

STATEMENT OF
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“Putting the Strategy in Sourcing: Challenges and
Opportunities for Small Business Contractors”

SUBCOMMITTEE ON CONTRACTING AND WORKFORCE
COMMITTEE ON SMALL BUSINESS
UNITED STATES HOUSE OF REPRESENTATIVES

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Chairman Hanna, Ranking Member Meng and members of the subcommittee, thank you for conducting today's hearing and for the invitation to share the Professional Services Council's (PSC) views about the potential impacts on small businesses of the federal government's strategic sourcing efforts. This is a matter of significant interest to PSC given both the unique diversity of our membership base and the equally unique diversity of the services our members provide to the federal government.

Introduction

PSC is the nation's largest association of companies providing services of all kinds to the federal government. Our membership of nearly 360 companies is comprised of firms of all sizes, including approximately 25 percent that are classified as small businesses in their fields, and an additional 25-30 percent that would be classified as smaller mid-tier firms—those companies that occupy the exceptionally challenging portion of the market in which they are no longer eligible for treatment as a small business and must now compete in the unrestricted federal procurement market.

It is this diversity of functions and sizes that provides the lens through which we view strategic sourcing initiatives. In all of our work, our goal is to provide input and insights to both the legislative and executive branches on a wide array of business policies and how they will impact all, or portions of, the federal services sector. Since services now accounts for almost 56 percent of the contract spending at the Defense Department and closer to 75 percent in the civilian agencies, it is essential that the government fully understand and assess the ways its actions and policies will affect the marketplace of firms that are so critical to the government's operations. Indeed, the government's goal should be to foster an environment of robust competition, high performance, agility, innovation, balanced opportunities for companies of all sizes, and accountability. It is with those objectives in mind that we approach federal procurement policy issues like strategic sourcing.

Proper Use of Strategic Sourcing

We strongly support the premise that the government should be using strategic sourcing, in the truest meaning of the term which encompasses a universe much larger than the Federal Strategic Sourcing Initiative (FSSI), for the vast majority of its procurements. If structured properly FSSI has the potential to deliver real benefits for federal agencies and taxpayers alike. As such, we commend the Office of Federal Procurement Policy for making strategic sourcing a priority and we support how many agencies have properly applied these techniques to specific sourcing opportunities. Yet, while we fully support the FSSI's intended objectives, we have significant concerns about its practical effects. Those concerns relate more to the way in which the term is used and understood and how the initiatives are implemented across the government than to the concept itself.

Strategic sourcing is not one "thing." It is a set of multi-layered, flexible procurement strategies that evolve and change depending on the nature and complexity of what is being bought. For pure commodities, strategic sourcing can be fairly simple and straightforward; for more complex needs, particularly higher-end services, the challenges and complexities grow substantially. For products, where place of performance or production is irrelevant, there are often plenty of options for small business utilization; for services, where place of performance is very relevant, the need to deliver services over geographic regions as one way of reducing overall costs poses a number of challenges to balancing the efficiencies of strategic sourcing with the goal of appropriate reliance on small businesses. In some cases, when basic quality may be adequate, price becomes the principal driver; in other cases, quality is of greater importance, and is as important, or more important, than price.

What Are the Objectives of Strategic Sourcing?

We must first come to a common agreement on the ultimate objectives driving strategic sourcing in the federal market. If the objective is solely and specifically to optimize government operations, that will drive one set of responses. If, however, the objective is to optimize government operations without impacting current socio-economic or other acquisition policy goals, then additional considerations must be taken into account. These questions are more than rhetorical and both can lead to perfectly rational, yet different conclusions. They go to the heart of today's hearing and to the heart of a number of other elements of federal acquisition policy and practice.

For example, is it better to have fewer small businesses receiving a higher volume of work from the government or a larger number of small businesses with a smaller share of the volume? After all, if the government were to optimize its use of strategic sourcing, as the term is understood and applied throughout the commercial world, the former is the more likely outcome, as we have already seen with the federal strategic sourcing of commodities such as office supplies.

The same questions are raised when it comes to the government's objective of conducting full and open competitions for its procurements. Under the GSA Schedules, for example, there is a broad array of suppliers that can be easily accessed by any government customer. Almost by definition, strategic sourcing will reduce the number of those suppliers. In the commercial world, that is the norm. As the Government Accountability Office (GAO) noted in its April report on the use of strategic sourcing in the commercial sector, companies often carefully conduct market research on industry capabilities, select one or two suppliers and stick with them, and manage them aggressively for many years.¹ But in the government environment, constant competition is a central tenet of the procurement process and expanding the breadth of firms capable of competing for federal work is a continuous goal.

Any evaluation of strategic sourcing must also take into account the impact on the industrial base, since limiting private sector participation in federal procurements has the potential to erode portions of the federal industrial base. When only a few companies are awarded contracts under a strategic sourcing initiative and dozens, if not hundreds, of companies are excluded from regularly competing for opportunities, how will the depth and breadth of the supplier base be affected? This dynamic is generally of less concern when the sourcing is of commodities since, by definition, they tend to be more widely available and the barriers to market entry are modest. But it becomes far more pronounced when the services being procured through strategic sourcing are complex or highly technical, involve capabilities and skills that are in short supply across the economy, and for which opportunities outside of government are plentiful.

These dynamics are important considerations. The objectives of the federal strategic sourcing initiative, and the level of support for retaining it in its current form or expanding it to additional commodities and services, will hinge on policymakers' ability to agree on the objectives of the initiative and the policy trade-offs that are willing to be made.

¹ "Strategic Sourcing: Leading Commercial Practices Can Help Federal Agencies Increase Savings When Acquiring Services;" GAO-13-417, 04/15/13. Available at: <http://www.gao.gov/products/GAO-13-417>

The Key Question

This statement provides our perspective on these concerns and seeks to establish a framework for the ongoing debate around the key question of today's hearing: will strategic sourcing harm small business?

In the end, the answer to that question comes back to the desired outcomes of the initiative and how we measure success. Today there is no consensus on the answer to this question, either in Congress or across the agencies. For some, the most important goal is to reduce government costs and increase quality only. For others, the goal is to reduce government costs and increase quality while doing no harm and engendering no changes to the current marketplace. Still others believe that, while efficiency is important, the government's first and foremost priority must be to protect its vital role in fostering small and small disadvantaged, veteran, woman-owned, or HUBZone businesses.

Each of these perspectives is valid. But the differences they reflect clearly underpin this hearing and other debate and discussion about strategic sourcing generally and the more focused FSSI specifically.

Thus, if I could define one desired outcome from this hearing, it would be to find a clear consensus on this key question so as to determine the future of strategic sourcing.

Will Strategic Sourcing Harm Small Business? It Depends.

It is impossible to say for certain whether federal strategic sourcing does, or does not, present a threat to the overall small business community. Clearly where companies sit in the marketplace drives their view of that question. But as the government moves away from the low hanging fruit of strategically sourcing commodity products and toward strategic sourcing of services, the evaluation of the risk to small businesses ultimately depends on the depth and sophistication of the government's understanding of strategic sourcing itself.

In other words, strategic sourcing, in the truest sense of the word, incorporates the full spectrum of procurement techniques outlined in the Federal Acquisition Regulation (FAR)—from lowest price, technically acceptable (LPTA) to full cost-technical tradeoffs, also known as "best value," and strategic sourcing's manifestations vary across that spectrum. This fact appears to be relatively well understood at the most senior levels of government and within the Strategic Sourcing Leadership Council (SSLC). But on the front lines, where the initiatives are actually implemented, that level of awareness and understanding is not overtly evident.

To many people across government, strategic sourcing is immediately translated into bulk buying to gain economies of purchasing scale—a far too simplistic interpretation of "real" strategic sourcing. Nonetheless, this perception is consistent with the disturbing and overwhelming trend we are witnessing in virtually every agency toward lowest price, minimally technically acceptable contract awards, even for complex requirements. Unless and until that limited knowledge and understanding is substantially reversed and acquisition workforce skills are meaningfully enhanced, the effectiveness of what could otherwise be a very smart and thoughtful initiative could well be sharply limited and its impacts, including but not limited to small business, could be negative.

This point also came through clearly in the GAO report on the use of strategic sourcing in the commercial marketplace. GAO reported that strategic sourcing is increasingly being used across the commercial sector for everything from basic commodities to sophisticated and complex services. But as

GAO also pointed out, the considerations that go into how strategic sourcing is implemented vary according to levels of complexity, risk and total cost. Similarly, GAO reported that, in the commercial sector, quality is often the most critical consideration, since the level of quality of a product or service can make or break a company. While that same philosophy is a fundamental underpinning of the FAR, recent surveys, including PSC's 2012 Biennial Acquisition Policy Survey,² have made clear that, across government, there is a growing default to lowest price awards in which quality is only a minor consideration. Likewise, grave concern exists among acquisition leaders and professionals about their workforce's current capabilities to do effective market research or conduct effective negotiations, two skills that are central to the development and implementation of an effective federal strategic sourcing effort.

GAO also identified another crucial differentiator between the way strategic sourcing is implemented in the commercial world and the way the federal government often operates—the way each defines “cost.” In the commercial world, cost is generally defined as the total enterprise-wide, life-cycle impact of the action. For example, when a company like Wal-Mart makes decisions as to whether to invest in a new logistics information system, their focus is not only on how much it will cost to build and operate that system, but also includes careful analyses of how that new system will impact productivity and efficiency elsewhere in the company, from asset visibility to stocking shelves in stores. Admittedly, that type of analysis can be very complicated but it is essential to understanding the full impact on their organization before implementing a strategic sourcing approach.

Too often in the government, however, “cost” is defined solely as the cost of the product or service being acquired, and is not viewed through that broader, more relevant, prism. Moreover, the very manner in which agency budgets are built can frequently inhibit the consideration of total cost. For example, when the Defense Department was beginning its effort to insource some work being performed by contractors, initial cost analyses only looked at the cost to the DoD component's budget, not the cost to the overall defense or federal budgets. In today's fiscal environment, with sequestration in place and even short-term budget clarity elusive, we see a wide range of cases in which immediate, highly localized cost reductions are being implemented even though they are likely to result in higher long-term agency-wide costs.

Another example is the OASIS procurement at GSA. One of the concerns that it has raised is that it is overly focused on driving down the unit cost of complex professional services and less so on overall value, quality and performance improvements. Indeed, some GSA officials stated repeatedly in public forums that the principal goal of OASIS is to drive down the labor hour costs of companies that provide complex, high-end, professional services. While reductions in hourly labor rates may or may not be justified in some areas, little was said about how OASIS would both drive efficiency and improve the quality of service. In both cases, small businesses were or would be disproportionately impacted by shortsighted efforts to drive down costs, as they typically have less ability to endure decreased margins driven by artificial price pressures than do larger firms—particularly for firms operating solely in the federal space.

² “The Balancing Act: Acquisition in an Unabated Crisis;” The 2012 PSC Acquisition Policy Survey, December 2012. Available at:

http://www.pscouncil.org/i/p/Procurement_Policy_Survey/c/p/ProcurementPolicySurvey/Procurement_Policy_S.a.spx?hkey=835b11ac-0fe7-4d23-a0e0-b98529210f7e

To GSA's credit, their extensive and continuous outreach to the private sector has been exceptional and it appears that they have taken to heart many of the comments that have been offered. Even while we await GSA's publication of the final OASIS solicitation and their explanation of how they reconciled competing policy interests, concern still exists as to how the competition and the implementation of the awards, which GSA has identified as part of FSSI, will play out.

The Road Forward

As I noted at the outset, PSC recognizes the potential benefits of the FSSI. We strongly support the initiative and applaud the creation of the Strategic Sourcing Leadership Council and the OMB memorandum that guides their work. However, we do have concerns that too rapidly expanding the FSSI can, and likely will, have deleterious impacts on both government and its supplier base, prominently including small business. Done right, strategic sourcing can be a win-win; done wrong, it is more likely to be a lose-lose.

Thus, we would make the following recommendations as the initiative moves forward:

- 1) Ensure the alignment of policy and programmatic objectives. There is little doubt about the effectiveness of recent strategic sourcing efforts for wireless services, laptops, and office supplies. But the question of whether the balance between the number of small business providers and the total dollars expended with small business is aligned with both the administration's and Congress's small business agendas is unclear. That alignment is essential to the effective and efficient expansion of strategic sourcing.
- 2) Develop and deploy the requisite training tools to the workforce without delay and require that all acquisition personnel involved in any specific strategic sourcing effort for other than the most basic commodities first complete the training.
- 3) Be highly judicious in the use of strategic sourcing for services, particularly for complex services. Moreover, require senior level (even up to the SSLC) review of significant strategic sourcing efforts for services to ensure the strategies being employed are clearly articulated and are not overly focused on simply forcing down labor rates at the expense of overall quality.
- 4) Pursue a flexible, rather than overly prescriptive, FSSI. Allow individual agencies some degree of flexibility to pursue their own, agency-unique, strategic sourcing initiatives and develop performance measures for both agency-specific and government wide initiatives that generate visibility into overall efficiencies, performance outcomes, small business impacts and other factors that will meaningfully inform the future shape, expansion and/or limitations of the FSSI.

Conclusion

Mr. Chairman, members of the committee, this hearing offers an important opportunity to discuss and explore a rapidly expanding government-wide initiative. The Office of Federal Procurement Policy, the SSLC, GSA and others are to be congratulated for their relentless efforts to ensure that federal agencies buy smart and buy well. That challenges to their work remain should come as no surprise. PSC is fully committed to working with them, and with you, to find the right balance and the best path forward for the government and the taxpayer in finding a clear consensus on the objective of the Federal Strategic

Sourcing Initiative; that consensus will then, in large part, drive and govern the future of the government's appropriate use of strategic sourcing.

I look forward to answering any questions you may have.