries could be severe.

RECOMMENDATIONS

Accordingly, we recommended that the Congress amend the Service Contract Act to make it clear that the act excludes coverage for ADP and other high-technology commercial product-support services.

Pending such action by the Congress and to avoid further serious impairment to the conduct of Government business, we recommended that the Secretary of Labor temporarily exempt from the act's coverage contracts and contract specifications for such services.

CURRENT STATUS OF ACTIONS ON OUR ISSUED REPORT

As you know, our report was issued to the Chairman, House Committee on Government Operations, on September 16, 1980. In publicly releasing the report a few days later, Chairman Brooks urged the Secretary of Labor to accept our recommendation for temporary exemption. He also expressed his hope that the Congress would write a permanent exemption into law. The Chairman has also asked the Secretary of Labor, the Administrator of GSA, and the Director, Office of Management and Budget, to submit formal comments on our

report. Those comments are still pending but should be released soon. In all probability, congressional hearings will be held early next year, but to our knowledge, no specific timetable for those hearings has been set.

In closing, I would like to thank Mike Timbers and the Coalition for inviting me to speak to this distinguished group and, at this time, I would be happy to respond to any questions you may have about our report.