

# Government Contracts Blog

Posted at 7:36 AM on June 14, 2010 by Sheppard Mullin

## **Federal "In-Sourcing": New Rules For Inherently Governmental Functions**

By [W. Bruce Shirk](#) and [Jessica M. Madon](#)

On March 31, 2010, the Office of Federal Procurement Policy (“OFPP”) issued a proposed rule implementing the Federal Activities Inventory Reform Act of 1998 (“FAIR Act”), 31 U.S.C. § 501. *See* 75 Fed. Reg. 16188. The essential purpose of the FAIR Act is to “provide a process for identifying the functions of the Federal Government that are not inherently governmental functions” and to that end requires all government agencies to conduct inventories of their activities to determine whether they are commercial or “inherently governmental.” The FAIR Act defines “inherently governmental function” as “a function that is so intimately related to the public interest as to require performance by Federal Government employees.” The proposed policy is intended to implement this broad definition by promulgating a meaningful definition of work which is “inherently governmental” and a policy outlining when work must be reserved for federal employees, *i.e.*, when the functions in question are “inherently governmental.”

We think that the question of what constitutes an inherently governmental function is an important one and that, in this instance, OFPP has produced an arguably creditable first draft of a policy to address a very difficult subject. That said, many people—even some who spend their working lives “Inside the Beltway”—find the subject of what constitutes an “inherently governmental function” to be at best dull—and efforts to discuss the topic with denizens of the Federal City often elicit a dismissive response along the lines of “Who cares?”. Nevertheless, some do care, if only because they are forced by circumstances to do so. That happened to members of the House Permanent Select Committee on Intelligence who just three years ago reported they were “concerned that the Intelligence Community does not have a clear definition of what functions are ‘inherently governmental’ and, as a result, whether there are contractors performing [sensitive] inherently governmental functions.” H.R. Report No. 110-131, at 42 (May 7, 2007). The Founders worried about it too—discussions in the Federalist Papers written by James Monroe, Alexander Hamilton and John Jay evidence “[c]oncern about which federal agency activities are inherently governmental … [and] … what functions are appropriate for the federal government to exercise.” GAO *Government Contractors; Are Service Contractors Performing Inherently Governmental Functions?* GAO/GGD 92-11 (November 1991) at 2.

### *Difficulty of Defining “Inherently Governmental”*

The problem with development of a workable policy is, of course, that defining the term “inherently governmental” with precision is extremely difficult. As demonstrated by the very broad formulation set out in the FAIR Act, Congress minimally provides that a function “so intimately related to the public interest” as to be “inherent” is one that requires the exercise of discretion in applying Federal Government authorities, the making of value judgments in decisions for the Federal Government, and the interpretation and execution of laws.

The difficulty of precise definition is one reason that OFPP’s March 31<sup>st</sup> issuance is its second effort to implement the FAIR Act’s inventory requirements. The first of these efforts was set out in Attachment A to OMB Circular A-76 and was insufficiently specific to be capable of systematic application and thus of little practical value to agencies attempting to conduct their required inventories. The proposed policy promises to be more useful, clarifying the definition of “inherently governmental function” by providing specific examples and, as well, identifying a new category of “critical functions” that are critical to an agency’s core mission and operation and which are either “inherently governmental” or so close to it that they bear constant scrutiny by the agency responsible for their performance. In this regard, the proposed policy is designed to identify which governmental functions must always be performed by federal employees and which agency functions are so critical to the agency’s core mission that the agency should consider using only federal employees to perform those functions.

### *Inherently Governmental Functions*

The proposed policy would elaborate on the FAIR Act definition by identifying certain specific types of activities as indicative of performance of an “inherently governmental function”:

- Binding the U.S. to take or not take some action by contract, policy, regulation, authorization, order, or otherwise;
- Determining, protecting, or advancing U.S. economic, political, territorial, property, or other interests by military or diplomatic action, civil or criminal judicial proceedings, contract management, or otherwise;
- Significantly affecting the life, liberty, or property of private persons;
- Commissioning, appointing, directing, or controlling officers or employees of the U.S.; and
- Exerting control over the acquisition, use, or disposition of the property, real or personal, tangible or intangible, of the U.S., including the collection, control, and disbursement of appropriations and other Federal funds.

On the other hand, under the proposal policy “inherently governmental functions” would not include:

- Gathering information for or providing advice, opinions, recommendations, or ideas to Federal Government officials; or
- Any function that is primarily ministerial and internal in nature.

In applying the above definitions, agencies are to consider the “nature of the function” to be performed and whether an exercise of discretion will be involved when applying the “inherently governmental” definition. If the function involves the direct exercise of sovereign power, then it must be performed by a federal employee. Similarly, if the function involves an exercise of discretion that would bind the government to a course of action, then it too must be performed by a federal employee.

Agencies are currently required to make written determinations that a proposed contract will not include the performance of inherently governmental functions. The proposed policy would further direct agencies to determine that they have enough internal resources to manage and control the contractors and take action where “internal control of mission and operations is at risk due to inappropriate or excessive reliance on contractors to perform critical functions.” The proposed policy would also require agencies to review existing contracts “to ensure the scope of the work or the circumstances have not changed to the point that inherently governmental authority has been transferred to the contractor.”

#### *Closely Associated Functions*

The proposed policy lists numerous examples of functions that are “closely associated” with inherently governmental functions that, while not statutorily prohibited from being outsourced, do require additional oversight. These closely associated functions include evaluating another contractor’s performance, assisting in contract management and any situation that might permit access to confidential business information. The proposed policy states a clear preference that federal employees perform such closely associated functions. If an agency chooses to outsource these functions, it must prepare a written determination that (i) the function is closely associated with an inherently governmental function, (ii) private sector performance of this function is appropriate and most cost effective for the agency; and (iii) the agency has sufficient internal capacity to effectively manage the contract. The agency must also establish contractual guidelines in the contract regarding the contractor’s decision-making, assign a sufficient number of qualified federal employees to administer contract, and avoid or mitigate conflicts of interest.

#### *Critical Functions*

Finally, the proposed policy addresses those functions that are “critical” to an agency’s mission and operation. Critical functions are those functions that form the core of the agency’s mission

and if performed incorrectly would cause mission failure. The proposed policy requires agencies to maintain “a sufficient internal capability to control its mission and operations,” and toward this end agencies must reserve a certain portion of the work for federal employees. If a critical function is not inherently governmental, it may be performed by a contractor, but only when it is cost-effective to do so.

#### *Additional Requirements*

The proposed policy also requires agencies to clearly identify contractor personnel in email and phone systems, office name plates, and badges. And it makes the somewhat impractical suggestion that contractor personnel should be physically separated from federal employees and work off-site whenever possible.

Agencies will also be required to conduct Strategic Human Capital Planning to ensure the agency has internal capacity to perform its critical functions, retain institutional knowledge, and manage contractors.

#### *Industry Comments*

As we’ve noted, this draft policy is a noticeable improvement over previous efforts but it has a number of serious shortcomings. For example, and as the Council of Defense and Space Industry Associations (“CODSIA”) notes in its June 4<sup>th</sup> comments on the proposal, the proposed policy’s underlying tone is “adversarial” – suggesting the separation of contractor and government personnel whenever possible being an excellent example of that tone. CODSIA has also made a number of specific suggestions for enhancement of the proposed policy, including:

- Changing the title of the policy letter to “Management of Inherently Governmental and Critical Functions.”
- Combining the category “functions closely associated with inherently governmental functions” with the category “critical functions.”
- Prohibiting the use of any definitions, categories of functions, or criteria used by agencies to determine work to be performed by government employees in policy or guidance that does not conform to the OMB policy letter.
- Using the term “critical position” for individual billets that, while not inherently governmental, must be occupied by government employees in order for the agency to maintain control of its mission and operations. Clearly articulate the criteria to be used by agencies in making critical position determinations.
- Requiring agencies to submit their list of inherently governmental and critical functions and list of critical positions, with the rationale for the determination, to OFPP. To ensure consistent application of this policy, develop and maintain a public database of functions and positions. Periodically audit agencies to verify that each is applying the criteria

appropriately.

- Fully integrating comprehensive manpower and human capital planning and cost considerations into agency determinations about these “critical functions.”

It is also important for OFPP to address those areas where out-sourcing is proper and encouraged. As pointed out by the Industry Logistics Coalition (“ILC”) in its May 21<sup>st</sup> comments, the policy should make clear that performance based acquisition and public-private partnerships continue to be appropriate acquisition methods.

A final version of this policy is expected to be published in the fall.

Authored by:

Jessica M. Madon

(202) 469-4919

jmadon@sheppardmullin.com

and

W. Bruce Shirk

(202) 741-8426

bshirk@sheppardmullin.com