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United States General Accounting Office 128510

**GAO**

Report to the Administrator, National  
Aeronautics and Space Administration

November 1985

**CONTRACTING OUT**

**NASA Not Complying  
With OMB Circular  
A-76**



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**National Security and International  
Affairs Division****B-220127**

November 27, 1985

The Honorable James M. Beggs  
Administrator, National Aeronautics  
and Space Administration

Dear Mr. Beggs:

During our survey of contract administration at the National Aeronautics and Space Administration's (NASA's) Lewis Research Center, we found that the Center contracted out functions such as instrument repair and graphic services, without comparing the contract costs to in-house performance costs. We later determined that NASA Headquarters, as a matter of policy, does not comply with the Office of Management and Budget (OMB) Circular A-76, which requires agencies to perform such cost comparisons. Thus, NASA has no assurance that needed services are being obtained in the most economical manner.

The NASA Associate Administrator for Management told us that NASA's current policy does not require cost comparisons before contracting out commercial-type activities, and it is unlikely that any of NASA's centers have done such comparisons. He also stated that NASA does not plan to implement such a policy because

- the high quality and experience of NASA managers makes such cost comparisons unnecessary,
- the preparation of a formal comparison is costly and disruptive to ongoing work, and
- the focus on cost would take emphasis away from achieving NASA's primary missions.

Additionally, the Associate Administrator stated that the research and development (R&D) exclusion in OMB Circular A-76 relieves NASA from having to perform cost comparisons for R&D activities.

OMB Circular A-76 established federal policy and procedures for determining whether activities should be performed by federal agencies or under contract. According to the Circular, the government shall not start or carry on any activity to provide a commercial product or service if it can be obtained more economically from a commercial source. One exception to contracting out is when an activity is so intimately related to the public interest as to mandate performance only by federal employees. Another exception is that the Circular does not apply to R&D.

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However, the Circular also states that severable in-house commercial activities in support of R&D are subject to the Circular.

The Circular also provides that federal agencies are to periodically review their activities that provide products or services that could be obtained from commercial sources. An activity performed by government employees is to be contracted out if a cost study shows that the contractor's cost is at least 10 percent lower than the government's in-house cost estimate. If the activity involves 10 or fewer government employees, a cost study is not required provided there is sufficient competition to ensure reasonable prices. Further, according to OMB, when personnel ceilings prevent the continuing of lower cost, in-house activity, the Circular directs agencies to request the additional spaces in their annual budget request. OMB requires agencies to report annually on their progress in implementing this Circular. The annual reports are to include such information as the results of the past year's cost comparisons and a review schedule for the agency's commercial activities.

We met with OMB officials to discuss NASA's noncompliance with the Circular and they stated that NASA had neither performed the cost comparisons nor submitted the annual reports required by the Circular. OMB's position is that NASA is subject to all provisions of the Circular, including the requirement to perform cost comparisons before contracting out commercial functions that are being performed in-house.

An OMB official clarified the Circular's applicability to R&D by stating that it was intended to allow agencies to maintain a core R&D capability in-house without requiring cost comparisons. However, if an agency believed it could contract out an R&D function without eroding its core capability, then a cost comparison would be required. In addition, support functions which are severable from the main R&D effort, such as security and maintenance, require cost comparisons.

OMB officials questioned NASA's noncompliance with the Circular during their ongoing dialogue concerning implementation of the President's Management Improvement Program. Since August 1984, OMB has repeatedly advised NASA that it must implement Circular A-76. While NASA refused to fully implement the Circular, OMB correspondence dated July 31, 1985, stated that NASA had agreed to analyze at least one function to assess the advantages or disadvantages of converting the function from civil service to contractor.

Since 1980 NASA's Lewis Research Center has awarded four contracts without performing A-76 cost comparisons for commercial activities that were formerly performed in-house by government employees. These contracts are currently valued at about \$13 million and include activities such as instrument repair and graphic services. Although some functions were contracted out concurrently with a reduction in authorized government employee positions, NASA did not, as required by Circular A-76, advise OMB whether the reductions in authorized staffing would result in higher costs through contracting out. We believe that NASA should have performed such cost comparisons and, if necessary, advised OMB of the higher costs. As it presently stands, neither NASA nor OMB can be assured that the functions are being performed in the most economical manner.

We requested and received comments on our draft report from NASA. (See app. I.) In his response, the Associate Administrator for Management emphasized that NASA has, since its inception, vigorously carried out the general policy inherent in Circular A-76, that commercial sources be relied on to supply the products and services the government needs. However, NASA agrees that it has not followed the procedural requirements of Circular A-76. The reasons cited include:

- Decisions about contracting out are based on management assessment of a variety of factors, including increased management flexibility and efficiency, changing workforce requirements, and lower total overall cost.
- While the cost of preparing a formal comparison is not prohibitive, it is very expensive and should be avoided if there are other alternatives.
- The adversarial process of an A-76 cost comparison focuses attention on a relatively small segment of the organization without regard to the efficiency and effectiveness of achieving the overall mission.

After we initially discussed NASA's policy with its headquarters officials, we followed up by asking Lewis Research Center officials for any kind of written material documenting its rationale for contracting out. Lewis officials stated that cost was a consideration but could not provide any evidence of it or any other alternative methods used to make its decision.

We believe that management decisions of the magnitude discussed here should include systematic consideration of cost to ensure that the most cost-effective decisions are reached. Circular A-76 procedures are intended to accomplish this objective, and therefore, we recommend that you implement the policy and procedures of OMB Circular A-76 requiring

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the performance of cost comparisons before contracting out in-house functions.

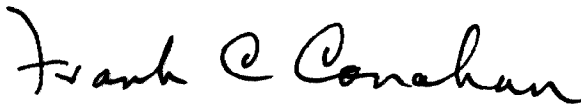
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During our survey, conducted between February and August 1985, we reviewed selected commercial service contract files at NASA's Lewis Research Center and provisions of OMB Circular A-76. We also discussed NASA's policy regarding the Circular with several NASA officials, including the Associate Administrator for Management, and several OMB officials, including the Deputy Associate Administrator for Policy Development, Office of Federal Procurement Policy. We conducted our work in accordance with generally accepted government auditing standards.

As you know, 31 U.S.C. 720 requires the head of a federal agency to submit a written statement on actions taken on our recommendations to the Senate Committee on Governmental Affairs and the House Committee on Government Operations no later than 60 days after the date of the report. A statement is also to be submitted to the House and Senate Committees on Appropriations with the agency's first request for appropriations made more than 60 days after the date of the report.

We are sending copies of this report to the Director, Office of Management and Budget; the Chairmen of the above-mentioned committees; and the Chairmen of the Senate Committee on Commerce, Science and Transportation, and the House Committee on Science and Technology.

Sincerely yours,



Frank C. Conahan  
Director



# Comments From the Associate Administrator for Management, National Aeronautics and Space Administration



National Aeronautics and  
Space Administration  
Washington, D.C.  
20546

Reply to Attn of: **NM**

OCT 17 1985

Mr. Frank C. Conahan  
Director  
National Security and International  
Affairs Division  
United States General Accounting Office  
Washington, DC 20548

Dear Mr. Conahan:

Thank you for the opportunity to comment on the GAO draft report entitled, "NASA Not Complying With OMB Circular A-76" (Code 392199).

Since its inception, NASA has relied heavily on the private sector for necessary goods and services to conduct its mission. In fact, there are indeed few Federal agencies that could claim the success that NASA can in its implementation of the A-76 tenet that, "...the general policy of the Government (is) to rely on commercial sources to supply the products and services the Government needs." NASA has in the past, and will continue in the future, to vigorously carry out this policy.

However, as the report states, NASA has not followed the procedural aspects of A-76, and thus is technically in "noncompliance." The reasons for this "failure" are rather inadequately stated in the report; we would consider the following more indicative of the NASA position:

- o NASA is an acknowledged leader in effective and innovative management. The success of NASA's management approach is clearly reflected in the corresponding success of the NASA high risk aerospace programs. Certainly, NASA management, as a long standing matter of policy and practice, does not contract out work without valid reasons to do so, such as lower total overall cost, increased management flexibility and efficiency, need to meet changing work force requirements, similarity among NASA institutions for the conduct of similar work, etc. Arithmetic cost comparisons are therefore just one element in the broad series of issues that must be considered in a decision to contract out work that is currently being conducted by in-house personnel.
- o The cost of preparing a formal comparison is expensive, and not only in the direct cost of conducting the study, but also in the diversions of manpower resources from program execution to the conduct of the study. Other costs include the overall lost productivity of the organization being studied (which can be significant), the great length of time necessary to conduct such studies, the potential opportunity costs of doing other management



Appendix I  
Comments From the Associate Administrator  
for Management, National Aeronautics and  
Space Administration

activities, and the inflexibilities of the A-76 process on prudent management actions during the time such studies are being conducted. NASA has a sound record of focusing on productivity improvement strategies which place employees, management and the American taxpayers in "win/win/win" situations. In short, looking at the "costs" based on the A-76 formula ignores many important factors necessary for efficient management. The cost of preparing formal cost comparison is not prohibitive, but in reality it can be very expensive and thus should be avoided if there are other alternatives available.

- o The conduct of an A-76 cost comparison, with all its procedural aspects, is an adversarial process which focuses attention on a relatively small segment of the organization without regard to the efficiency and effectiveness of the larger organization toward achieving its mission. At NASA, there is a great deal of attention placed on creating the most effective and efficient NASA/contractor team possible. To make work performance decisions on the narrow issue of relative costs of sub-elements of the organization would indeed seem to focus emphasis away from achieving NASA's primary missions, among which is the conduct of its business as efficiently as possible.

In summary, we believe that in the NASA context where the vast majority of work is already contracted out, reliance on the A-76 cost comparison formula would not provide any assurance that needed services are being obtained in the most economical manner possible. Clearly, NASA is supportive of the policy and principles espoused in A-76. However, the narrow procedural aspects of A-76 must be considered in light of the broad series of issues that come into play in making a decision to contract for services. As a result, NASA will follow the procedural aspects of that directive when it is clear that its application would provide meaningful assurance that the lowest overall cost is achieved.

Sincerely,

  
for C. Robert Nysmith  
Associate Administrator for Management



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