

Roundup

An Update on Government Contracts Issues for Clients & Friends

November 2008 Vol. IV, No.7

In This Issue:

FAR Council Issues Final Mandatory Disclosure Regulations	1
DOD Preference for SDB's Held Unconstitutional.....	4
Highlights of the FY 2009 Defense Authorization Act	5
Bid Protests: Two Court of Federal Claims Decisions Overturn Agency Decisions Overriding the Automatic Stay Pending GAO Resolution of Bid Protests.....	8

FAR Council Issues Final Mandatory Disclosure Regulations

By Claude P. Goddard (claude.goddard@akerman.com)

In November 2007, at the request of the Justice Department, the FAR Council issued controversial proposed regulations requiring mandatory disclosure of criminal violations and overpayments on federal contracts. The proposed regulations were later expanded to include mandatory disclosure of civil False Claims Act violations. Earlier this year, Congress required the issuance of regulations regarding these matters before the end of the year. Those regulations were issued on November 12, 2008 and become effective December 12, 2008. The new regulations essentially adopt the proposed rules, with some refinements. The core requirements for mandatory disclosure of crimes, false claims, and overpayments on federal contracts remain. The critical features of the new regulations are set forth below:

1. The New Regulations Require Mandatory Disclosure By All Contractors.

- The current regulation imposes contractual requirements for ethics/compliance programs only on contracts in excess of \$5 million and with a period of performance in excess of 120 days.
- The new regulation does not change this scheme. Contractors will have a contractual obligation to adopt compliance programs and make mandatory disclosures only on contracts meeting the \$5 million/120 day thresholds. FAR 3.1004(a) (requiring insertion of the clause in specified contracts). This obligation will become effective on the date the provision is incorporated into the contract.
- However, the new regulation clarifies that a contractor may be suspended or debarred, even when the clause is not in the contract, if a principal of the contractor knowingly fails to timely disclose credible evidence of a violation of Federal criminal law involving fraud, conflict of interest, bribery, or gratuity violations found in Title 18, or a violation of the civil False Claims Act, or a significant overpayment. FAR 3.1003(a)(2) & 3.1003(a)(3). This is because the failure to make such timely disclosures constitutes a cause for debarment, regardless of any contractual obligation to disclose. Id.; FAR 9.406-2(b)(1)(vi) & FAR 9.407-2(a)(8).

2. Timeliness Rules.

- Timeliness of disclosure as required by contract or internal control systems is measured from the date of determination by the contractor that evidence is credible or the date the contract clause was incorporated, or date the internal control system was established (as the case may be), whichever is later.
- But, for suspension/debarment purposes, timely disclosure is measured from the date the contractor determines the evidence is credible, or from the effective date of the rule (December 12, 2008), whichever event occurs later.
- Use of specific time frames (e.g., 30, 60, or 90 days) for considering disclosures "timely" was rejected.

3. Contractors Will Have To Disclose All Past Crimes, False Claims and Overpayments—And Do So Shortly After December 12, 2008.

- The contractual obligation to disclose is prospective only. It becomes operative only when the clause requiring disclosure is incorporated into the contract.
- However, once the new cause for debarment becomes effective (on December 12, 2008), the new suspension/debarment provisions will trump the contract disclosure provisions. Contractors will have to timely disclose any past misdeeds, or else risk suspension or debarment for failing to do so.
 - **This means contractors must be prepared to disclose known past misdeeds within a timely period after December 12, 2008—or face possible suspension/debarment.**

- The obligation to disclose extends for 3 years after final payment, so contractors will have to disclose any wrongdoing on contracts that have not been closed for 3 years, or else face suspension or debarment.

4. Disclosure Rules.

- Disclosures must be made whenever, in connection with the award, performance, or closeout of the contract or any subcontract under it, the Contractor has credible evidence that a principal, employee, agent, or subcontractor of the Contractor has committed (a) a violation of Federal criminal law involving fraud, conflict of interest, bribery, or gratuity violations found in Title 18 of the United States Code; or (b) a violation of the civil False Claims Act. FAR 52.203-13(b)(3)(i).
 - The new regulation substituted in "credible evidence" instead of "reasonable grounds to believe" to clarify that a contractor has the ability to conduct an internal investigation before making a report. The "credible evidence" standard is higher, allowing the contractor to determine credibility before deciding to disclose.
 - The new regulation substituted the above language for "crime" to clarify that acts unrelated to the specified crimes are not subject to disclosure.
- The contractual requirement to disclose overpayments arises under the Payments clause; the failure of a principal knowingly to disclose overpayments is a cause for suspension/debarment. FAR 3.1003(a)(3).
- A failure to disclose is not a ground for suspension/debarment unless a "principal" of the contractor knowingly fails to timely disclose the wrongdoing.
 - A "Principal" means an officer, director, owner, partner, or a person having primary management or supervisory responsibilities within a business entity (e.g., general manager, plant manager, head of a subsidiary, division, or business segment, and similar positions). FAR 2.101(b)(2) & FAR 52.203-13(a).
 - The limitation to Principals is intended to preclude suspension/debarment when only low level employees have knowledge of the violation and do not inform their superiors.
 - The unreported overpayment must be "significant" or "material" to invoke the suspension/debarment provisions.

5. Other Matters.

- "Full Cooperation" means disclosure to the Government of information sufficient for law enforcement to identify the nature and extent of the offense and the individuals responsible for the conduct. It includes providing timely and complete responses to the Government's requests for documents and access to employees with information. FAR 52.203-13(a).
 - It does not require waiver of attorney privileges, or Fifth Amendment rights.

- It does not restrict a Contractor from conducting an internal investigation or defending a proceeding or dispute related to a potential or disclosed violation.
- The Government, to the extent permitted by law and regulation, will treat information disclosed as confidential where the information has been marked "confidential" or "proprietary." FAR 52.203-13(b)(3)(ii).
- Violations must be disclosed to the agency Office of Inspector General (OIG), with a copy to the Contracting Officer. FAR 52.203-13(b)(3)(i).
 - The report must be made to the agency that awarded the contract.
 - If the violation relates to an order under an ordering vehicle used by multiple agencies, the Contractor must notify the OIG of the ordering agency and the IG of the agency responsible for the basic contract. FAR 52.203-13(b)(iii).
 - If the violation relates to more than one government contract, the Contractor may make the disclosure to the agency OIG and Contracting Officer with the largest dollar value contract affected by the violation.
- Prime Contractors are not required to review or approve subcontractors' compliance programs. Primes are subject to suspension/debarment only if they fail to disclose known violations by subcontractors.
 - The new rules do not require that disclosures by subcontractors be made through their prime contractors.

DOD Preference for SDB's Held Unconstitutional by Federal Circuit

By Daniel J. Donohue (daniel.donohue@akerman.com)

On November 4, 2008, the Federal Circuit issued a decision in Rothe v. Dept. of Defense and Dept. of the Air Force, Case No. 2002-1017, November 4, 2008, this decision could have a major impact on small business contracting. By declaring the DOD's small disadvantaged business goal of 5% unconstitutional, the Federal Circuit calls into question the opportunities for small disadvantaged businesses (SDB) as prime contractors and also the requirements for prime contractors to meet certain small business subcontracting goals. The full impact of the decision is not yet certain.

In 1988, Rothe Development Corporation lost a competition for an Air Force contract to a SDB even though Rothe's price was lower. The Air Force gave the SDB a price evaluation preference authorized by the current 10 U.S.C. § 2323, which authorizes DOD to grant a price evaluation preference of up to 10% for SDB's. The statute, 10 U.S.C. § 2323, sets a goal of awarding 5% of DOD contracts to SDB's, including 8(a) firms. It also incorporates the Small Business Act's presumption that certain minorities are socially disadvantaged, and allows DOD to use a price evaluation preference of up to 10% to award contracts to small disadvantaged contractors. Rothe alleged that the statute on its face violated the Equal Protection Clause of the Fifth Amendment. The District Court granted the Government's motion for summary judgment. The Federal Circuit reversed, and enjoined DOD from implementing the statute.

The Federal Circuit held that the statute creates an explicit racial classification and thus is subject to strict scrutiny. The statute may survive such strict scrutiny only if it serves a compelling government interest and is narrowly tailored to meet that interest. To establish a compelling governmental interest, the court held that the Government had the burden of proving that Congress had a "strong basis in evidence" that remedial action based on race was necessary.

The District Court relied upon a number of studies and concluded that the government met its burden. The Federal Circuit reviewed the same studies and concluded that their methodology was flawed and thus that they did not provide the strong evidence required to justify Congress' decision to take remedial action based on race. For example, the Federal Circuit noted that the studies did not consider whether a company's size affected its capacity to obtain contracts, and that this might explain why small disadvantaged firms got fewer contracts than big companies. The Federal Circuit did not hold that the studies were without merit; rather it only held that they do not provide the strong evidence required to justify a racial classification.

The Court held that in 2006, when Congress most recently enacted this preference for SDB's, Congress did not have before it strong evidence to determine that remedial action based on race was necessary. Thus, the court held that 10 U.S.C. § 2323 was facially unconstitutional and violated the Equal Protection clause of the Fifth Amendment and deprive the plaintiff of due process. The Federal Circuit remanded the case to the District court in Texas with instructions for that district court to enjoin DOD's implementation of the DOD statute, 10 U.S.C. § 2323.

Highlights of the FY 2009 National Defense Authorization Act.

By J. Michael Littlejohn (michael.littlejohn@akerman.com)

On October 14, the President signed the FY 2009 Defense Authorization Act (Pub. L. No. 110-417). There are several important provisions for government contractors.

Personal Conflicts of Interest.

One important provision of the Act is the new directive from Congress for OFPP to develop regulations regarding "personal conflicts of interest" for contractor employees that assist the Government in "inherently governmental functions." This legislation is tied to a GAO report issued in the Spring of 2008 that addressed concerns about certain contractor employees that worked closely with the government on acquisition and other sensitive issues. Under Section 841, the OFPP is required to develop regulations that would implement a "standard policy" to prevent personal conflicts of interest by contractor employees "performing acquisition functions closely associated with inherently governmental functions (including the development, award, and administration of Government contracts)." The policy is to include a definition of "personal conflict of interest." More importantly, contractors will be required to set up procedures to identify

and prevent personal conflicts of interest, have an oversight plan to "verify compliance," and report any violations to the contracting officer. The legislative history states that contractors should be required to obtain financial disclosures from employees working in such capacity. In addition, Congress has talked the OFPP with reviewing the FAR to determine if there should be additional regulations to deal with Organizational Conflicts of Interest.

GAO Examination Rights.

Under Section 871, the Comptroller General "and his representatives" are now provided with the authority to "interview any current employee" in addition to the right to look at any records of contractors and subcontractors that "directly pertain to, and involve transactions relating to" a contract or subcontract. Notably, this authority is limited to the power that GAO has to examine records, and it specifically does not extend to the Contracting Officer or the Defense Contract Audit Agency's audit power.

Limits On Noncompetitive Contracts.

Section 862 provides that, if an agency decides because of urgent and compelling circumstances to issue a contract using non-competitive procedures by limiting sources from which it obtains bids, the contract will be limited in time to the "time necessary" "to meet the unusual and compelling requirements of the work to be performed" and the time for the agency "to enter into another contract for the required goods and services through the use of competitive procedures." This time may not exceed one year unless the agency head "determines that exceptional circumstances apply." Accordingly, this provision seems to limit the agency's ability to enter into a sole source contract or limited source competition for all long-term requirements on a product or service that it needs immediately. For instance, it might provide suppliers that have been excluded from a sole source award because their product was not qualified at the time of award with the argument that the agency must compete the requirement as soon as the supplier qualifies.

"Fair Notice" of Purchases under Multiple Award Contracts.

Under Section 863, the statute requires the FAR to be amended within one year to require "enhanced competition in the purchase of property and services ... pursuant to multiple award contracts" by requiring contracting officers to make any purchase under a multiple award contract exceeding the simplified acquisition threshold by competitive procedures. In order to meet "competitive procedures," the CO will be required to (1) give all multiple award contract holders "fair notice" of an intent to purchase -- which must include the "description of the work" and the "basis" of selection, and (2) give all contractors responding to the "fair notice" a chance to submit an offer and "have that offer fairly considered by the official making the purchase." The Contracting Officer must provide the notice to at least "3 qualified contractors" or it must determine "in writing that no additional qualified contractors were able to be identified despite reasonable efforts to do so." The CO can also waive the requirement for competitive procedures if it can justify limiting competition under 41 U.S.C. 253j(b) or 10 U.S.C.

2304c(b) or another law requires purchase from a specified source. If the contracting officer makes a sole source award of a task or delivery order, it must publish a notice of the award on FedBizOpps within 14 days of award and disclose its justification to the extent allowed under FOIA. Pursuant to the statute, these rules on competition will apply to GSA Schedule contracts, multiple award task order contracts, and any other indefinite delivery, indefinite quantity contract issued to 2 or more sources.

Limits on Subcontractor Tiering.

Under Section 866, the FAR will be amended within one year to "minimize the excessive use by contractors of subcontractors... that add no or negligible value" and to ensure that primes and subcontractors do not receive "indirect costs or profit on work performed by a lower tier subcontractor" to which the prime or subcontractor "adds no, or negligible, value (but not to limit charges for indirect costs and profit based on the direct costs of managing lower-tier subcontracts." The new statute would apply to any "cost reimbursement" or "task or delivery order" over the simplified acquisition threshold. The statute does not impact the limits on tiering that were placed on DOD contractors under 2007's DOD Authorization Act.

Definition of Commercial Items Regarding Services.

Under Section 868, the NDAA requires that the FAR be amended within 180 days to change definition of commercial services to clarify that the term commercial item may include "services that are not offered and sold competitively in substantial quantities in the commercial marketplace, but are *of the type* offered and sold competitively in substantial quantities in the commercial marketplace" but only if the Contracting Officer determines that the contractor has submitted "sufficient information" to "evaluate, through price analysis, the reasonableness of the price for such services." The CO *may* request the contractor to submit limited information to determine price reasonableness which could be "prices paid for the same or similar commercial items under comparable terms and conditions by both government and commercial customers." If the CO finds such information is not "sufficient", then it can ask the contractor to provide "other relevant information regarding the basis for price or cost, including information on labor costs, material costs, and overhead rates." Contractors should note that the CO's analysis is a two-step process that does not require the contractor to provide internal cost data until the CO decides it cannot determine price reasonableness on "prices paid." Secondly, the statute does not require nor authorize the CO to ask for certified cost and pricing data from the contractor.

COFC Overturns Agency Stay Overrides

By Daniel J. Donohue (daniel.donohue@akerman.com)

Two recent decisions of the Court of Federal Claims granted declaratory judgments invalidating agency decisions to override the CICA automatic stay of contract performance while GAO protests of the contract awards were pending. E-Management Consultants, Inc. v. United States, No. 08-680C (Hewitt, J., October 14, 2008) and Nortel Government Solutions, Inc. v. United States, No. 08-682C (Futey, J., October 20, 2008). The decisions discuss standards agencies must meet in order to override the CICA stay. While these decisions are not the first to overturn agency override decisions, they should be of interest to both protesters wishing to challenge agency override decisions and to agencies wishing to defend such decisions.

By way of background, the Competition in Contracting Act of 1984 (CICA), 31 U.S.C. § 3551-56, provides for an automatic stay of contract performance pending resolution of a timely GAO bid protest. CICA also allows an agency to override the stay to allow contract performance to proceed while the protest is pending if the head of the procuring activity determines that "performance of the contract is in the best interests of the United States," or that "urgent and compelling circumstances that significantly affect interests of the United States will not permit waiting for the decision of the [GAO] concerning the protest." 31 U.S.C. §3553(d)(3)(C). The automatic stay is intended to preserve the status quo so that a remedy is possible in the event that GAO recommends that the protested contract award be set aside.

The E-Management and Nortel decisions both held that Court of Federal Claims has jurisdiction under the Tucker Act, 28 U.S.C. § 1491, to hear claims for declaratory and injunctive relief to overturn an agency decision to override the automatic stay. The Tucker Act gives the Court broad jurisdiction to hear any case alleging violation of a statute or regulation "*in connection with* a procurement or proposed procurement." Since E-Management and Nortel alleged that the agencies' override decisions violated the CICA, a statute that has a connection with procurement, the Court of Federal Claims had jurisdiction.

The decisions also held that the Tucker Act also establishes court's standard of review as that under the Administrative Procedures Act (APA) - whether the agency action is "arbitrary, capricious, an abuse of discretion or otherwise not in accordance with law." Under that standard, the issue is whether the decision to override the automatic stay "lacked a rational basis" or "involved a violation of regulation or procedure."

The test of whether a discretionary decision has a rational basis is whether the agency provided a coherent and reasonable explanation of its exercise of discretion. The test of whether an agency's decision is arbitrary or capricious considers four factors: whether the agency "[1] relied on factors which Congress has not intended it to consider, [2] entirely failed to consider an important aspect of the problem, [3] offered an explanation for its decision that runs counter to the evidence before the agency, or [4

rendered a decision that] is so implausible that it could not be ascribed to a difference in view or the product of agency expertise."

Finally, both decisions held that, with specific reference to review of an agency's override of the statutory stay, the court reviews "(1) whether significant adverse consequences would occur if the agency did not override the stay (2) whether reasonable alternatives to the override were available, (3) how the benefits of overriding the stay compared to the potential cost of the override, including costs associated with the potential that the protester might prevail before GAO, and (4) the impact of the override on the competition and integrity of the procurement system."

E-Management Decision – Override Lacked a Rational Basis. In the first case, E-Management timely filed a GAO protest against an award to a competitor of a negotiated contract for information technology (IT) services for the National Highway Traffic Safety Administration (NHTSA) of the Department of Transportation. NHTSA decided to override the automatic stay, citing as justification "the best interests of the United States." While its GAO protest remains pending, E-Management filed a Complaint in the Court of Federal Claims seeking declaratory and injunctive relief against the override decision. The Court issued a declaratory judgment against the override, to reinstate the stay of contract performance. The GAO protest remains pending and a decision is expected by December 26, 2008.

In the E-Management case, the court held that the first two factors - whether the agency "[1] relied on factors which Congress has not intended it to consider, or [2] entirely failed to consider an important aspect of the problem" both weighed against the override. The court found that significant adverse consequences would not necessarily occur without an override because evidence in the record showed that the agency could add funding to E-Management's existing contract to continue IT support while E-Management's GAO protest was pending. With respect to the third and fourth factors – concerning "benefits of overriding the stay" and the "impact of the override on competition and the integrity of the procurement system" - the court rejected the agency's justification that these favored the override because the agency had a reasonable chance of winning the protest and thus the contract award may not be disturbed. The court held that this reliance on the agency's likelihood of success on the merits of the GAO protest was an "impermissible consideration" because the purpose of the stay is to prevent agencies from ignoring protests. Thus, the court held that the NHTSA "failed to consider an important aspect of the problem" and thus its decision to override the stay lacked a rational basis.

Nortel Case - Urgent and Compelling Circumstances Did Not Justify the Override. Nortel timely filed a GAO protest against the award to SRA of a negotiated contract for IT services for the Drug Enforcement Agency (DEA). This current protest is part of a long-running series of GAO protests over award of this contract. DEA originally awarded the contract to Nortel in 2007, but took corrective action in response to SRA's GAO protest. DEA then revised its solicitation and awarded to SRA, but then again took corrective action in response to Nortel's protest. Upon resoliciting again this

year, DEA awarded the contract to SRA, followed by Nortel's protest to the GAO and DEA's decision to override the stay. Since 2007 when these protests started, Nortel and two other contractors have been providing the IT services to DEA under bridge contracts.

The DEA based its override decision on a fundamental assertion that the bridge contracts are insufficient to satisfy its IT needs because the bridge contractors – including Nortel – could not retain employees as the contract award date drew near. DEA argued that this constituted urgent and compelling circumstances. While DEA relied upon five separate problems or failures as examples of these urgent and compelling circumstances, the court found that the DEA's own data, declarations and testimony showed that the problems had causes unrelated to the bridge contracts and that the bridge contracts provided sufficient staffing to handle DEA's needs. In considering the first two factors concerning override decisions - "(1) whether significant adverse consequences would occur if the agency did not override the stay (2) whether reasonable alternatives to the override were available" – the court held that there were no adverse consequences to maintaining the status quo while Nortel's GAO protest was pending and that continued performance by Nortel and other bridge contractors provided reasonable alternatives to overriding the stay.

The court also considered "how the benefits of overriding the stay compared to the potential cost of the override, including costs associated with the potential that the protester might prevail before GAO, and (3) the impact of the override on the competition and integrity of the procurement system." The court rejected DEA's argument the potential cost savings favor proceeding with the potential override. The court found that DEA itself recognized that, by overriding the stay, DEA would incur higher costs in taking corrective action if GAO sustained Nortel's protest. But the court rejected DEA's rationale that such higher cost was justified because the contract with SRA would provide "sustainable" IT services by reducing the need to obtain security clearances for new employees. The court found that the override does nothing to alleviate instability for employees, and that such instability exists for any contractor until the GAO protest is decided and the contract finally is in place.

Finally, DEA argued that the override was in the "best interests of the United States" because DEA would save money by proceeding with the contract with SRA. The court held that such a cost concern does not support a "best interests" justification. Thus, the court granted declaratory relief stating that the override decision was invalid, and the therefore the automatic stay was reinstated.

The E-Management and Nortel decisions are the most recent example of the Court of Federal Claims' willingness to review an agency decision to override the statutory automatic stay during a GAO protest. An agency seeking to override the stay must take care to determine whether the factors discussed above support an override. These two decisions suggest that the court will not accept unsupported agency arguments that the stay will have "adverse consequences" or that there is "no alternative" to overriding the stay. In particular, agencies would be well advised to consider any available alternatives to override – like bridge contracts or extensions to the incumbent contract.

About Our Government Contracts Group

The Government Contracts Group at Akerman Senterfitt Wickwire Gavin assists large and small businesses with all types of federal government contracts issues. To do business with the federal government, contractors must deal with a unique and complicated series of statutes, regulations and procedures. We help clients work with this system to maximize contracting opportunities with federal government agencies. We provide counseling and representation to clients in the areas of contract compliance issues, bid protests, Small and Disadvantaged Business matters, contractor and subcontractor claims administration, construction contracts, information technology contracts, and international contracts. In addition, we are uniquely qualified to advise and assist contractors who provide goods or services to the U.S. Postal Service.

Members of our Government Contracts Group can be reached by telephone at (703) 790-8750 or by email at the following addresses:

Daniel J. Donohue daniel.donohue@akerman.com	Stephen B. Hurlbut steve.hurlbut@akerman.com
Michael Gatje mike.gatje@akerman.com	Pavan I. Khoobchandani pik@akerman.com
Donald G. Gavin donald.gavin@akerman.com	Steven J. Koprince steven.koprince@akerman.com
Jeffrey G. Gilmore jeff.gilmore@akerman.com	J. Michael Littlejohn michael.littlejohn@akerman.com
Claude P. Goddard, Jr. claud.goddard@akerman.com	Hal J. Perloff hal.perloff@akerman.com
Sarah M. Graves sarah.graves@akerman.com	J.R. Steele jr.steele@akerman.com
David P. Hendel david.hendel@akerman.com	Brian P. Waagner brian.waagner@akerman.com
Robert Andersen robert.andersen@akerman.com	Michael A. Fayad michael.fayad@akerman.com
Farah Khan farah.khan@akerman.com	

For more information on issues addressed in this newsletter, or on services provided by our Government Contracts Group, please contact Claude P. Goddard, Jr., or J. Michael Littlejohn at (703)790-8750 or by email at claud.goddard@akerman.com or michael.littlejohn@akerman.com. We also invite you to visit our web site at www.akerman.com.

This monthly publication of the Government Contracts Group of Akerman Senterfitt, with offices in Florida, California, New York, Virginia, Wisconsin, and the District of Columbia, is intended to inform firm clients and friends about legal developments in the area of government contracts law, including recent decisions of various courts and administrative bodies. Nothing in this publication should be construed as legal advice or a legal opinion, and readers should not act upon the information contained in this publication without seeking the advice of legal counsel. Moreover, this newsletter does not create an attorney-client relationship.

Unsubscribe: If you no longer wish to receive this publication, please email Amy Carson at amy.carson@akerman.com and include "unsubscribe Roundup" in the subject line.

© 2008 Akerman Senterfitt Wickwire Gavin

www.akerman.com