

PUBLIC WORKS AND GOVERNMENT SERVICES CANADA

AUDIT AND REVIEW BRANCH

PRELIMINARY SURVEY REPORT

1999-643

**Review of Minister's Accountability
for Alternative Service Delivery Contracting**

Audit and Review Committee Approval

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* Information has been withheld pursuant to the provisions of the Access to Information Act.

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Executive Summary

Authority for the Project

This review was approved by the Audit and Review Committee (ARC) as part of the 1999/2000 Audit and Review Plan.

Objectives

To examine the Minister's accountabilities related to contracting for Alternative Service Delivery (ASD) contracts and to examine the extent to which ASD contracts and supporting mechanisms are in keeping with these accountabilities.

Background

The public sector in Canada, like public sectors in other countries around the world, has been undergoing a period of structural change and renewal. Strong forces, including debt and deficit pressures, increased global competition and information technologies, have been driving these changes. As an important part of the government's strategy for *getting government right*, in 1995, the Treasury Board issued a framework for alternative program delivery to provide departments with strategies, principles and criteria to promote client-oriented, affordable and innovative government services.

Scope

This preliminary survey focuses on one of the Alternative Service Delivery (ASD) arrangements - contracting out - where the government transfers the operation of, but not the responsibility for a function, to a private sector contractor for a specific period of time by means of a contractual arrangement. As the government's procurement arm, Public Works and Government Services Canada (PWGSC) has been called upon to provide procurement services for those alternative program delivery arrangements that are contractually based.

All work was carried out at Headquarters and confined to those ASD projects managed by Supply Operations Service Branch (SOSB). Major Crown Projects and Repair and Overhaul contracting were excluded from the review.

Key Findings

Contracting out for an ASD requirement occurs after the Government has made its decision to contract out, for the first time, services which were traditionally provided by public servants.

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Although there are a number of distinguishing features, ASD contracting is no different than traditional service contracting, from a strict legal perspective. ASD contracts are usually complex in scope, high in dollar value, long in duration, and require consideration of complex costing elements and human resource elements, such as in-house bids and Canada Labour Code provisions for successor rights. ASD contracts are therefore considered to be higher in risk than most services contracts.

The question of whether the ASD contractor must follow government policy, regulation and legislation for its contracting activity is a complex issue which has not been tested in the courts. Each case should be examined on its own merit taking into consideration how the procurement was structured, whose need it is, who is the requisitioning authority, and who will take title. Other factors to consider include the degree of competition, the nature of the work, the appropriateness of bundling various services, and whether the Contractor is acting as an agent of the Crown.

Interviewees held various views on the appropriateness of in-house bids, with procurement personnel expressing concern about the ability to uphold the principles of fair and equitable treatment to all bidders. Other potential areas of vulnerability in the procurement process include aspects of the solicitation and bid evaluation processes, bundling of requirements, treatment of human resource issues, utilizing performance-based statements of work, linking payment to performance, and devoting sufficient resources to adequately manage the contract. Concerns were also raised in the 1999 Report of the Office of the Auditor General (OAG) related to performance indicators, monitoring and performance management procedures, successor rights, profit markups and sole source contracts.

Conclusions

The Minister's accountabilities for ASD contracting are the same as they are for other types of service contracting. They are, however, more difficult to safeguard in light of the risks associated with unique, complex and sensitive requirements which involve the human resource dimension of transferring work done by public servants to the private sector. Some of the uncertainties associated with ASD contracting stem from an unclear policy framework for in-house bids and some unanswered questions relating to contracting and other activities by the prime contractor.

Given the complexity of ASD contracting, PWGSC, in conjunction with its client departments, can play a key role in putting in place mechanisms for alternative delivery arrangements to ensure that the public interest is protected in terms of fairness, equity, and openness and stands the test of public scrutiny in matters of prudence and probity. Certain aspects of the procurement process such as bundling services at the solicitation stage, developing evaluation criteria, crafting contractual clauses to address particular ASD issues, linking performance and payment, and providing sufficient contract management are critical to providing value-added support to ensure clients achieve their intended program results and address the principles of accountability.

As for service delivery, the creation of a Centre of Expertise for ASD contracting is considered a positive initiative to strengthen PWGSC's role in providing value-added services and to support client departments in adhering to the principles of accountability identified by the OAG and TBS.

The differing views on the future number of ASD requirements, suggest a need for increased environmental scanning to determine clients' requirements and to allow the department to better plan and provide skilled procurement resources. Given this unknown, the complexity and heightened risks associated with certain aspects of ASD contracting, and the need for experienced, highly skilled procurement officers in headquarters and the regions, it is not known if PWGSC will be in a position to support its clients effectively, if there are a significant number of ASD requirements in the future.

Recommendations

1. *In light of the issues raised through this preliminary survey, and the recent audits by the Office of the Auditor General which cover the contracting process for ASD projects, it is recommended that no further review work be conducted by ARB at this time.*
2. *It is recommended that the ADM, SOSB, take the lead, with input from the Regional Directors General, in conducting an environmental scan of client departments to determine the number, and nature of future ASD projects requiring PWGSC's services.*
3. *If it is determined that the future number of ASD requirements is significant, and that ASD contracting will continue to be a viable business for the department, it is recommended that the ADM, SOSB consider the applicability of the issues identified herein and develop a risk management framework which would include, as a minimum, the following:*
 - *clarification of roles and responsibilities between client departments, headquarters and regions*
 - *a human resource strategy to assure sufficient and appropriately skilled procurement resources including the development of a special training module on ASD contracts*
 - *a review of the current policy framework to identify gaps and develop policy specific to ASD requirements on topics such as in-house bids and successor rights*
 - *a review to determine whether mechanisms and resources are in place for diligent contract management, monitoring and reporting to senior management*
 - *an examination on a case by case basis, of the proposed contracting activities of the prime contractor, with appropriate input from legal counsel, to ensure*

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that the risk of contravening the trade agreements is minimized and to determine the appropriateness of placing restrictions on the prime contractor's procurement of goods and services under the contract

1. Introduction

1.1 Authority for the Project

This review was approved by the Audit and Review Committee (ARC) as part of the 1999/2000 Audit and Review Plan.

1.2 Objectives

To examine the Minister's accountabilities related to contracting for Alternative Service Delivery (ASD) contracts and to examine the extent to which ASD contracts and supporting mechanisms are in keeping with these accountabilities.

1.3 Background

The public sector in Canada, like public sectors in other countries around the world, has been undergoing a period of structural change and renewal. Strong forces, including debt and deficit pressures, increased global competition and information technologies, have been driving these changes. As an important part of the government's strategy for *getting government right*, in 1995, the Treasury Board issued a framework for alternative program delivery to provide departments with strategies, principles and criteria to promote client-oriented, affordable and innovative government services.

Government departments implementing alternative program delivery try to select the best way to deliver programs, activities, services and functions to achieve government objectives, while creating a more client-oriented, affordable and innovative program delivery environment. This can be done in numerous ways, including: establishing more service-oriented and businesslike Special Operating Agencies and other flexible service delivery arrangements; establishing new forms of co-operation among departments such as sharing administration services at the local level; setting up Crown corporations; negotiating partnering arrangements with other levels of government, the private and voluntary sectors; devolving programs and services to the provinces; commercializing government services to improve efficiency while protecting the public interest; and privatizing government programs and services that no longer serve a public policy purpose.

1.4 Scope

This preliminary survey focuses on one of the Alternative Service Delivery (ASD) arrangements - contracting out - where the government transfers the operation of, but not the responsibility for a function, to a private sector contractor for a specific period of time by means of a contractual arrangement.¹ As the government's procurement arm, Public Works and Government Services Canada (PWGSC) has been called upon to provide procurement services for those alternative program delivery arrangements that are contractually based.

¹ Treasury Board of Canada Secretariat. *Framework for Alternative Program Delivery*

2. Results of the Preliminary Survey Phase

2.1 Work Performed

The work for the preliminary survey consisted of documentation review and interviews with key stakeholders in PWGSC, the Treasury Board Secretariat (TBS), the Department of National Defence (DND), the Canadian International Trade Tribunal (CITT), the Office of the Auditor General (OAG), and the Public Policy Forum. ★

All work on this project was carried out at Headquarters and confined to those ASD projects managed by Supply Operations Service Branch (SOSB). Major Crown Projects and Repair and Overhaul contracting were excluded from the review.

More specifically, this phase of the review work examined the characteristics of ASD contracting including responsibilities, regulatory and policy obligations; possible issues with respect to policy, service delivery (including resource planning and the organization of ASD contracting); and potential areas of vulnerability in the procurement process.

2.2 Profile of ASD Contracting

2.2.1 Description

Contracting for an ASD requirement occurs after the Government has made its decision to contract out, for the first time, services which were traditionally provided by public servants. As previously stated, contracting out is transferring the operation of a function to a contractor for a specified period but not transferring the responsibility for it.

There are a number of features which distinguish ASD contracts, although from a strict legal perspective, ASD contracting is no different from traditional service contracting. ASD contracts are usually complex in scope, high in dollar value and long in duration. In addition to contracting out non-core services that were previously provided by public servants, ASD contracts may "bundle" or integrate several separate activities into one large requirement at a sub-program level. Increasingly, clients are seeking full service providers with the focus on performance requirements and not technical specifications. Complexities not seen in other service contracts centre around human resource elements, including the consideration of in-house bids and Canada Labour Code provisions for successor rights. Other complexities relate to the costing elements and the need to compare in-house costs and service delivery with alternative proposals. For these reasons, ASD contracts are considered to be higher in risk than most services contracts.

2.2.2. Statutory/Regulatory/Policy Framework

PWGSC's contracting activities are governed by a number of statutes, regulations, trade agreements, and policies. These include the *Department of Public Works and Government Services Act*, the *Financial Administration Act*, the *Government Contracts Regulations*, the *World Trade Organization-Agreement on Government Procurement (WTO-AGP)*, the *North American Free Trade Agreement (NAFTA)*, the *Agreement on Internal Trade (AIT)*, *Treasury Board Contracting Policy*, and the *PWGSC Supply Manual*.

In terms of ASD contracting, a number of guidelines are relevant, including TB's *Framework for Alternative Program Delivery*, the *Manager's Guide to the Human Resource Implications of Alternative Service Delivery*, and the *Work Force Adjustment Directive*. TBS officials have advised that plans have been made to update the *Framework for Alternative Program Delivery* for March 2000.² Other TB guidelines such as the *Guide to the Costing of Outputs in the Government of Canada*, *Make or Buy?*, and *Making the Organization More Efficient*, also have contracting implications.

2.2.3 Responsibilities of Minister of PWGSC

The *Department of Public Works and Government Services Act* expresses PWGSC's broad mandate of providing materiel and other management services to all departments as follows:

"The Department shall operate as a common service agency for the Government of Canada, and its activities as a common service agency shall be directed mainly toward providing the departments, boards and agencies of the Government of Canada with services in support of their programs."

The Act grants the Minister of PWGSC exclusive authority for the procurement of goods but not exclusive authority for the procurement of services. Program departments are able to carry out services procurements on their own or have PWGSC do the procurement on their behalf.

When PWGSC is carrying out the procurement, it is the contracting authority and is considered to be responsible for all aspects of the procurement process as per the Guiding Principle on Accountability expressed in the Supply Manual as follows: *"PWGSC is accountable for the integrity of the complete procurement process, including all actions taken within the process ..."*.

The foundation for government contracting, as expressed in the TB Policy on Contracting, states:

"The objective of government procurement contracting is to acquire goods and services and to carry out construction in a manner that enhances access, competition and fairness and results in best value or, if appropriate, the optimal balance of overall benefits to the Crown and the Canadian people."

² 1999 Report of the Office of the Auditor General, *Chapter 23 Involving Others in Governing - Accountability at Risk*, para. 23.41

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Government contracting shall be conducted in a manner that will:

- (a) stand the test of public scrutiny in matters of prudence and probity, facilitate access, encourage competition and reflect fairness in the spending of public funds;*
- (b) ensure the pre-eminence of operational requirements;*
- (c) support long-term industrial and regional development and other appropriate national objectives."*

Throughout the preliminary survey interviewees indicated that the Minister's accountabilities for ASD contracting are no different than they are for all other types of contracting and the objectives expressed above for government contracting are applicable to ASD contracting.

2.2.4 Responsibilities of Client Departments

While PWGSC is accountable for the integrity of the complete procurement process, there are elements within the process which are primarily the responsibility of the client department. Clients are typically responsible for defining the operational needs, developing the business case and project plan, obtaining project approvals as required, developing specifications that describe the quantity and quality of services to be delivered, the levels of service, performance standards, measurement systems and the methods and frequency of reporting. Clients also take the lead in evaluating the technical aspects of proposals, monitoring contractor performance, receiving and accepting goods and services, and making final payment to the contractor. PWGSC provides value-added service by being directly involved with the client throughout the ASD contracting process.

2.2.5 Responsibilities of the Treasury Board Secretariat

TBS assists the Government of Canada in managing its human, financial, information and technology resources prudently and in a manner that best supports the government's objectives and priorities. As the administrative arm of the Treasury Board, TBS has a dual mandate: to support the Treasury Board as a committee of ministers, and to fulfill the statutory responsibilities of a central government agency. TBS recommends and provides advice to the Treasury Board on policies, directives, regulations, and program expenditure proposals with respect to the management of the government's financial, human, and material resources. It is also responsible for the comptroller function of government, and supports the Treasury Board in its role as the general manager and employer of the Public Service.

The main areas of activity in the central administration of the Public Service cover expenditure management, personnel management, and financial and information management. In the area of financial management, TBS provides leadership through policies, frameworks of accountability, business process renewal, effective review, and sound financial and contracting management so that departments may provide innovative and affordable services to their clients.

2.2.6 Volume/Statistics

For statistical purposes, contracts for ASD requirements issued by PWGSC are treated as services contracts and are not readily identifiable through the statistical contract information system. To determine the current population of ASD contracts in SOSB, ARB requested statistical information from procurement personnel. ASD contracts were described as those resulting from a decision to contract for private sector expertise to manage and operate a government function or activity which may have been performed in house or was performed via a series of contracts awarded and managed by the Crown and where responsibility/accountability for the program or service remains with the Crown. In response, ARB was advised of 13 current ASD projects managed by SOSB on behalf of seven client departments. ~~★~~

2.2.7 Recent Reviews/Recent Initiatives

Relevant documentation relating to alternative delivery arrangements and accountability arrangements are discussed below.

2.2.7.1 TBS Working Paper

In its recent Working Paper on accountability expectations and approaches in Alternative Delivery arrangements³, TBS describes the federal government's framework for results-based management and accountability. The framework consists of a three-step strategy: identifying key results; measuring performance, learning and improving; and reporting to Parliament and Canadians on what was achieved in a balanced and credible way.

The Working Paper noted that in alternative delivery arrangements, although accountability may be shared or overlap, the federal government is still accountable for its own contributions or areas of responsibility. Ministers are accountable for:

- policy direction and decision-making to support programs
- program delivery structure
- putting in place adequate accountability frameworks or mechanisms for alternative delivery arrangements to ensure that the public interest is protected in terms of fairness, equity, prudence and openness;
- providing Parliament and the public with the relevant, accurate, consolidated and timely information on the use of the public funds and the results Canadians received.

³ Treasury Board of Canada Secretariat, Draft Staff Working Paper entitled, *Alternative Delivery (AD) Accountability Expectations and Approaches*, November 23, 1999.

2.2.7.2 Joint TBS/OAG Discussion Paper

In their joint Discussion Paper entitled, “*Modernizing Accountability Practices in the Public Sector*”, the Office of the Auditor General and the Treasury Board Secretariat identified five principles for effective accountability which apply to newer forms of accountability relationships. Alternative service delivery is one such relationship. The five principles are:

- The roles and responsibilities of the parties in the accountability relationship should be well understood and agreed upon.
- The objectives being pursued, the accomplishments expected and the constraints respected should be explicit, understood and agreed upon.
- The performance expectations need to be clearly linked to and in balance with the capacity (authorities, skills, and resources) of each party to deliver.
- Credible and timely information should be reported to demonstrate the performance achieved and what has been learned.
- Enlightened and informed review and feedback on the performance achieved should be carried out by the accountable parties, where achievements and difficulties are recognized and necessary corrections made.

The paper further points out that accountability for results asks if program managers have done everything possible with their authorities and resources towards affecting the achievement of intended results and if they have learned from past experience what works and does not work. Accounting for results of this kind means demonstrating that managers have made a difference, that through their actions and efforts they have contributed to the results achieved. It means managers are accountable for what they can influence as well as what they can directly control.

Clearly, PWGSC procurement officers have a role to play, during the contracting out process, to support client program managers in maintaining the five principles of accountability and accounting for results.

2.2.7.3 1999 OAG Report

The 1999 OAG Report includes two chapters on contracting out Alternative Service Delivery requirements: Chapter 18: *Public Works and Government Services Canada, Alternative Forms of Delivery: Contracting for Property Management Services*, and Chapter 27: *National Defence, Alternative Services Delivery Issues*.

The main points raised by the OAG in chapter 18, which covered the Alternate Forms of Delivery (AFD) project in RPS, were that the bidding process was open, transparent and fair, contracts were well designed and the handover to the contractor went smoothly. The OAG gave positive recognition of the use of “fairness monitors” during the contracting process. However, the OAG also noted that because some of the key monitoring and control features were not in place at the handover of operations, ongoing management of the contracts has been problematic. Since important items such as budgets, assessments of building conditions, and performance

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indicators were not completed on time, PWGSC was not able to carry out a complete assessment of the contractor's performance in the first year. The OAG recommended that PWGSC develop an action plan with the contractor to deal with outstanding contractual issues, including target completion dates and responsibilities for resolving them. PWGSC agreed with the recommendation.

The main points raised by the OAG in chapter 27, which covered DND's ASD projects, were that many of the business case analyses for the projects were poorly done, as options were not always adequately assessed or the best option chosen; the government lacks an adequate policy framework for "partnering" with the private sector; and contracting out large service programs, and inflexible contract arrangements resulted in payments for unused training capacity.

Specific concerns raised in the chapters, which directly relate to the contracting process for ASD projects, include the need to have timely and accurate information in order to establish appropriate performance indicators; the need for monitoring and performance management procedures to ensure the contractor is fulfilling its obligations; the need to properly consider labour code provisions for successor rights; the need to justify the profit markup in accordance with the PWGSC profit policy; and the need to obtain value for money by ensuring the pricing structure relates to services received. The OAG also raised concerns about sole-sourcing contracts, without first assessing the capability and willingness of the marketplace to compete, and the concern about contracts being extended without competition.

In its response to chapter 27, DND noted that it is devoting a higher level of management attention to ASD projects, including business case analysis, and is ensuring that staff are adequately trained. The TBS response to chapter 27 referred to the ASD Practice Guide and Database, which TBS is currently developing, to pull together the collective experience on ASD and to guide the evolution of ASD throughout the federal public service. TBS also noted that it is currently taking the lead on an interdepartmental initiative to reform procurement including policy considerations that govern the full procurement life cycle. PWGSC response indicated that it is supportive of continuing work on improving the guidelines and training for large multi-year service contracts and will be working with TBS in this regard.

3 Discussion of Possible Issues

3.1 Policy Issues

3.1.1 Contracting by the prime contractor

Given the extent of subcontracting that is likely to occur with the large ASD contracts, the question of whether the ASD contractor must follow government policy, regulation and legislation for its contracting activity is a key issue. It is also a complex issue, which has not been tested in the courts, therefore each case should be examined on its own merit.

Discussion with interviewees about the contracting activities of the ASD contractor focussed mainly on the applicability of trade agreements.



Interviewees agreed that an ASD contractor should never be acting as an agent of the Crown. This is consistent with the General Conditions normally included in ASD contracts which clearly state that neither the Contractor nor any of its employees is engaged as an agent of the Crown. Nevertheless, the behaviour of the parties in carrying out the contract may lead to the development of a Crown/agent relationship (or an employer/employee relationship), despite PWGSC's best efforts to structure the contract in a manner that prevents this. The possibility of creating a Crown/agent relationship was identified by a number of interviewees as a real risk to the Crown which is exacerbated by the long duration of ASD contracts.

The view was also expressed that the trade agreements would likely apply if, through improper bundling of services, a subcontracting activity required by the government in the main contract was not central to the basic purpose of the main contract. In other words, trade agreements must not be bypassed by merging several different requirements which are not directly linked to the purpose of the contract. An example of improper bundling might be the provision of office furniture under a buildings renovation contract.

It was the general view that if the ASD contract was awarded after a "healthy" competitive process among a number of companies and if the scope of services being contracted was in

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keeping with the basic objectives of the procurement, and was consistent with standard industry practice, then contracting by the ASD contractor would likely be considered part of the normal execution of the contract and the trade agreements would not apply at the subcontract level. The nature of what is being contracted out is a factor in determining whether government accountabilities are applicable to the prime contractor. If, for example, spares are being used in the provision of aircraft repair and overhaul services, the procurement of spares would not be subject to trade agreement obligations.

SOSB's Policy Notification (PN) No. 42, entitled *Third Party Procurement - Interim Guidelines* adds another dimension to the question by asking "if" and "when" restrictions should be put on a main supplier's freedom to buy goods and services. The interim guidelines were prepared in response to the recognition that the way in which the government operates is changing: there is increased use of alternative service delivery mechanisms, numerous small contracts are being replaced with one larger contract and clients are increasingly seeking overall service providers who will provide and be responsible for all aspects of a good or service - from design, through maintenance and repair, to disposal. What the government used to buy, under the well-known rules of government procurement, is now being bought by others, who are not bound by the same legal and policy obligations.

As explained in PN No. 42, third party procurement takes place when a government contractor, in the course of performing a contract, buys goods and services, using money that the government is paying under the main contract. It includes using sub-contractors to perform parts of the work, buying components for assembly into what the government has bought, and buying the equipment required to provide a service. These guidelines provide a framework to be used by procurement personnel during the procurement planning stage, to help them decide whether restrictions should be put on the contractor's procurement of goods and services. Under this framework, after assessing the factors of ownership, scope, severability/materiality and risk, one of the following conclusions will be reached:

- the Third Party Procurement (TPP) should be carried out by the contractor;
- the TPP should be carried out by the contractor, but following some rules set in place by the government, or
- the TPP should be carried out by the government.

On the subject of the business practices and behaviours of the ASD contractor, several interviewees expressed the view that while the Minister would likely not be legally accountable, he would likely be politically accountable for improper practices by the ASD prime contractor. An example cited was the use of a contractor with extremely poor human resource practices reflecting badly on the government.

3.1.2 In-house Bids

The issue of in-house bids came up repeatedly in the interviews. In-house bids are prepared by in-house personnel, in response to a solicitation for bids for certain functions and activities that

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are currently performed in-house. This process is different from that of Employee Take-Over (ETO), where ETO employees provide services after leaving the public service.

There is some question as to the official government position regarding the acceptability of in-house bids, notwithstanding the 1995 TB Decision⁴ that gave departments authority to consider in-house bids. The acceptability of in-house bids has not been tested in the courts nor at the CITT.

Within DND, any new ASD initiatives that lend themselves to in-house competitive bids are to be tested for savings through a "most efficient organization" exercise to determine if they should proceed to competition with the private sector. This involves reviewing the in-house activity to determine if it can be re-engineered to create a more efficient organization. If the necessary steps are taken to ensure the activity is conducted in an efficient and cost-effective way, bids may not be solicited from the private sector. If a decision is ultimately made to seek proposals from the private sector, the in-house organization would be permitted to submit an in-house bid.

Allowing in-house bids was considered, by some interviewees, to be a fair practice since it provides personnel directly affected by the possible change in service delivery an opportunity to demonstrate what they can do. Some PWGSC officials, on the other hand, expressed concerns about upholding the principles of fair and equitable treatment by permitting employees to submit in-house bids, as PWGSC's ability to establish a level playing field in the solicitation process could be jeopardized. To the extent that an in-house team may have access to information not otherwise available to the private sector, the department may be vulnerable to a challenge under the trade agreements.

Other interviewees noted that the government cannot award a legally binding contract to itself, and that through the in-house bid process, the government is merely creating the illusion of holding a valid competition, which in reality is a "make or buy" decision exercise.

3.1.3 Sole sourcing

Chapter 27 of the 1999 OAG Report notes that the government procurement process is based on the principles of probity, openness, transparency and the ability to withstand public scrutiny, equal access, competition and fairness. The Government Contracts Regulations permit sole-source contracts under certain conditions - namely, when the need is one of pressing emergency in which delay would be injurious to the public interest, the nature of the work is such that it would not be in the public interest to solicit bids, only one person or firm is capable of performing the contract, or the estimated expenditure does not exceed \$25,000.

The OAG's audit of ASD contracts in DND raised a number of concerns about value for money and the equity and fairness of the contracting process. Five of the nine ASD contracts audited by the OAG, including the \$2.8 billion NATO Flying Training in Canada contract, were awarded without competition.

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The sole sourcing of some of the DND contracts may point to a possible conflict between the government's objective of delivering more affordable, efficient and innovative services ("getting government right") and the need for an accessible, open, and competitive procurement system. For PWGSC, as the common services organization responsible for the integrity of the procurement system, this is an area of particular risk in that the award of a sole source contract may not withstand the test of public scrutiny, nor challenges to the courts or the CITT.

3.1.4 Re-competing the Requirement

Discussion with interviewees indicated that departments need to think about the long-term effects of contracting out their requirements. While in theory, there is an option to move the activity back in-house at the end of the contract, in practice, resorting to an in-house option is highly unlikely. Once the Crown loses its in-house capability to conduct the work, there is no realistic fall back position, other than continuing to contract for the requirement.

Concerns were expressed about difficulties in re-competing the requirement once it has been contracted with one contractor for an extended period of time. Although the courts acknowledge that an incumbent may have an advantage from the experience it has gained in a previous contract, the long-term nature of an ASD contract could further entrench such an advantage, making it unlikely for other bidders to compete successfully. To ensure fairness to all bidders, the need to prevent the ASD contractor from becoming deeply involved in the development work for the replacement contract was raised as a major issue. Concern was also expressed about the difficulty in determining transition costs, particularly if contractor tasks have become intertwined with government tasks.

Concerns were also voiced about the provision of in-house resource requirements needed for the re-contracting process. Having contracted out, it is natural for a department to either reduce its resources, or redeploy them for other purposes. When it is time to re-compete the ASD contract, a sufficient level of staff or funds may not be available within the client department to conduct activities such as developing statements of requirements, evaluation criteria, etc.

3.2 Service Delivery Issues

3.2.1 Resource planning within PWGSC

It is not evident that PWGSC is undertaking environmental scans to determine what ASD projects are on the horizon. Differing views were expressed during the interviews regarding future ASD projects. Some noted that ASD activities are slowing down; others suggested that ASD projects will continue to proliferate.

A number of interviewees expressed concern about the organization's ability to provide adequate support to clients, in light of the limited resources in SOSB. If PWGSC is not aware of incoming ASD requirements and is not involved with clients during the early planning stages for ASD requirements, resource planning within PWGSC will be done on an ad hoc basis as projects arise

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and individuals with the right skill sets to manage these complex requirements may not be assigned to them.

Given the complexity of ASD contracting, procurement officers require special expertise and perhaps a new way of thinking from that needed in traditional service contracts. They may be required to assist clients in developing business cases, in obtaining input from industry on the proposed business case and industry capability, and in developing performance-based Statements of Work. ASD procurement officers may also be required to advise clients and industry on issues relating to the displacement of public servants (such as successor rights), develop appropriate bid evaluation schemes, write the contract in language that does not encourage employer/employee relationships, link the Basis of Payment to performance, negotiate special financing arrangements, and diligently monitor performance. Several interviewees indicated that the department needs to develop its expertise in these areas. Others noted that due to the uniqueness and complexity of ASD contracts, advisory services from legal counsel and financial experts are becoming increasingly important. PWGSC may be at risk if it does not ensure that its procurement officers are equipped with the skills and expertise they need to appropriately advise and support its clients.

Although procurement personnel raised the concern about high resource consumption throughout the contracting process for ASD projects, there does not appear to be any systematic collection of data on ASD resource utilization. If contracting for ASD requirements continues or increases, this lack of data could impede the department's ability to plan and manage ASD contracts; and to determine its value-added relative to resources consumed.

3.2.2 Organizational Issues

ASD contracting is currently conducted in all Sectors within SOSB and in some regional offices. The Science, Informatics, Professional Services Sector (SIPSS) was designated as the lead organization and Centre of Expertise for ASD contracting in SOSB in an attempt to standardize approaches and to provide guidance and assistance to other Sectors/Regions involved in ASD contracting. For ASD projects within SIPSS, a senior Director and Legal Counsel are assigned to each project, in addition to their regular duties. Efforts were made by SIPSS to identify one person in each Region to act as a focal point for ASD requirements. Although not formalized, SIPSS prepares lessons learned and, to some extent, shares them with others involved in ASD contracting. It was apparent through interviews that others outside of SIPSS who have experience with ASD contracting are providing necessary guidance and assistance to regional counterparts who are involved in such projects.

Although there is an informal network established to provide guidance and assistance, a formal management control framework within PWGSC has not been established to manage the risks associated with the large, complex ASD projects. Suggested elements of a management control framework that were not present include the assignment of a project leader within PWGSC who would interface with the Project Leadership regimes in the client department; in very high risk cases the establishment of an advisory committee within PWGSC to guide the project leader;

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designated functional support (both legal and financial); an appropriate performance measurement and reporting system; and an evaluation mechanism.

3.3 Potential Areas of Vulnerability in the Procurement Process

3.3.1 Solicitation/Bid Evaluation

Competing government objectives may arise with ASD contracting and PWGSC has a key role to play in terms of ensuring that government contracting is conducted in a manner that “stands the test of public scrutiny in matters of prudence and probity, facilitates access, and encourages competition”. The solicitation and bid evaluation processes are therefore critical and leave the department open to criticism if not properly managed.

The bundling of requirements is an area of particular vulnerability for the department in terms of its ability to maintain an open, fair, and accessible procurement system. Interviewees noted that although the bundling of services into large packages may realize administrative efficiencies and possible cost savings, it could also reduce the number of bidding opportunities available to small and medium-sized enterprises. Moreover, the department should be scrupulous in ensuring that bundles are not designed to circumvent the obligations of the trade agreements, or designed in a manner that precludes competition, as this could compromise the integrity of the procurement system.

The scope and magnitude of ASD projects, coupled with performance-based statements of work, make the structuring of the evaluation criteria complex. The evaluation of bids can be difficult, increasing the risk of errors being made and the process being challenged.

3.3.2 Appropriate contractual provisions

There are other unique risks to ASD contracting and PWGSC must structure the contract to deal with various issues such as: the possibility of labour strikes, the union dimension, the definition of 'essential service', the non-performance by government employees interfacing with the contractor, and in DND's case, the potential employment of contractor personnel in a war zone. While most interviewees believed that the standard terms and conditions are adequate for ASD contracts, conceptualizing these complex projects and crafting appropriate contractual provisions was raised as an issue.

* This is complicated by the need to avoid making things so onerous for the contractor that the anticipated efficiencies and economies may not be realized.

To the extent that payment is tied to performance, the basis of payment is a critical aspect of the contract, and must reflect an equitable sharing of risk between the Crown and the contractor. The lack of specificity in describing the tasks, coupled with the fluctuating nature of services

⁵ *Treasury Board Contracting Policy*, March 6, 1998

requirements, makes structuring the basis of payment difficult. If not properly structured, the government may not receive value for money.

Several interviewees raised the issue of contractual language that could have the effect of creating a Crown/agent relationship or an employer/employee relationship. The challenge for SOSB is to avoid using prescriptive language yet still find a way to express the government's expectations and its needs in terms of expected outcomes. If the contract is not structured in a manner as to establish the contractor as an independent operator, such a relationship could be created.

3.3.3 Performance Measures and Contract Management

Performance-based work statements should identify the results the government wants to achieve - the expected outcomes and service quality - and should express these needs in a way that facilitates the measurement of results. In that regard, DND officials voiced concern that the traditional Request for Proposal/Statement of Work approach does not lend itself to some of the more complex ASD projects because the requirements are greater in scope and difficult to describe in a manner that will enable bidders to prepare and cost out a proposal. While some of the ASD projects are essentially a continuation of services already being provided by DND, others are more complex, and represent a new way of doing things. As such, they are not as easy to describe. DND also mentioned the considerable effort involved in breaking down an overarching requirement such as "to provide support for low level flying" into meaningful contract requirements and performance standards.

OAG officials spoke about the need for the government to develop expertise in monitoring contracts. Contract management is critical in achievement of intended results. ASD contracts require careful monitoring to ensure the Crown's interests are protected given their magnitude, complexity and inclusion of remuneration schemes tied to contract performance and incentive-type bases of payment. However, resource constraints within SOSB have forced it to delegate much of the contract management responsibilities to client departments. From the client perspective, the client may be moving from being the "do-er" to monitoring the "do-er". This may leave a void in the client domain, weakening PWGSC's ability to rely on the technical expertise of the client.

Many interviewees noted the need for the right level of procurement expertise and resources to dedicate to ASD contracting. Management within SOSB expressed the concern that recent downsizing may have resulted in insufficient resources with the know-how to handle the complexities associated with ASD contracting. One ASD project, for example, was transferred from SIPSS to a regional office for contract administration. However, the file was subsequently returned to SIPSS as the resource demands were too great for the region to handle.

4. Conclusion

The Minister's accountabilities for ASD contracting are the same as they are for other types of service contracting. They are, however, more difficult to safeguard in light of the risks associated with unique, complex and sensitive requirements which involve the human resource dimension of transferring work done by public servants to the private sector. Some of the uncertainties associated with ASD contracting stem from an unclear policy framework for in-house bids and some unanswered questions relating to contracting and other activities by the prime contractor.

Given the complexity of ASD contracting, PWGSC, in conjunction with its client departments, can play a key role in putting in place mechanisms for alternative delivery arrangements to ensure that the public interest is protected in terms of fairness, equity, and openness and stands the test of public scrutiny in matters of prudence and probity. Certain aspects of the procurement process such as bundling services at the solicitation stage, developing evaluation criteria, crafting contractual clauses to address particular ASD issues, linking performance and payment, and providing sufficient contract management are critical to providing value-added support to ensure clients achieve their intended program results and address the principles of accountability.

As for service delivery, the creation of a Centre of Expertise for ASD contracting is considered a positive initiative to strengthen PWGSC's role in providing value-added services and to support client departments in adhering to the principles of accountability identified by the OAG and TBS.

The differing views on the future number of ASD requirements, suggest a need for increased environmental scanning to determine clients' requirements and to allow the department to better plan and provide skilled procurement resources. Given this unknown, the complexity and heightened risks associated with certain aspects of ASD contracting, and the need for experienced, highly skilled procurement officers in headquarters and the regions, it is not known if PWGSC will be in a position to support its clients effectively, if there are a significant number of ASD requirements in the future.

5. Recommendations

1. *In light of the issues raised through this preliminary survey, and the recent audits by the Office of the Auditor General which cover the contracting process for ASD projects, it is recommended that no further review work be conducted by ARB at this time.*
2. *It is recommended that the ADM, SOSB, take the lead, with input from the Regional Directors General, in conducting an environmental scan of client departments to determine the number, and nature of future ASD projects requiring PWGSC's services.*
3. *If it is determined that the future number of ASD requirements is significant, and that ASD contracting will continue to be a viable business for the department, it is recommended that the ADM, SOSB consider the applicability of the issues identified herein and develop a risk management framework which would include, as a minimum, the following:*
 - *clarification of roles and responsibilities between client departments, headquarters and regions*
 - *a human resource strategy to assure sufficient and appropriately skilled procurement resources including the development of a special training module on ASD contracts*
 - *a review of the current policy framework to identify gaps and develop policy specific to ASD requirements on topics such as in-house bids and successor rights*
 - *a review to determine whether mechanisms and resources are in place for diligent contract management, monitoring and reporting to senior management.*
 - *an examination on a case by case basis, of the proposed contracting activities of the prime contractor, with appropriate input from legal counsel, to ensure that the risk of contravening the trade agreements is minimized and to determine the appropriateness of placing restrictions on the prime contractor's procurement of goods and services under the contract.*