

Government Contracts Advisory

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National Defense Authorization Act for Fiscal Year 2008

Despite President Bush's veto of the National Defense Authorization Act for Fiscal Year 2008, Congress quickly passed a revised version of the bill, and he signed the measure into law on January 28th (Public Law 110-181). The new law contains numerous provisions of interest to the government contracting community, most found within Title 8 of the bill. Senator Carl Levin (D-MI), Chairman of the Senate Armed Services Committee, recently described the acquisition-related provisions as "the most significant reform of government procurement in the last decade." In the aggregate, the acquisition-related provisions will significantly affect the way the Department of Defense (DOD) purchases goods and services. The summary below highlights the provisions of the law of most consequence or greatest interest to the government contracting community. While this Advisory provides a summary overview of the law's major acquisition provisions, several of these sections are individually significant and will be the subject of separate Government Contracts Advisories in the near future.

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Acquisition Policy and Management Issues

Lead Systems Integrators

Effective October 1, 2010, DOD will be prohibited from awarding new contracts for lead systems integrator functions for major acquisition systems. Section 802 is intended to severely limit or actually prohibit DOD's use of lead systems integrators except for those that are actually the systems contractors in the first place. The limitation is absolute by 2010 and immediate for those systems that have not proceeded through low rate initial production (LRIP). Importantly, subsection 802(c)(3) contains a limitation allowing DOD to award contracts to obtain acquisition support functions for major systems so long as the contractor does not perform inherently governmental functions, federal employees remain responsible for determining which actions are in the government's best interest, and the prime contractor may not advise or recommend the award of contracts or subcontracts to an entity wholly or partially owned by the prime contractor.

Domestic Source and Content Restrictions

In an attempt to respond to industry and DOD pleas for relief from the specialty metal clause of the Berry Amendment, Congress last year amended 10 USC sec. 2533a to provide expanded waiver authority for domestic source and content restrictions (sec. 842, National Defense Authorization Act for Fiscal Year 2007, Pub. L. 109-364). This approach, however, has proven unworkable. DOD has been inundated with waiver requests, and the waiver process has become too slow and cumbersome to permit the Department to efficiently acquire the goods it needs. Congress therefore again has amended the specialty metals clause by increasing the number and availability of exceptions. Section 804 provides that while the statute applies to the acquisition of commercial items, it does not apply to contracts or subcontracts for the acquisition of commercially available off-the-shelf (COTS) items, other than for the acquisition of specialty metals not incorporated into end items, certain forgings and castings, some high performance magnets, and certain fasteners.

As amended by section 804, 10 USC 2533b authorizes streamlined compliance for commercial derivative military articles based on a contractor's certification that minimum threshold quantities are being purchased during the period of contract performance. Other amendments to the statute state that, for the purposes of the domestic sourcing exemption for the purchase of electronic components in which

the specialty metal content is minimal, the term “electronic components” does not include any assembly, such as a radar, that incorporates structural or mechanical parts. Domestic sourcing requirements also do not apply to items containing specialty metals not melted in the United States so long as the weight does not exceed two percent of the total weight of specialty metals in the item. Because of the complexity of the specialty metal provisions, a more thorough and detailed summary will be provided independently of this Government Contracts Advisory.

Commercial Items and Services

Concern about alleged abuse and misuse of commercial item and service acquisition authority has caused Congress to impose new requirements that DOD contracting officers must follow. The two areas of congressional concern are buying commercial services of a type offered and sold competitively in substantial quantities in the commercial marketplace and buying subsystems, components and parts of major weapon systems. To remedy concerns about whether the government is receiving a fair and reasonable price when buying such commercial items, section 805 requires the contracting officer to make a written determination that the offeror has submitted sufficient information to evaluate, through price analysis, the reasonableness of the price. Contracting officers may request from the offeror prices previously paid for the commercial service by both government and commercial customers. If prices provided by offerors are not sufficient to determine price reasonableness, the contracting officer may request information on labor costs, material costs, and overhead rates. Although a written determination of price reasonableness is required when buying a subsystem of a major weapon system that is a commercial item, it is not for components and spare parts to be used in a commercial system or subsystem (section 815).

In section 805, Congress has limited DOD’s authority to use time and material contracts when buying commercial services. DOD now can only use a time and materials contract when buying commercial services if the commercial services are for the support of a commercial item, an emergency repair service, or other commercial services if the agency head approves a contracting officer’s written determination, among other things, that the use of a time and materials contract is in the best interest of the government.

Congress is also requiring DOD to prepare new and detailed reports and inventories on commercial service contracts (sections 806 and 807). For the past five years, Congress has pushed the Department to conduct comprehensive spending analyses and to leverage its buying power to ensure that funds for commercial services are well spent. The Department’s lack of responsiveness is the reason for the imposition of these more detailed reporting and inventory requirements.

In section 808, Congress further requires periodic independent management reviews of contracts for services. Congress also directs DOD to issue guidance regarding the use of service contractors to provide contract support functions. The conferees again express discomfort with programs such as lead systems integrators that use contractors to provide program support and acquisition support services that in effect have them managing other contractors. The guidance is required to include periodic studies of the extent to which such interdependence arises and the nature of the financial interests of acquisition support contractors in contracts or subcontracts covered by their work – i.e. organizational conflicts of interest.

In section 822, DOD’s authority to use simplified acquisition procedures to buy property or services that are commercial items valued at no more than \$5 million is extended for two years, until January 1, 2010.

In the aggregate, the provisions dealing with commercial items and services reflect further limitations on outsourcing and privatization. The narrowed focus on what constitutes commercial services, including those for time and materials, the required split out of expenditures for such commercial services, inventory of such outsourced services, and management reviews are really the predicate for a determination whether the services should be brought back in house and performed directly by government employees.

Major Defense Programs

Multiyear Contracting

These provisions, largely applicable to major weapons systems procurements, impose further limitations on multi-year contracting and propose a more rigorous determination of milestones. In particular, section

811 amends 10 USC 2306b to permit DOD to enter into multiyear contracts valued at \$500 million or more if the Secretary of Defense provides certain certifications. Included among the new certifications are that an internal cost analysis has been performed, that the system being acquired has not exceeded the Nunn-McCurdy critical cost growth threshold within the five years preceding the contract, that enough end items have been delivered to determine that the unit cost estimates are realistic, that the contract is a fixed price contract, that during the fiscal year in which the contract is to be awarded sufficient funds will be available to perform the contract in that fiscal year, and that the future-years defense program will include enough funding to execute the program. If not all the certification conditions are met, the Secretary of Defense may nevertheless certify that a multiyear contract is in the best interest of the Department of Defense because of exceptional circumstances. Requests for increased funding for major systems under a multiyear contract must be accompanied by an explanation of how the request will affect the foregoing determinations made by the Secretary.

Further reflecting congressional concern with cost growth in major weapons system procurements, section 816 requires the Undersecretary of Defense for Acquisition, Technology and Logistics to conduct an annual review of systemic deficiencies in major defense acquisition programs that have led to critical cost threshold breaches or required recertifications by the Joint Requirements Oversight Council. In the same vein, the section 817 requires the Secretary of Defense to submit a report to Congress on the strategies of the Department of Defense for balancing the allocation of funds and other resources among major defense acquisition programs.

Battlefield Contracting

The conference report also contains several disparate provisions which, when considered collectively, suggest increasing congressional oversight of the contracting process related to the ongoing conflicts in Iraq and Afghanistan.

Section 810 codifies the new position of the command acquisition executive for Special Operations Command (SOCOM). This executive is to be responsible for the overall supervision of acquisition matters for SOCOM, whose forces currently play a key role in the ongoing conflicts in Iraq and Afghanistan. Section 824 permits the Secretary of Defense to exempt SOCOM from leasing limitations with respect to termination liability when certain conditions are met.

The review and audit of wartime contracts will continue. A newly created Commission on Wartime Contracting in Iraq and Afghanistan is to study contracting for the reconstruction of Iraq and Afghanistan, logistical support of coalition forces, and the performance of intelligence and security functions in those countries (section 841). The eight member Commission may hold hearings and receive testimony and evidence but is without subpoena power. The Commission is modeled after the Truman Commission which exposed fraud and abuse in World War II contracting. The Commission's final report is due in two years.

The Act also makes clear that Congress is striving for greater coordination in contracting among executive branch agencies. Section 842 requires the Department of Defense Inspector General, the Special Inspector General for Iraq Reconstruction, the Special Inspector General for Afghanistan Reconstruction (created by section 1229 of the Act), the State Department Inspector General, and the Inspector General for the United States Agency for International Development to conduct a series of audits of contracts for work in Iraq and Afghanistan pursuant to comprehensive and coordinated audit plans.

Section 861 requires the secretaries of Defense and State and the Administrator of the Agency for International Development to enter into a memorandum of understanding (MOU) in order to better coordinate contracting in Iraq and Afghanistan. Congress also requires the Government Accountability Office (GAO) to report annually on contracting matters in Iraq and Afghanistan, with emphasis on the total number of contracts and task orders, the total value of awards, and whether competitive procedures have been used (section 863). The GAO further is required to report on the number of personnel working on these contracts, the number of personnel performing security functions, and the number of personnel killed or wounded.

The new law also focuses on the activities of private security contractors. Section 862 requires a new Federal Acquisition Regulation (FAR) clause for **all** government contractors "performing private security functions under a covered contract in an area of combat operations." The requirements of this new FAR clause mirror those which already exist for private security firms contracted by DOD, as required by DFARS clause DFARS 252.225-7040. However, by adding this new requirement to the FAR, the Act

extends those provisions to all security contractors employed in combat zones by the U.S. Government, for example those performing protective services or providing military and police training for the State Department. Notably, section 862 does not define what constitutes a "covered contract," although the Act's language indicates it will only apply to security contractors, not those firms providing logistics or reconstruction support to the U.S. Government in combat zones. Also exempted from the new FAR clause are "contracts entered into by elements of the intelligence community in support of intelligence activities," language which includes the CIA and other agencies comprising the broader "intelligence community."

General Contracting Authorities

Of note in this subtitle of the bill is section 830, which concerns the widely reported congressional practice of earmarking funds for particular purposes. Section 830 requires the Comptroller General to report to Congress on the use of other than competitive procedures in the award of contracts with funds known as earmarks. The GAO is directed to compare the procedures used to implement congressional programs with those in contracts to implement programs or projects of special interest to senior executive branch officials.

Accountability in Contracting

Enhanced Competition for Task and Delivery Order Contracts

Section 843 makes a series of significant changes to current law governing competition for and under task and delivery order contracts. The most notable of the changes expands protest rights relating to orders placed under such contracts. In this context, task and delivery order contracts are indefinite delivery/indefinite quantity contracts, other than Federal Supply Schedule (FSS) contracts, that are generally awarded to multiple companies. Unlike prevailing law applicable to the award of orders under FSS contracts, protests of the award of orders under multiple award task or delivery order contracts are currently authorized only in limited circumstances.

The Act makes three principal changes to current law:

1. In order to award a task or delivery order contract exceeding \$100 million to a single source (rather than making multiple awards), the agency head must make one of four potential determinations in writing: (a) that the expected orders are integrally related; (b) that the contracts provides only for firm, fixed price orders at prices established in the contract; (c) that only one source is qualified and capable of performing the work at a reasonable price; or (d) that there are exceptional circumstances.
2. For orders in excess of \$5 million, the fair opportunity process required by current law must include: (a) notice of the order including a clear statement of agency requirements; (b) a reasonable period of time to prepare a proposal in response to the notice; (c) disclosure of the significant factors and subfactors to be considered in evaluating proposals and their relative importance; (d) for best value awards, the basis for award and the relative importance of quality and price/cost factors; and (e) an opportunity for a post-award debriefing.
3. For orders valued in excess of \$10 million, section 843 removes the current statutory restriction on protests, but gives GAO exclusive jurisdiction over protests of such high value orders. For protests based on the ground that the order increases the scope, period, or maximum value of the contract (which are authorized under current law), the Court of Federal Claims would continue to have jurisdiction concurrent with that of GAO.

The new fair opportunity requirements for orders in excess of \$5 million will take effect 120 days after enactment of the Act and will apply to any order awarded on or after that date. The expansion of protest rights will take effect 120 days from enactment of the Act and remain in effect for three years from that date.

Other Accountability, Ethics and Conflict of Interest Issues

Several provisions of the new law reflect continuing congressional interest in greater contractor accountability, in ensuring ethical behavior from contractors and their employees, in short stopping

conflicts of interest – both personal and organizational, and a search for better compliance tools.

Emphasizing the importance of openness in government contracting, section 844 amends the Federal Property and Administrative Services Act of 1949 (41 USC 253) and 10 USC 2304 to require civilian and DOD agency heads to generally make publicly available within 14 days of the award of a noncompetitive contract the justification and approval (J&A) for the use of noncompetitive procedures. The time period is extended to 30 days in cases of unusual and compelling urgency. Of similar import is section 845, which requires agency inspectors general, in their semi-annual reports to Congress, to include an annex on completed contract audits containing “significant audit findings.” These findings are defined to include unsupported, questioned, or disallowed costs in excess of \$10 million or other findings the agency inspector general deems significant.

Whistleblower Protection

Section 846 would make substantial changes to the existing contractor employee whistleblower protection statute. Under this provision, contractor employees are protected against reprisal if they disclose “ information that the employee reasonably believes is evidence of gross mismanagement of a DOD contract, a gross waste of DOD funds, a substantial and specific danger to public health or safety, or a violation of law related to a DOD contract or grant.” Under prior law, reprisal protections attached only if the employee reported “information relating to a substantial violation of law related to a contract.” Second, the provision protects employees who disclose information of wrongdoing to “a Member of Congress, a representative of a Committee of Congress, an Inspector General, the Government Accountability Office, a Department of Defense employee responsible for contract oversight or management, or an authorized official of an agency or the Department of Justice.” Previously, protected disclosures had to be made to a Member of Congress or an authorized official of an agency or the Department of Justice.

Thus, this section significantly expands the circumstances under which contractor employees are protected against reprisal, and the quantum of evidence needed to trigger employee protections is lowered (the employee is now protected if he or she reasonably believes the disclosed information is evidence of wrongdoing.) Perhaps just as important, contractor employees who feel aggrieved by the agency head’s reprisal determination or other action are given a *de novo* right of action at law or equity in federal district court, without regard to the amount in controversy and complete with on demand jury trial. It thus seems clear that the Congress is seeking to incentivize contractor employees to report wrongdoing as well as protect them for disclosing suspected employer wrongdoing, even if the facts ultimately fail to substantiate gross mismanagement or waste of taxpayer funds.

Conflict of Interest Issues

Section 847 requires certain senior DOD officials to request written opinions from agency ethics officials regarding post-employment restrictions on their work before accepting any compensation from new employers. The new requirement applies to all employees covered by procurement integrity restrictions (those personnel who participated personally and substantially in acquisitions with a value of at least \$10 million) and other specified senior DOD officials. Contractors may not compensate covered officials who left DOD within the past two years unless they first confirm that the ethics opinion was timely requested. Covered officials and contractors who fail to comply are subject to the administrative penalties available for procurement integrity violations at 41 USC § 423(e). Such opinions are currently available on a voluntary basis. Making them mandatory and a matter of enforcement is a major alteration in the law applicable to senior DOD officials leaving government service.

Congress also has altered the way contractors are required to manage their employee conflicts of interest. Section 848 directs a GAO study of (at a minimum) the extent to which major defense contractors have ethics programs and the extent to which they cover a number of specific topics, including

- Availability of mechanisms like hotlines for reporting possible violations internally or to the government
- Notice of whistleblower protection
- Ethics training
- Internal audit or review programs for violations
- Self-reporting by contractors to the government
- Disciplinary action for violations
- Management oversight

The joint explanatory statement on the bill also includes direction that the GAO include information in its report on the extent to which contractor programs require (1) disclosure of personal financial interests and outside employment by key personnel performing work for the government; (2) conflict mitigation measures for addressing any personal conflicts of interest of employees in connection with their work on Department of Defense contracts; and (3) procedures for reporting these personal conflicts of interest and any mitigation measures to the Department of Defense.

Other Matters

Title 8 of the bill includes several sections requiring studies and reports on various topics. In addition to those mentioned above, those of potential significance to the contracting community include a GAO report on the organization and structure of major defense acquisition programs (section 813), a report on DOD policies for the acquisition of information technology (section 887), a report establishing a plan aimed at increased use of environmentally friendly products (section 888), and a GAO review of the use authorities under the Defense Production Act of 1950 (section 889). Another provision aimed at the prevention of export control violations requires the Secretary of Defense to issue regulations requiring defense contractors who provide goods or technology subject to export controls under the Arms Export Control Act or the Export Administration Act of 1979 to comply with those laws and regulations, including specifically the International Traffic in Arms Regulations and the Export Administration Regulations. Section 890 requires a contract clause enforcing this requirement and requires the Secretary of Defense to assist contractors in meeting regulatory requirements.

Conclusion

Title 8 of the National Defense Authorization Act for Fiscal Year 2008 contains a sweeping and varied array of provisions that will affect government contractors. The common threads among them are greater restrictions on outsourcing and privatization, greater scrutiny of contractor behavior, particularly for those contractors working in Iraq and Afghanistan, the desire for increased contractor accountability and concern over conflicts of interest, and new constraints on the contracting process, especially with respect to multi-year contracts and commercial items and services. Time will tell whether these changes benefit government contracting over the long term.

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