



PROJECT ON GOVERNMENT OVERSIGHT

Outsourcing Savings - Myth BUSTED!

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On September 13th, POGO released *Bad Business: Billions of Taxpayer Dollars Wasted on Hiring Contractors*. The report compares the cost of outsourcing work to contractors with the cost of using federal employees. For years, federal agencies have assumed that outsourcing work to contractors would reap the benefits of private sector efficiencies and save taxpayer dollars. Policy makers have debated the size of the government and whether federal employees are overpaid, often relying on studies that simply compare federal and private sector salaries.

However, those analyses have not recognized that the cost of outsourcing is not what the employees of contractors are paid by their employers, but rather the amount that the government pays to the employing private sector contractors. As a result, previous analyses did not reflect the fact that actual government contractor billing rates for federal service contractors are significantly higher than the full costs (salary and fringe benefits) of hiring federal employees. Rather than relying on data to compare federal and private sector pay, POGO's analysis took a closer look at the actual amounts paid by government agencies when they contract with federal service contractors.

POGO found that taxpayers are likely paying a cost premium for outsourcing services to contractors, as compared with having federal employees performing the work. We hope that our study alters the current debate and that it forces members of Congress and the public to ask for data proving that using contractors saves money. Given the nation's ongoing economic problems, this analysis has become even more necessary because approximately one-quarter of all discretionary spending now goes to service contractors – that is \$320 billion a year in service contract spending.

POGO is not alone in finding that contractors can be more expensive than federal employees. Recently, the Commission on Wartime Contracting (CWC) and the Defense Department issued reports that largely support our findings. The CWC found (see p. 226) that money could be saved in certain high-skill positions if the work was performed by federal civilian personnel. And, despite DoD's recent flip-flopping on insourcing, last week it released a report finding that 50 percent (see p. 5; full report) of its FY 2010 insourcing was conducted because the work could be "more cost effectively delivered by civilian personnel of the Department."

There has been some confusion about our inclusion of private sector compensation figures. Those figures are not intended to represent what any specific government contractor pays its employees. In fact, for the GSA schedule rates examined, we don't know what any contractor employee makes in salary and benefits (although one commenter stated it was typically about 1/3 of the billing rate). Simply stated, in far too many instances in government contracting, including under GSA schedule contracts, the transparency that supports the prices

paid to contractors (to include salary, benefits, overhead, and general and administrative costs, as well as profit) is simply absent. And, that's the way contractors like it.

The inclusion of private sector compensation data simply was meant to show that the federal government is paying its contractors, on an annualized basis, at rates that are significantly higher than either average public or private sector compensation rates. Our goal was to get people to end the typically misleading and inaccurate comparisons that look at public vs. private sector compensation – and focus instead on what the government is actually paying when it outsources work.

Since we released our report, there have been a number of mischaracterizations made by the contractor industry of our work. Below are a few of them, along with our responses:

- Industry Complaint: POGO unfairly used contractor loaded rates--rates that include salaries, benefits, administrative costs, profits, etc.
- POGO Response: We would love to see contractor cost or pricing data. If they would lay those cards on the table that would be wonderful. Unfortunately, the last seventeen years of so-called “acquisition reform” having been primarily about keeping important data away from government contract negotiators—data that would lead to better negotiation outcomes and more informed contract pricing. If rates are so much lower, as claimed by the Professional Services Council, than GSA should list both the ceiling prices and the *actual prices negotiated* to ensure that all government agencies are aware of current sales trends. But, what matters for the purposes of the current POGO report, is the cost to the government to contract with the company(ies) for the services studied. And that's what we analyzed.
- Industry Complaint: POGO's analysis was flawed because it did not include all government overhead and lifecycle costs for federal employees.
- POGO Response: All additional overhead was excluded, including the government's overhead rate to award, administer, and oversee contractors which would be in addition to the billing rates paid by agencies. If we added the government's overhead costs for federal employees, we would need to do the same for situations when the government used contractors to perform the work. Even assuming POGO had added the standard OMB A-76 12% “overhead” rate, this would not have changed the results of the study. Incidentally, we intentionally only used billing rates for contractors operating out of federal government facilities to more closely keep our comparison apples – to apples.
- Industry Complaint: POGO did not include pension costs.
- POGO's response: Yes, we did. We added OPM's and BLS's full fringe benefit and pension percentages. In fact, all personnel related fringe benefits were included in the government compensation data.
- Industry Complaint: POGO is not considering the short-term nature of many government contracts.
- POGO's response: That's because that isn't generally true anymore. In fact, many GSA schedule contracts extend for multiple years and cost taxpayers millions of dollars. Furthermore, POGO pointed out in our report that the government should more fully exercise its existing authority to hire temporary federal employees (5 CFR Part 316 for competitive service and at 5 CFR part 213 for excepted service appointments). Moreover, the “short-term” argument is a red herring. Even if true, it still does not justify the yearly cost of outsourcing billions of hours of work to contractors. All those hours worked by contractors can be translated into personnel FTEs, and it is those FTEs that matter, because that is what is being paid for on a gross basis, not some specific piece of work that may be relatively short term in nature.

- Industry Complaint: POGO ignored superior contractor education, experience, and skills.

- POGO's response: We would dispute this characterization as would the statistics available from the U.S. Office of Personnel Management, which seem to support the conclusion that the typical federal employee is better educated and has more experience than his/her non-Federal counterpart. Also, given that so many government contractor employees are actually retired federal employees, this argument has a number of obvious weaknesses.

- Industry Complaint: POGO's analysis is based on averages and improper costing models that have been criticized by the Center for Strategic and International Studies (CSIS).

- POGO's response: While CSIS and the contractor industry claim cost models outlined under Circular A-76 are flawed because it favors government employees, federal employee unions claim that the A-76 model favors contractors. We take some comfort that both sides believe that cost model favors the other. POGO will work with Congress and the Office of Management and Budget to create a system that fairly and accurately reflects all government costs. Furthermore, POGO's report also incorporated cost comparison models used by DoD (DTM-09-007), which also use averages.

- Industry Complaint: POGO did not mention outcomes.

- POGO's Response: In fact, we cite a few government studies that explain how outcomes and performance should always be a factor in deciding to insource or outsource—that's called accountability!

POGO received one call from a government official who reminded us that hiring 10 contractor employees to work for three months might require the agencies and Congress to reevaluate staffing restrictions. Who knows - in the long run, a government employee, or two, might work fewer hours and cost taxpayers a lot less money than those 10 contractor employees.

Another government official emailed me stating that it is time for contractors (and I think GSA too!) to "fess up that the GSA schedule prices are outrageously high!"