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Before the Congress of the United States
U.S. House of Representatives
Committee on Small Business
Subcommittee on Contracting and Workforce

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Insourcing Gone Awry: Outsourcing Small Business Jobs

Mr. Chairman and members of the Small Business Committee on Subcontracting and Workforce: It is an honor and a privilege to comment regarding recent legal developments on insourcing, their adverse impacts upon small business and job creation, and the lack of transparency in the process, particularly within the Department of Defense. More, specifically, I have been asked to provide you today with my insights into the recent decision by the U.S. Court of Federal Claims in *Hallmark-Phoenix 3, LLC v. United States*, No. 11-98C (Fed.Cl.) (May 13, 2011) ("*Hallmark* case"). In the case, the Court ruled that it lacks jurisdiction to review insourcing decisions by the federal government because private contractors are not within the "zone of interests" to be protected by the insourcing statutes at issue, namely 10 U.S.C. §§ 129a & 2463. Most troubling, the Court stated in footnote 24 of its opinion that "[w]hile some of the district courts in these [insourcing] cases have (correctly) concluded that they lack jurisdiction, it appears more accurate to say that no court has jurisdiction over suits such as these." While I do not agree that this pronouncement reflects the current state of the law and have challenged it, I am here to recommend legislative actions that I believe will eliminate any barrier to small business having their day in court with respect to insourcing. Simply stated, this should include:

1. Amending the definitions of "protest" in the Competition in Contracting Act ("CICA"), 31 U.S.C. § 3551(1) to provide that such includes: (F) Conversion of a function that is being performed by private contractors to federal civilian or military employee performance.

2. Amending 31 U.S.C. § 3551(2) to provide: (C) Prudential standing in a protest action is coextensive with interested party status.

3. Imposing a legislative moratorium on insourcing until the Obama Administration completes its evaluation of the impact of insourcing on small business, and the general overall cost savings (if any) of the insourcing initiative to date.

On May 5, 2011, the Congressional Research Service ("CRS") issued a report titled *Functions Performed by Federal Contractors: An Overview of the Legal Issues. See* www.fas.org/sgp/crs/misc/R41810.pdf. In this report, CRS opined that Congress could expand courts' jurisdiction over insourcing decisions, require that agencies issue guidelines that are more or less likely to be found legally binding under the Administrative Procedure Act, expand or limit direct-hire authority, impose or remove restrictions on federal employment of former contractor employees, or protect small businesses from the effects of insourcing. CRS noted pending legislation, the Freedom from Government Competition Act, S. 785, H.R. 1474, which would require a "public-private competitive sourcing analysis" and a determination that insourcing provides best value. *See* 53 GC ¶ 143. This report does an excellent job of pointing out the issues and highlighting that much more thought is needed in this area regarding the impacts of insourcing, especially as it relates to small business and their labor force. It may also be time to put on the brakes while these impacts are studied.

What has happened since the CRS Report was issued has made Congressional oversight and action even more critical. On May 13, 2011, the Court of Federal Claims issued its opinion in the *Hallmark* case. This was a bid protest that arose from an insourcing determination by the United States Air Force Space Command ("Air Force") relating to a small business contract for transportation and vehicle maintenance services. This is not an instance where we are dealing with inherently governmental functions, work that was historically done by federal civilians, or a poor contractor. One of my first actions as a procurement law advisor in Iraq in 2004 was to

issue an opinion saying that we cannot hire contractor mercenaries to guard convoys destined for military use in a combat zone. This is not Hallmark's contract. We're talking wrenches not weapons; paint not policy making. Hallmark has received excellent performance marks. And we also know that, despite their vague representations to the contrary, the Air Force will continue to outsource vehicle maintenance. So, the case is strong that early termination of Hallmark's contract is imprudent and contrary to statute and regulation. The applicable statutes were 10 U.S.C. §§ 129a and 2463, which together required the Air Force to use the "least costly" form of manpower, whether "military, civilian, or private contractor." Hallmark has asserted in this litigation that the government is indeed not using the least costly form of manpower and has not followed its own directives in several respects. The Air Force responded in Court that only Congress can question their conclusions and the manner in which their analysis was performed and the Court ultimately agreed. The matter is now on appeal to the Federal Circuit.

To add an interesting twist to this, the Court had issued an opinion in another case with a different judge that accepted jurisdiction over a similar insourcing case. The case was *Santa Barbara Applied Research, Inc. v. United* States, No. 11-86C (May 4, 2011) ("*SBAR* case"). The Court in the SBAR case decided simply that jurisdiction over a protest was coextensive with interested party status. Showing an economic interest in both SBARs and Hallmark's case sufficient for interested party status was certainly not difficult since they both had options remaining on their contracts and would continue to bid the work when it was time to bid again. The decision in the *SBAR* case was both simple and logical given the history of protests, so my recommendation here is for Congress to legislatively adopt the reasoning of the SBAR case to provide that jurisdiction is coextensive with interested party status. Before that occurs, however,

we should discuss a little about what the Court did in the *Hallmark* case and whether that makes any sense.

What was so surprising in the *Hallmark* case is how the Court went through a litany of arcane legal concepts in a seeming exercise to manufacture a host of legal hurdles to private contractors' challenge of insourcing. Ultimately the Court in the *Hallmark* case concluded that despite the plain language of 10 USC § 129a, Congress somehow intended to deny private contractors a judicial remedy. Even though Section 129a clearly and explicitly requires the Department of Defense to use private contractors if they are the least costly form of manpower, the Court reads this language out of context by saying that private contractors were not the intended beneficiary of the statute. In legal parlance, the Court decided that there was no "prudential standing" because private contractors are not within the "zone of interest" of the statutes. In other words, the Court decided that no one, other than Congress, can be relied upon to challenge an agency determination using other than the least costly form of manpower, even where, as here, substantial and judicially manageable questions exist. *Contra CC Distributors, Inc. v. United States*, 883 F.2d 146, 151-153 (D.C. Cir. 1989).

This stands in direct conflict with how 10 U.S.C. § 129a became law. The Court in *CC Distributors* found that there were no judicially manageable standards for the statute in question because it did not require either a cost comparison or use of the form of manpower that is "less costly." *Id.* 883 at 153-154. However, the Court went on to find that the underlying regulations required the Defense Department to use the "less costly" form of manpower and required a cost comparison when making the determination. The regulations here require the same comparison, and the statute, 10 U.S.C. § 129a, was changed the following year in 1990 to require the use of the "least costly" form of manpower (military, civilian, or private contractor) and an "apples to

apples" comparison. *Id.* at 152-154. This erased the prior gap in prudential standing, assuming one was required at all. The Court in the *Hallmark* case ignores these legislative facts and disregards the Court's contrary decision in the *SBAR* case, which properly dismissed the concept of prudential standing. The Court in the *Hallmark* also ignored that Hallmark's interests were clearly aligned with those of Congress in assuring that the "least costly" form of manpower is used.

Ultimately, it is the decision of Congress whether to allow challenges to insourcing by private contractors. Secretary Gates has wisely put a freeze on federal civilian hiring and the Army's Secretary has required all insourcing actions be approved at his level. Internally, the Department of Defense recognizes that it has not addressed all of the impacts. I spoke personally with the decision-makers at the Air Force after the insourcing of Hallmark's contract was announced. They conceded that they had not considered the impact to either small business or the impact to the union labor force that worked for Hallmark. We note here that part of the basis for Hallmark's protest was that the Air Force had not met all legal constraints, including those designed to protect small businesses. Congresswoman Jackson-Lee of Texas recently commented on this case and the impropriety of the Defense Department competing with small businesses for other than inherently governmental functions. *See* Congressional Record p. H3624-25, May 25, 2011). This statement is more than just a "sense of Congress;" it is statutory policy. *Accord* 10 USC Sec. 2304e (prohibiting competition between DoD and small business). Perhaps it is time the Defense Department be required to consider these things before they do further damage the small business contractors through insourcing.