

October 1, 2007

The Honorable Timothy Kaine
Governor of Virginia
1111 East Broad Street
Richmond, VA 23219

The Honorable John H. Chichester
Chairman, Senate Finance Committee
General Assembly Building, 10th floor
Richmond, VA 23219

The Honorable Vincent F. Callahan, Jr.
Chairman, House Appropriations Committee
General Assembly Building, 9th floor
Richmond, VA 23219

Gentlemen:

I am pleased to submit this report in response to Chapter 566 (2005) an Act to amend and reenact the third enactment of Chapter 994 of the Acts of Assembly of 2004, relating to the Competitive Government Act. The legislation requires the Governor to conduct a biennial enterprise-wide examination of the commercial activities being performed by state employees to ensure that these activities are being accomplished in a most cost-effective manner. All requirements of the Act have been met and the attached report reflects the manner in which services are provided by the Executive Department.

The legislation provides for the Secretary of Administration, in consultation with the Secretary of Finance and the Secretary of Technology, to submit a report once every second year of the biennium on the examination of commercial activities to the Governor and the Chairs of Appropriations and Senate Finance. In addition, the Governor is required to identify three enterprise-wide commercial activities biennially for assessment, re-engineering, and possible outsourcing.

The Governor and his administration have been, and remain, committed to serving the needs of Virginia's citizens through a state government that provides services in the most efficient and effective manner possible.

The 2007 Commercial Activities Inventory report maximized use of the technology available within state government and utilized the existing databases of the Department of Human Resource Management, Department of Accounts, and the Department of Planning and Budget. Although the Competitive Government Act states the examination of the commercial activities inventory could be conducted by a commercial source

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through a solicitation under the Public-Private Education Facilities and Infrastructure Act or the Virginia Public Procurement Act, the decision was made to utilize data and technology resources available within state government.

This information will be available on the web site of the Commonwealth Competition Council at www.egovcompetition.com

I would be pleased to respond to any questions you may have following a review of the attached reports.

Sincerely,

Viola O. Baskerville

Attachment

Preface

Chapter 566 (2005), an Act to amend and reenact the third enactment of Chapter 994 of the Acts of Assembly of 2004, relating to the Competitive Government Act requires the Governor to conduct a biennial enterprise-wide examination of the commercial activities being performed by state employees to ensure that these activities are being accomplished in a most cost-effective manner. All requirements of the Act have been met and the attached report reflects the manner in which services are provided by the Executive Department.

This examination is to be completed at least once in every two-year period and may be conducted entirely by a commercial source through a solicitation process as provided in the Virginia Public Procurement Act (§ 2.2-4300 et seq.) or the Public-Private Education Facilities and Infrastructure Act of 2002 (§ 56-575.1 et seq.). During every two-year period, the examination is to consider at least three commercial activities as the Governor may identify. The legislation further required that guidance be developed in determining functions that should be performed by state employees because they are inherently governmental in nature, and those that may be suitable for cost comparison analyses. This and all other provisions of the legislation have been met.

The Governor and his administration remain committed to serving the needs of Virginia's citizens through a state government that provides services in the most efficient and effective manner possible. The administration has conducted many initiatives and implemented several enterprise-wide business function reengineering projects that are achieving increased efficiencies and cost reductions. All have included public-private partnerships and outsourcing to private entities in accordance with the Virginia Public Procurement Act. This is the second report under the Competitive Government Act.

The five spreadsheets attached delineate the service activities of the Executive Department for the 2006-2007 fiscal year and arrays data for salaried and wage employment and contractual services.

Appreciation is extended to the Departments of Accounts, Human Resource Management, Planning and Budget, the Commonwealth Competition Council, the Office of Administration and the Virginia Information Technologies Agency for providing centralized information and technical support to meet the requirements of this legislation. Any comments or questions on the report should be directed to the Commonwealth Competition Council at the Department of Planning and Budget (804) 786-5064.

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Reports

Report 1: Services provided by the Executive Department Containing Commercial Activities

Report 2: Pass-Through Grants and/or Inherently Governmental Services of the Executive Department

Report 3: Executive Department Salaried and Wage Employment Expenditures

Report 4: Executive Department Salaried and Wage Employment Statistics with Contractual Expenditures

Report 5: Executive Department Contractual Services

Executive Summary

The Governor and his administration remain committed to serving the needs of Virginia's citizens through a state government that provides services in the most efficient and effective manner possible. The administration has conducted many initiatives and implemented several enterprise-wide business function reengineering projects that are achieving increased efficiencies and cost reductions. All have included public-private partnerships and outsourcing to private entities in accordance with the Virginia Public Procurement Act.

The Commonwealth of Virginia delivers its services in a variety of ways, including state employees, outsourcing, public-private partnerships, or a combination of these. The Competitive Government Act defines state employees as all persons employed by the Commonwealth to provide services, including both salaried and wage employees, and all persons engaged to perform work for or to provide services to the Commonwealth. This report reflects the delivery of services by the Executive Department of state government for fiscal year 2007.

In implementing the provisions of this legislation, the Governor directed the Secretaries of Administration, Finance, and Technology to (i) develop a methodology for updating the inventory of commercial activities previously developed by the Commonwealth Competition Council; (ii) provide guidance in determining functions that should be performed by state employees because they are inherently governmental in nature, and those that may be suitable for cost comparison analyses; (iii) determine which commercial activities are suitable for consideration for outsourcing at the agency level and which should be the subject of enterprise-wide approaches; (iv) provide guidance to agencies and institutions in making realistic and fair cost comparisons for contracting with the private sector; and (v) recommend such other actions as may be necessary and appropriate to procure the services, and develop the required reports.

In addition, in keeping with the requirements of the legislation, the Governor identified the following three enterprise-wide initiatives for 2005: fleet operations and maintenance, seat of government mail operations and services, and real estate operations and services. The results of these initiatives will be submitted to the Governor and House Appropriation and Senate Finance Committees by October 1, 2007.

The information presented expands upon the 205 commercial activities identified in the 1999 inventory compiled by the Commonwealth Competition Council and includes all activities of the Executive Department of state government. The former commercial activity topics will now be identified as service areas. This conforms to the naming structure for the state budget.

During the 2007 fiscal year, there were in excess of 700 services being provided for Virginia's citizens by the Executive Department. Removing the 178 services that are

considered pass-through grants and/or inherently governmental services, there are 539 services that contain some form of commercial activities. Efforts are underway to determine which of these services, or portions of these services, are considered inherently governmental, meaning that only the state workforce should deliver the service. The General Assembly and Governor have authorized over 98,900 classified employees in the Executive Department to provide its services. Recognizing that in many cases there is need to supplement the Executive Department workforce, almost 11,000 individuals have been employed by the state agencies and institutions as wage employees during the 2007 fiscal year. In addition, the Commonwealth spent \$7.95 billion in contractual services.

Details on the analyses done to develop the list of services and the delivery mechanisms for the Executive Department are reflected on the attached five reports:

Report 1: delineates the services of the Executive Department of state government that contain some form of commercial activities. This is a more comprehensive listing of services provided than in the 1999 inventory. Once the decision is made to study the service in depth and the outcome is known and implemented, it is intended that the activity will be moved to a completed list of services. As services are studied, the inherently governmental aspects of each will be identified and moved to a list of inherently governmental services. These two additional lists will be included in the information available on the web.

Report 2: lists the pass-through grant funding services which have been removed from the activities of state government identified in Report 1.

Report 3: arrays expenditures in salaried and wage information for the 2007 fiscal year.

Report 4: arrays salaried and wage employment statistics and contractual services for the 2007 fiscal year.

Report 5: reflects expenditures in contractual services for the 2007 fiscal year. This information will be available on the web sites of the Commonwealth Competition Council at <http://www.egovcompetition.com>.

2007 Commercial Activities Inventory

The Governor and his administration remain committed to serving the needs of Virginia's citizens through a state government that provides services in the most efficient and effective manner possible. The administration has conducted many initiatives and implemented several enterprise-wide business function reengineering projects that are achieving increased efficiencies and cost reductions. All have included public-private partnerships and outsourcing to private entities in accordance with the Virginia Public Procurement Act.

The Commonwealth of Virginia delivers its services in a variety of ways, including state employees, outsourcing, public-private partnerships, or a combination of these. The Competitive Government Act defined state employees as all persons employed by the Commonwealth to provide services, including both salaried and wage employees, and all persons engaged to perform work for or to provide services to the Commonwealth. This report reflects the delivery of services by the Executive Department of state government for fiscal year 2007.

This report complies with Chapter 566 (2005) an Act to amend and reenact the third enactment of Chapter 994 of the Acts of Assembly of 2004, relating to the Competitive Government Act. This Act requested the Governor to biennially conduct an enterprise-wide examination of the commercial activities being performed by state employees to ensure that they are being accomplished in a most cost-efficient and effective manner. For the purposes of this report, the legislation defined state employees as all persons employed by the Commonwealth to provide services, including both salaried and wage employees, and all persons engaged to perform work for or to provide services to the Commonwealth. In turn, the Secretary of Administration is to submit a report on the examination to the Governor and the Chairs of Appropriations and Senate Finance by October 1, 2007.

This report responds to these actions. In accordance with the legislation, the Governor directed the Secretaries of Administration, Finance and Technology to be responsible for accomplishing five major tasks:

- (i) develop a methodology for updating the inventory of commercial activities previously developed by the Commonwealth Competition Council;
- (ii) provide guidance in determining functions that should be performed by state employees because they are inherently governmental in nature, and those that may be suitable for cost comparison analyses;
- (iii) determine which commercial activities are suitable for consideration for outsourcing at the agency level and which should be the subject of enterprise-wide approaches;

(iv) provide guidance to agencies and institutions in making realistic and fair cost comparisons for contracting with the private sector; and,

(v) recommend such other actions as may be necessary and appropriate to procure the services, and develop the reports provided for in the third enactment of the legislation.

All requirements have been met.

In addition, as required by the legislation, the Governor identified the following three enterprise-wide initiatives for 2005; the results for these initiatives will be submitted to the Governor and House Appropriation and Senate Finance Committees by October 1, 2007.

1. fleet operations and maintenance
2. seat of government mail operations and services
3. real estate operations and services

Brief history of the methodology for updating the Commonwealth Competition Council inventory of commercial activities

The 1999 commercial activities inventory published by the Virginia Commonwealth Competition Council was the first such inventory developed for a state government in the nation. Each of the 205 activities listed in that inventory was cross-walked to the Virginia Information Technologies Agency taxonomy on services provided and to the new service area structure being implemented for state government by the Department of Planning and Budget. This new structure standardizes the service area titles, allowing the citizen and the individual state agency to utilize one set of familiar service titles when interested in how the state budget is being spent and on what services. The results of this process identified other services not included in the 1999 inventory and are now included in what is intended to be a standardized inventory.

Beginning in January 2005, the Department of Planning and Budget revised the Virginia State Government Program Structure resulting in the change of many service area titles. Therefore, the service area titles reflected below may not all coincide directly with those in the 2005 report. Additionally, the Department of Planning and Budget also conducted a review of all Aid to Localities service areas since the publication of the last report which has resulted in a clearer identification of these costs. Finally, actual FY2007 expenditures are reported here whereas prior reports have reported base budget totals.

Guidance in determining inherently governmental functions

Extensive research occurred in order to develop guidance for identifying inherently governmental functions within Virginia state government. This included

conversations with individuals outside the Commonwealth such as other state governments, the Council of State Government, the National Association of State Budget Officers and the Federal government Office of Management and Policy which publishes the federal definition of inherently governmental. Within our state government, research included conversations with the Office of the Attorney General, Division of Legislative Services, Department of Accounts, Department of General Services, Department of Planning and Budget, and the Commonwealth Competition Council, as well as a review of the Constitution of Virginia. While each agency was familiar with the term, there were only two references within Virginia state government:

1. The Agency Procurement and Surplus Property Manual (APSPM)¹ states that in Phase One of their long-standing “Make or Buy” Analysis Procedures, a list of all services must be made of (1) those being provided or proposed to be provided by the agency to the public or to other agencies and (2) the services the agency provides or contracts for in support of its operations. Once that is done, their guidance states that consideration should be given to the public acceptability of contracting. Determination is then made of which services are close to the fundamental purpose of government (such as judicial, police, tax collection, revenue disbursement, intergovernmental affairs) or which are essential to the government’s ability to protect the health, safety and welfare of its citizens (such as regulatory functions). The APSPM stresses exercising caution in considering services of this nature to be provided by contractors. While some parts of a particular service may be suitable for being provided by a contractor, others may not.

2. The Privatization/Competition Manual² defines an inherently governmental activity as being so intimately related to the public interest as to mandate performance by state employees.

The federal government has the most extensive guiding principle³ on inherently governmental functions found during this research. This policy letter establishes the federal executive branch policy relating to service contracting and inherently governmental functions. Its purpose is to assist executive branch officers and employees in avoiding an unacceptable transfer of official responsibility to government contractors.

¹ The public interest, public well being, and public trust require that inherently governmental activities be uninterrupted and continuous to alleviate risk and fulfill the Constitutional mandate. Agency Procurement and Surplus Property Manual, September 1998, Department of General Services, Division of Purchases and Supply, Richmond, Virginia 23219, Chapter 4, General Procurement Guidelines & Planning, 4.25 Make-or-Buy Analysis, and Annex 4-C, “Make or Buy” Analysis Procedures

² The Privatization/Competition Manual, 1998, Commonwealth Competition Council, Richmond, Virginia, 23219, page 14.

³ Policy Letter 92-1 to the heads of Federal government executive agencies and departments, September 23, 1992, <http://www.arnet.gov/Library//OFPP/PolicyLetters/Letters/PL92-1.html>. This policy letter was issued pursuant to section 6(a) of the Office of Federal Procurement Policy (OFPP) Act, as amended, codified at 41 U.S.C. [section] 405.

This research suggests that an “inherently governmental” activity in the Commonwealth of Virginia is one that is so intimately related to the public interest, public well being, and public trust as to mandate its performance by the governmental entity, state employees, and their direct agents. “Inherently governmental” includes:

- the act of governing;
- authority to collect and spend public revenues, and
- entitlements (from the Constitution of Virginia).

The public interest, public well being, and public trust require that inherently governmental activities be uninterrupted and continuous to alleviate risk and fulfill the Constitutional mandate.

Authority for “governmental activity” is established in the Constitution of Virginia:

- people have a right to uniform government of Virginia;
- governmental activity should produce the greatest degree of happiness and safety, and be most effectively secured against the danger of maladministration; and,
- exhibit a firm adherence to justice, moderation, temperance, frugality and virtue by frequent recurrence to fundamental principles.

Examples of inherently governmental activities:

- an effective system of education throughout the Commonwealth;
- free elections;
- transportation system;
- defense from enemy attack on the soil of Virginia;
- intercourse with other and foreign states;
- taxation and assessments at fair market value;
- ultimate control over the acquisition, use, or disposition of the property, real or personal, tangible or intangible, of the Commonwealth, including the collection, control or disbursement of appropriated and other state funds; and,
- natural resources for the benefit, enjoyment and general welfare of the people of the Commonwealth.

The act of governing, as in the exercise of government authority, implies discretion:

- discretion in making policy decisions;
- discretion in interpretation and execution of the laws of the Commonwealth to commit the government to a course of action;
- discretion in determining strategy;
- discretion in establishing the level of state control that is required over an activity; and,

- discretion in making activities available to private performance, particularly in considering factors like institutional knowledge, as well as other tangible and intangible factors.

The greater the amount of discretion involved in performing the activity, the more likely it is inherently governmental. In addition to the degree of discretion, the effect of an inherently governmental activity is that it commits government. For example, decisions, regulations, and policies are commitments of government. Activities, however, that support making decisions, regulations, and policies are not necessarily inherently governmental. The totality of circumstances must be considered in recognizing “inherently governmental” activities, not only discretion.

Delivery of services

During the 2007 fiscal year, there were in excess of 700 services being provided for Virginia’s citizens by the Executive Department. Removing the 178 services that are considered pass-through grants and/or inherently governmental services, there are 539 services that contain some form of commercial activities. Efforts are underway to determine which of these services, or portions of these services, are considered inherently governmental, meaning that only the state workforce should deliver the service. The General Assembly and Governor have authorized over 98,900 classified employees in the Executive Department to provide its services. Recognizing that in many cases there is need to supplement the Executive Department workforce, almost 11,000 individuals have been employed by the state agencies and institutions as wage employees during the 2007 fiscal year. In addition, the Commonwealth spent \$7.95 billion in contractual services.

Selected statistics are listed below on the top agencies and institutions expending the most on salaried and wage payrolls during the 2007 fiscal year. The top agencies and institutions expending the most dollars for salaried and wage employees, excluding fringe benefits, were:

	<u>Salaried Payroll</u>
Department of Transportation	\$380,480,582
University of Virginia	\$371,165,533
Virginia Polytechnic Institute and State University ⁴	\$338,672,819
Virginia Community College System ⁵	\$271,106,884
Virginia Commonwealth University	\$259,792,059
University of Virginia Medical Center	\$245,793,758
George Mason University	\$196,846,274
Department of Health	\$149,881,697
Department of State Police	\$124,205,021
James Madison University	\$111,503,115

Wage employee hours worked range from 3,590 to under an hour:

⁴ Includes the salary expenditures for the VPI Co-op Extension.

⁵ Includes the salary expenditures of the entire system.

Wage Payroll

Virginia Community College System ⁶	\$121,802,605
Virginia Polytechnic Institute and State University ⁷	\$89,518,635
University of Virginia	\$65,590,060
University of Virginia Medical Center	\$63,284,782
Virginia Commonwealth University	\$54,429,762
George Mason University	\$47,888,742
Virginia Community College System	\$23,528,337
Old Dominion University	\$22,642,253
James Madison University	\$21,645,551
Department of Alcoholic Beverage Control	\$19,399,916

The top contractual services utilized by the Executive Department during the 2007 fiscal year included:

Service Area	FY07 Expenditures	Agencies
Insurance Premiums for Health Services for		
Individuals	\$1,484,443,473.85	12
Medical Services	\$1,456,518,320.91	109
Nursing Home Services	\$1,240,197,977.79	7
Hospital Services	\$895,967,850.90	28
Highway Repair and Maintenance Services	\$380,105,857.56	34
Management Services	\$312,984,565.76	135
Skilled Services	\$285,495,553.17	168
Architectural and Engineering Services	\$213,200,031.44	93
Clinic Services	\$190,187,370.68	49

The full details on each topic are found in the attached reports.

Reporting Documentation

Based on the examination of all activities within the Executive Department of state government, the following reports are attached to document the results of commercial activities inventory and analysis:

Report 1 Delineates the services of the Executive Department of state government that contain some form of commercial activities. This is a more comprehensive listing of services provided than in the 1999 inventory. Once the decision is made to study the service in depth and the outcome is known and implemented, it is intended that the activity will be moved to a completed list of services. As services are studied, the inherently governmental aspects of each will be identified and moved to a list

⁶ Includes the wage expenditures for the entire system.

⁷ Includes the wage expenditures for the VPI Co-op Extension

of inherently governmental services. These two additional lists will be included in the information available on the web.

Report 2: lists the pass-through grant funding services which have been removed from the activities of state government identified in Report 1.

Report 3: arrays expenditures in salaried and wage information for the 2007 fiscal year.

Report 4: arrays salaried and wage employee statistics, and contractual services for the 2007 fiscal year.

Report 5: reflects expenditures in contractual services for the 2007 fiscal year.