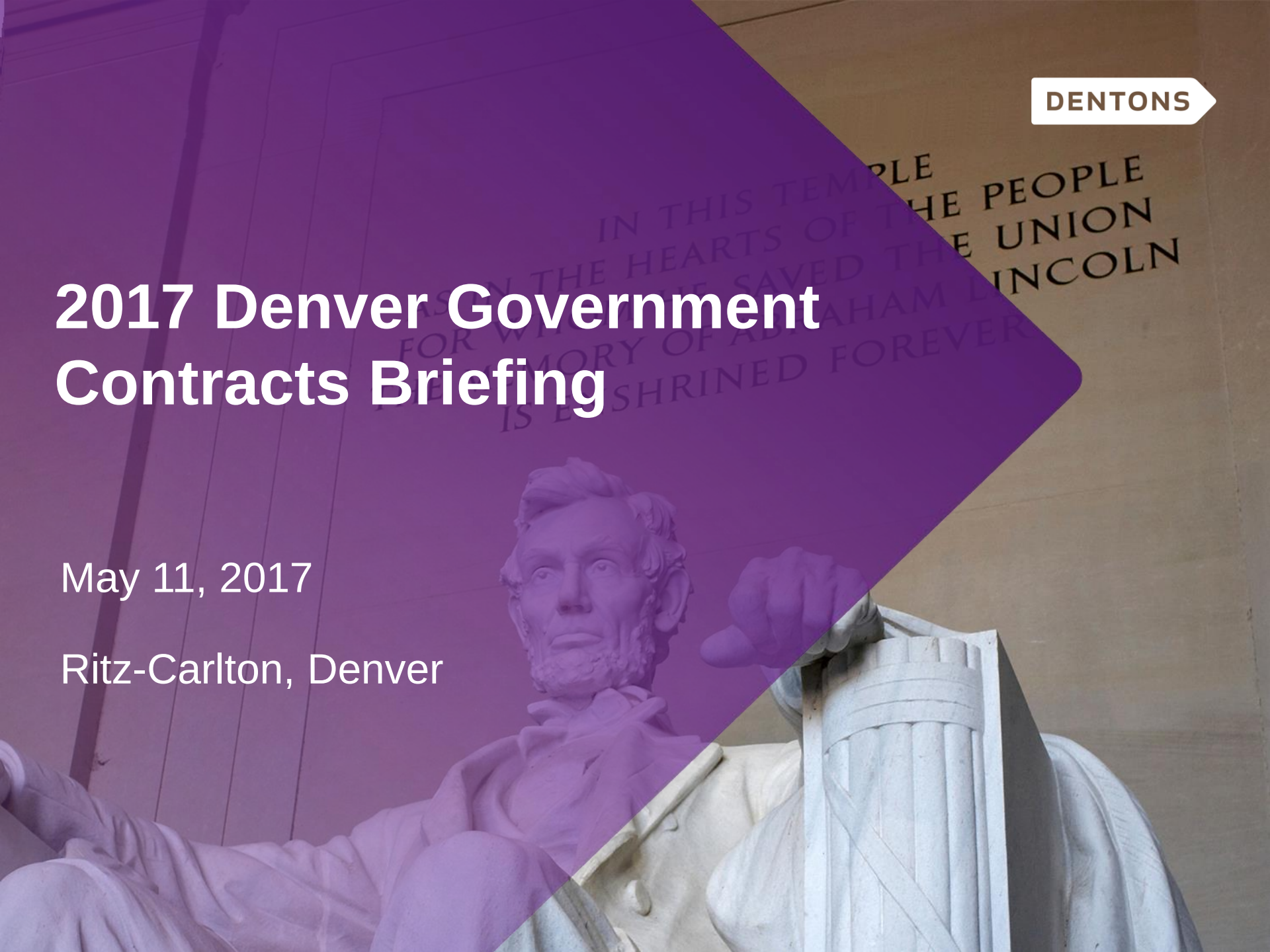

2017 Denver Government Contracts Briefing

May 11, 2017

Ritz-Carlton, Denver

Contract Procurement and Award

Jessica C. Abrahams
Joseph G. Martinez

Overview

- Acquisition and protest developments
- Communications with contractors
- Procurement and personnel
- Joint ventures: whose past performance matters?
- Evaluation errors
- Fee recovery
- Protest playbook
  - Where to protest timely electronic submissions?
  - Where to protest to obtain immediate relief?

Acquisition and Protest Developments
Protests at the COFC

- Historical comparison of COFC cases from FY2011-2016

	FY2016	FY2015	FY2014	FY2013	FY2012	FY2011
Protests Filed	124 (down 1.5%)	126 (up 15%)	110 (up 31%)	84 (down 15%)	99 (up 1%)	98 (up 11%)
Pre-Award	31	35	35	20	42	29
Post-Award	93	91	75	64	57	69

- 2016 specifics
  - 65 protest decisions in total
  - 64 published opinions
  - 1 unpublished opinions

Acquisition and Protest Developments
Protests at the GAO

- Historical comparison of GAO cases from FY2011-2016

	FY2016	FY2015	FY2014	FY2013	FY2012	FY2011
Cases Filed	2,789 (up 6%)	2,639 (up 3%)	2,561 (up 5%)	2,429 (down 2%)	2,475 (up 5%)	2,353 (up 2%)
Cases Closed	2,734	2,647	2,458	2,538	2,495	2,292
Merit (Sustain + Deny) Decisions	616	587	556	509	570	417
Number of Sustains	139	68	72	87	106	67
Sustain Rate	22.56%	12%	13%	17%	18.6%	16%
Effectiveness Rate	46%	45%	43%	43%	42%	42%
ADR (Cases Used)	69	103	96	145	106	140
ADR Success Rate	84%	70%	83	86%	80%	82%
Hearings	2.51% (27 cases)	3.10% (31 cases)	4.70% (42 cases)	3.36% (31 cases)	6.17% (56 cases)	8% (46 cases)

Acquisition and Protest Developments

Task Order Protests

- Historical comparison of GAO Task Order Protests from FY2011-2016

	FY2016	FY2015	FY2014	FY2013	FY2012	FY2011
Total Number of Cases Filed	2,734	2,639	2,561	2,429	2,475	2,353
Total Number of Task and Delivery Order Protests	375	335	292	259*	209	147
Percent of Total	13.7%	12.7%	11.4%	10.6%	8.4%	6.2%

*Beginning in 2013, GAO reported the number of task and delivery order protests as a subset of the number of cases closed rather than the number of cases filed

- Update: On Dec. 14, 2016, GAO's authority to hear protests on non-defense task or delivery orders over $10M was restored (previously expired on Sept. 30, 2016) (H.R. 5995)

Acquisition and Protest Developments

NDAA FY2017

- DOD task order bid protest threshold increased to $25M (Sec. 835)
- Requires report, due Nov. 30, 2017, on the prevalence and impact of bid protests (identifies 14 specific topics), including
  - An analysis of bid protests filed by incumbent contractors, including
    - (A) the rate at which such protesters are awarded bridge contracts or contract extensions over the period that the protest remains unresolved; and
    - (B) an assessment of the cost and schedule impact of successful and unsuccessful bid protests filed by incumbent contractors on contracts for services with a value in excess of $100M
  - An analysis of how often protestors are awarded the contract that was the subject of the bid protest
  - An analysis of the effect of the quantity and quality of debriefings on the frequency of bid protests (Sec. 885)
- Report demonstrates continued Congressional interest in the bid protest process and address view that incumbents are gaming the system by protesting

Acquisition and Protest Developments
NDAA FY2017 (cont.)

- Requires GAO to include a list of most common grounds for sustaining protests in its annual report to Congress (Sec. 889)
  - Previously performed by GAO
  - FY2016
    1. Unreasonable technical evaluation
    2. Unreasonable past performance evaluation
    3. Unreasonable cost or price evaluation
    4. Flawed selection decision
  - FY2015
    1. Unreasonable cost or price evaluation
    2. Unreasonable past performance evaluation
    3. Failure to follow evaluation criteria
    4. Inadequate documentation of the record
    5. Unreasonable technical evaluation

Communications with Contractors

What Are Discussions?

- The "acid test" for determining whether discussions occurred is "whether the offeror has been afforded an opportunity to revise or modify its proposal" (*Rotech Healthcare, Inc.*, B-413024, 2016 CPD ¶ 225 (Comp. Gen. Aug. 17, 2016))
  - A request for, or providing of, information related to offeror responsibility, rather than proposal evaluation, is not discussions (*Northrop Grumman Sys. Corp.-Costs*, B-412278.6, 2017 CPD ¶ 68 (Feb. 7, 2017))
- An oral presentation after proposal submission does not equate to discussions when
  - The offeror failed to demonstrate the presentation revised its proposal
  - The offeror was not provided the opportunity to revise or modify its proposal. *Sapient Gov't Servs., Inc.*, B-412163.2, 2016 CPD ¶ 11 (Comp. Gen. Jan. 4, 2016).

Communications with Contractors
What Are Discussions? (cont.)

- Clarifications may only be used to resolve minor/clerical errors or clarify certain aspects of a proposal
  - Contractor's failure to provide a signed JV agreement, when required by the solicitation, was not a minor oversight that could be cured through clarifications, even when the JV was an established LLC, had its own DUNS number, and was working on another contract for the same agency (*CJW-Desbuild JV, LLC*, B-414219, 2017 CPD ¶ 94 (Comp. Gen. Mar. 17, 2017))

Procurement and Personnel
Departure of Key Personnel

- Solicitation: material requirement is the identification of key personnel
  - Before proposal submission, bait and switch requires
    - That an offeror either knowingly or negligently represented that it would rely on specific personnel that it did not expect to furnish during contract performance
    - That the misrepresentation was relied on by the agency
    - The agency's reliance on the misrepresentation had a material effect on the evaluation results

Procurement and Personnel
Departure of Key Personnel (cont.)

- Solicitation (cont.)
  - Post-proposal submission
    - Upon notice of the departure of a key personnel prior to contract award the agency has two options
      - Evaluate the proposals as submitted and reject the proposal as technically unacceptable for failure to meet a material requirement; or
      - Reopen discussions to permit the offeror to correct this deficiency
    - A rejection of an offeror's proposal because a key personnel departed, not at the fault of the contractor, creates risk that a proposal may be deemed "unacceptable" *(URS Fed. Servs., Inc.*, B-413034, 2016 CPD ¶ 209 (Comp. Gen. July 25, 2016))
  - Recently GAO blurred the lines between the two (*Gen. Revenue Corp.*, *et al.*, B-414220.2, 2017 WL 1316186 (Comp. Gen. Mar. 27, 2017))

Joint Ventures and Past Performance
Whose Past Performance Matters?

- Solicitation: "past performance of either party in a joint venture counts for the past performance of the entity;" often assumed that one member's past performance = JV's past performance
- Update: the agency may properly consider the past performance of a single JV member that is responsible for particular performance (*IT Enter. Sols. JV, LLC.*, B-412036.3, 2017 CPD ¶ 66 (Comp. Gen. Jan. 31, 2017); *TA Servs. of S.C., LLC*, B-412036.4, 2017 CPD ¶ 67 (Comp. Gen. Jan. 31, 2017))
- Reminder on past performance description: conditional language, generalized statements, and high-level summaries deemed to provide "technical approach;" not actual past performance experience (*Mercom, Inc. v. United States*, No. 16-1475C, 2017 WL 1034484 (Fed. Cl. Mar. 14, 2017))

Evaluation Errors
Best Value v. LPTA

- Solicitation: award to be made of best-value basis
  - Agency cannot treat all offers as acceptable without any comparative analysis and select the lowest price because that would essentially turn the procurement into LPTA (*Patriot Sols., LLC*, B-413779, 2016 CPD ¶ 376 (Comp. Gen. Dec. 22, 2016))
  - Trade off analysis must be documented
  - A tradeoff analysis that fails to furnish any explanation as to why a higher-rated proposal does not in fact offer technical advantages or why technical advantages are not worth a price premium does not satisfy the requirement for a documented tradeoff rationale
- Demonstrates agencies' preferences for LPTA and likely continued attempt to use LPTA analysis in more technically complex procurements

Fee Recovery
Update

- Fee recovery at risk
  - Corrective action taken after filing two agency reports not sufficient to recover attorneys fees even in a close call based upon the "high bar" set by the clearly meritorious standard (*Northrop Grumman Sys.*, 2017 CPD ¶ 68)
  - Corrective action taken at recommendation of COFC and based upon comments that COFC was leaning in favor of the protestor was not sufficient to recover attorneys fees (*Dellew Corp. v. United States*, No. 2016-2304, 2017 WL 1541520 (Fed. Cir. May 1, 2017))
- Creates risk that corrective action taken upon recommendation of COFC or GAO will not entitle protestor to fee recovery

Protest Playbook

Where to Protest Timely Electronic Submissions?

- GAO/COFC split on timely receipt of electronic proposal
  - Receipt of an electronic quotation by the government's server is not the equivalent to being under the government's control (*Peers Health*, B-413557.3, 2017 CPD ¶ 93 (Comp. Gen. Mar. 16, 2017))
  - Receipt of an electronic quotation by the government's server is the equivalent to being under the government's control (*Fed. Acquisition Servs. Team, LLC v. United States*, 124 Fed. Cl. 690 (2016))
- The timely submittal of a proposal to the wrong location within FedConnect is sufficient when
  - The agency is aware of the submission
  - The proposal is out of the protestor's control
  - Competitive harm will not occur from acceptance of the proposal (*AECOM Tech. Servs., Inc.*, B-411862, 2015 CPD ¶ 353 (Comp. Gen. Nov. 12, 2015))

Protest Playbook
Where to File to Obtain Immediate Relief?

- Two primary statutes form basis for bid protests
  - Competition in Contracting Act (CICA): gives the GAO jurisdiction over bid protests
    - Update: GAO maintains jurisdiction over federal agencies that use non-appropriated funds despite its bid protest regulations that state it lacks jurisdiction over non-appropriated fund activities (*Info. Experts, Inc.*, B-413887, 2017 CPD ¶ 16 (Comp. Gen. Dec. 30, 2016))
  - Tucker Act: gives the COFC jurisdiction over bid protests
    - Note: FAR also provides for "agency" level protests
- GAO: automatic stay available if filed within 10 days of award or 5 days of debriefing; must file early enough for GAO to notify CO of protest
- COFC: no automatic stay; must seek temporary restraining order (TRO) or have agency voluntarily stay award

Protest Playbook
Where to File to Obtain Immediate Relief? (cont.)

- On a motion for a TRO, the COFC weighs four factors
  - Immediate and irreparable injury to the movant
  - The movant's likelihood of success on the merits
  - The public interest
  - The balance of hardship on all the parties
- As recent as last year, COFC required a showing of the first two elements prior to weighing the remaining factors (*Loch Harbour Grp., Inc. v. United States*, 128 Fed. Cl. 294, 300 (2016))
- Update: COFC may grant a TRO without any showing of the movant's likelihood of success when the government has not produced the administrative record and the parties have not had an opportunity to brief the merits of the protest (*Cont'l Servs. Grp., Inc. v. United States*, No. 17-449, 2017 WL 1174458, at *1 (Fed. Cl. Mar. 29, 2017))

Questions?

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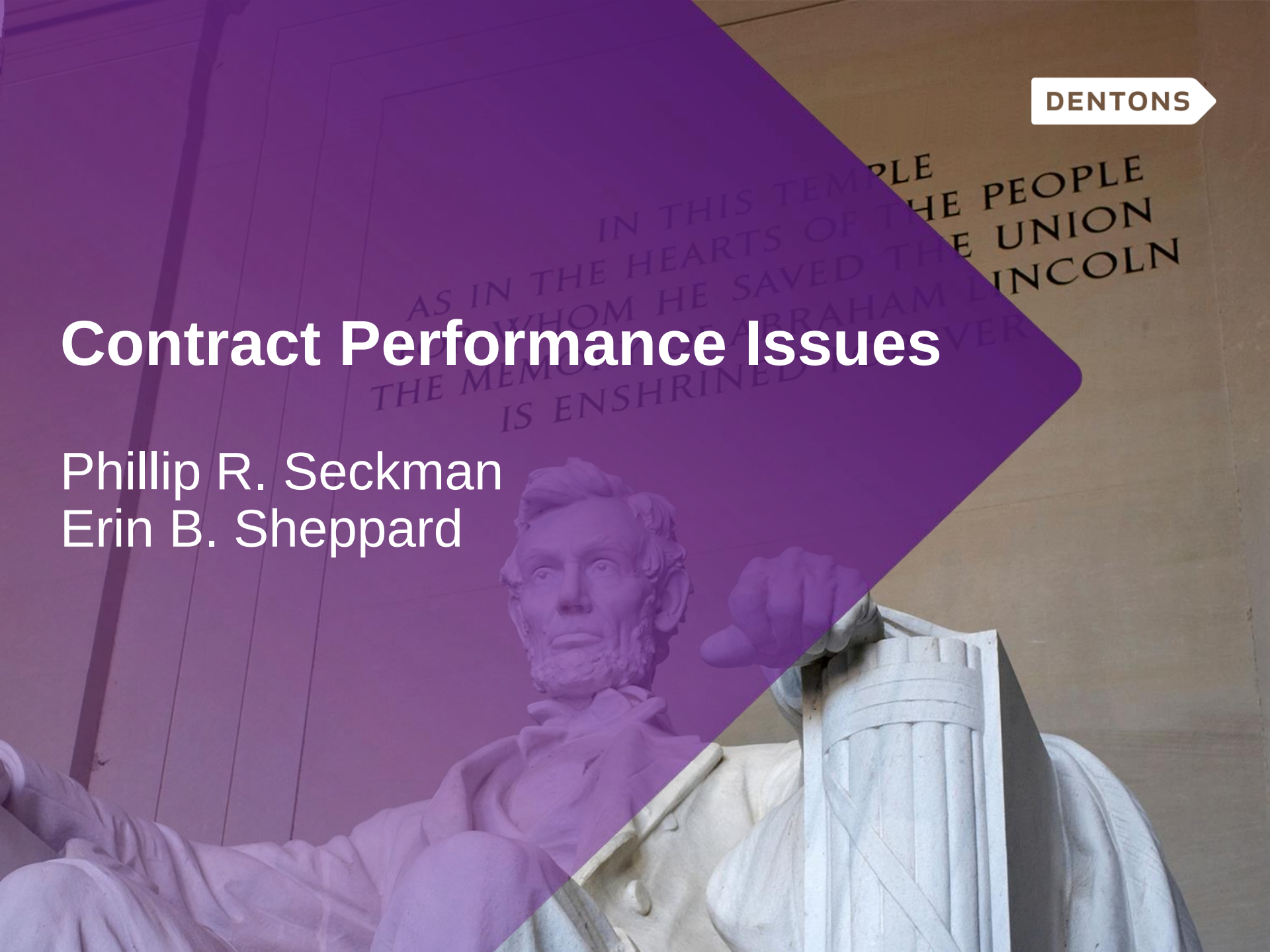

Contract Performance Issues

Phillip R. Seckman
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Key Lessons from a Year in Performance Cases

- Watch what you are waiving
- Representations matter (caveats notwithstanding)
- Know what you are selling
- An option is exactly that
- Stop at your own risk
- CPAR jurisdiction is all bark and little bite
- Go to the right CO
- Not all fraud is created equal
- SOL remains a powerful, though less lethal, arrow in the quiver

Waiver
Watch What You Are Waiving

- Release language did not apply to claim for equitable adjustment, where contractor had notice of increased cost for future order but order was placed after release was signed (*United Launch Servs., LLC*, ASBCA No. 56850, 16-1 BCA ¶ 36,483)
- Clear and unambiguous language in a document such as a contract modification may satisfy requirements of both release and accord and satisfaction (*Military Aircraft Parts*, ASBCA No. 60692, 17-1 BCA ¶ 36,627)

Waiver
Watch What You Are Waiving (cont.)

- Contractor entitled to payment under contract modification rather than termination clause where modification was signed prior to government's improper termination for default converted to termination for convenience (*Paradise Pillow, Inc. v. Gen. Servs. Admin.*, CBCA 5179, 5440, 17-1 BCA ¶ 36,641)
- Clear release language in bilateral settlement agreement bars claims under contracts subject to settlement agreement
- Contractor may be equitably estopped from challenging settlement agreement if it accepts benefits of agreement
- Unconscionability is determined at time parties enter into agreement, and cannot be based on hindsight (*ServiTodo LLC v. Dep't of Health & Human Servs.*, CBCA 5524, 17-1 BCA ¶ 36,672)

Waiver
Watch What You Are Waiving (cont.)

- Tucker Act jurisdiction existed where government breached settlement agreement that did not contain provisions expressly stating availability of monetary remedies because where there is a breach of a government contract, there is a presumption that a damages remedy will be available (*Rocky Mountain Helium, LLC v. United States*, No. 2016-1278, 2016 WL 6775965 (Fed. Cir. Nov. 16, 2016))
- Release language finalizing all actions "under this contract" in task order modification issued in response to REA applied to all claims under task order based upon review of modification language and intent of parties (*Supply & Serv. Team GmbH*, ASBCA No. 59630, 17-1 BCA ¶ 36,678)

Changes
Representations Matter (Caveats Notwithstanding)

- Equitable adjustment available where government misrepresents material facts on which contractor reasonably relies to its detriment
- Contractor entitled to recover for cost of work it was not expected to perform, even if it incurs fewer labor hours than it had bid (*King Aerospace, Inc.*, ASBCA No. 57057, 16-1 BCA ¶ 36,451)

Changes
Representations Matter (cont.)

- Two types of differing site conditions claims
  - Type I: "subsurface or latent physical conditions at the site which differ materially from those indicated in this contract"
    - Conditions indicated in contract differ materially from those encountered
    - Conditions encountered reasonably unforeseeable given the information at time of bidding
    - Contractor reasonably relied upon interpretation of contract
    - Contract was damaged as a result of material variation
  - Fact that representations as to conditions are labeled as "for information only" or that contractor was required to perform further investigation after award does not deprive contractor the right to rely on government's pre-contract representations (*Tetra Tech Facilities Constr., LLC*, ASBCA Nos. 58568, 58845, 16-1 BCA ¶ 36,562)
  - Type II: unknown physical conditions of an unusual nature which differ materially from those ordinarily encountered and generally recognized as inherent in work at the project's location

ID/IQ Contracts
Know What You Are Selling

- Contractor not able to recover costs incurred to develop item anticipated to be used in ID/IQ contract where no line item covered development of item and services were only items priced (*CAE USA, Inc.,* CBCA 4776, 16-1 BCA ¶ 36,377)
- Contracts that lack a guaranteed minimum quantity or any clause requiring government to order all its requirements from the contractor is neither an ID/IQ nor a requirements contract
  - Contractor was entitled to be paid only for the actual work it performed (*ASW Assocs., Inc. v. Envtl. Prot. Agency*, CBCA 2326, 16-1 BCA ¶ 36,453)

Options
An Option Is Exactly That

- Government has broad discretion when exercising options and may decline to do so, absent bad faith, abuse of discretion, or arbitrary or capricious action (*Smart Way Transp. Servs.*, ASBCA No. 60315, 16-1 BCA ¶ 36,569)
- Exercise of an option must be unconditional and in exact accord with the terms of the contract being renewed
  - For example, attempt to renew only portion of space through lease option that contemplated renewal of entire space is not an effective option exercise
  - Alleged verbal agreement concerning the partial option was not binding because the government official lacked authority to modify the lease and parties contemplated a written agreement only (*First Crystal Park Assoc. Ltd. P'ship v. United States*, 130 Fed. Cl. 260 (2017))

Duty to Proceed
Stop at Your Own Risk

- Contractors must perform the contracts they execute and cannot require the government to rewrite the contract so that they can build a project they like better
- Failure to perform due to disagreement with government's project design, rather than excusable causes, may be grounds for default termination (*Indus. Consultants, Inc. DBA W. Fortune & Co.,* ASBCA Nos. 59622, 60491, 17-1 BCA ¶ 36,691)
- Employee strike/resignation may be excuse for delay to the extent contractor's management actions that instigated the strike/resignation were reasonable (*Asheville Jet Charter & Mgmt., Inc.,* CBCA 4079, 16-1 BCA ¶ 36,373)

Duty to Proceed
Stop at Your Own Risk (cont.)

- Contractor is required to perform "at the reasonable direction of the CO," regardless of whether government was using correct inspection standard for aircraft parts (*Precision Standard, Inc.*, ASBCA No. 58135, 16-1 BCA ¶ 36,398)
- Contractor may be precluded from claiming government acted in bad faith when it improperly terminates contract because bilateral modification converting termination to convenience renders moot the challenge to the default termination (*Universal Home Health & Indus. Supplies, Inc.*, CBCA 4012, *et al.*, 16-1 BCA ¶ 36,370)

CPAR System

CPAR Jurisdiction Is All Bark and Little Bite

- Agencies must enter contractor performance evaluations into the CPARS for contracts that exceed simplified acquisition threshold (FAR 42.1502(b)): quality, cost control, schedule, management, small business utilization, etc.
- ASBCA had jurisdiction over claim alleging negative rating via CPARS constituted bad faith and breach of good faith and fair dealing where claim amount was derived by mathematical formula of estimating future expense expected to counter "apparent bad faith libelous actions" of government (*Gov't Servs. Corp.*, ASBCA No. 60367, 16-1 BCA ¶ 36,411)
- Boards of contract appeals may assess whether an unsatisfactory evaluation was arbitrary or capricious
- No jurisdiction to direct government to revise CPARS rating in a particular way through some form of injunctive relief (*CompuCraft, Inc. v. Gen. Servs. Admin.*, CBCA 5516, 17-1 BCA ¶ 36,662)

Picking the Correct Agency
Go to the Right CO

- Two different contracting officers may be involved in a task order issued under a Federal Supply Schedule (FSS) contract with GSA
  - The ordering activity CO
  - The schedule contract CO
- When performing work under a GSA FSS task order, a claim involving the terms of the underlying schedule contract (rather than the performance of the task order) must be filed with GSA CO (*Consultis of San Antonio, Inc. v. Dep't of Veterans Affairs*, CBCA 5458, 2017 WL 1241076 (Civilian B.C.A. Mar. 31, 2017))

Offset
Not All Fraud Is Created Equal

- General rule: ASBCA lacks jurisdiction under CDA over certain fraud-related claims
- However, a prior material breach defense is available to government in CDA cases as matter of federal common law (because it is not a "claim") even if the underlying breach allegation involved fraud (*Laguna Constr. Co. v. Carter*, 828 F.3d 1364 (Fed. Cir. 2016))

Statute of Limitations

SOL Remains a Powerful, Though Less Lethal, Arrow in the Quiver

- Government demand for reimbursement of an alleged overpayment barred by CDA's six-year statute of limitations because government knew or should have known of discrepancy in contractor's vouchers when it paid interim vouchers (*Sparton DeLeon Springs LLC*, ASBCA No. 60416, 17-1 BCA ¶ 36,601)
- Claim for subcontractor costs not barred by CDA SOL because claim accrued when contractor received subcontractor's certified cost claim for the entirety of its costs (*Kellogg Brown & Root Servs., Inc. v. Murphy*, 823 F.3d 622 (Fed. Cir. 2016))

Questions?

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Compliance and Fraud

Mark J. Meagher
Rachel M. Cannon

Overview

- False Claims Act (FCA)
  - 2016 Enforcement Trends
  - Implied Certification: the Supreme Court's *Escobar* Decision
  - FCA Developments
- DOJ Evaluation of Corporate Compliance Programs

2016 Enforcement Trends

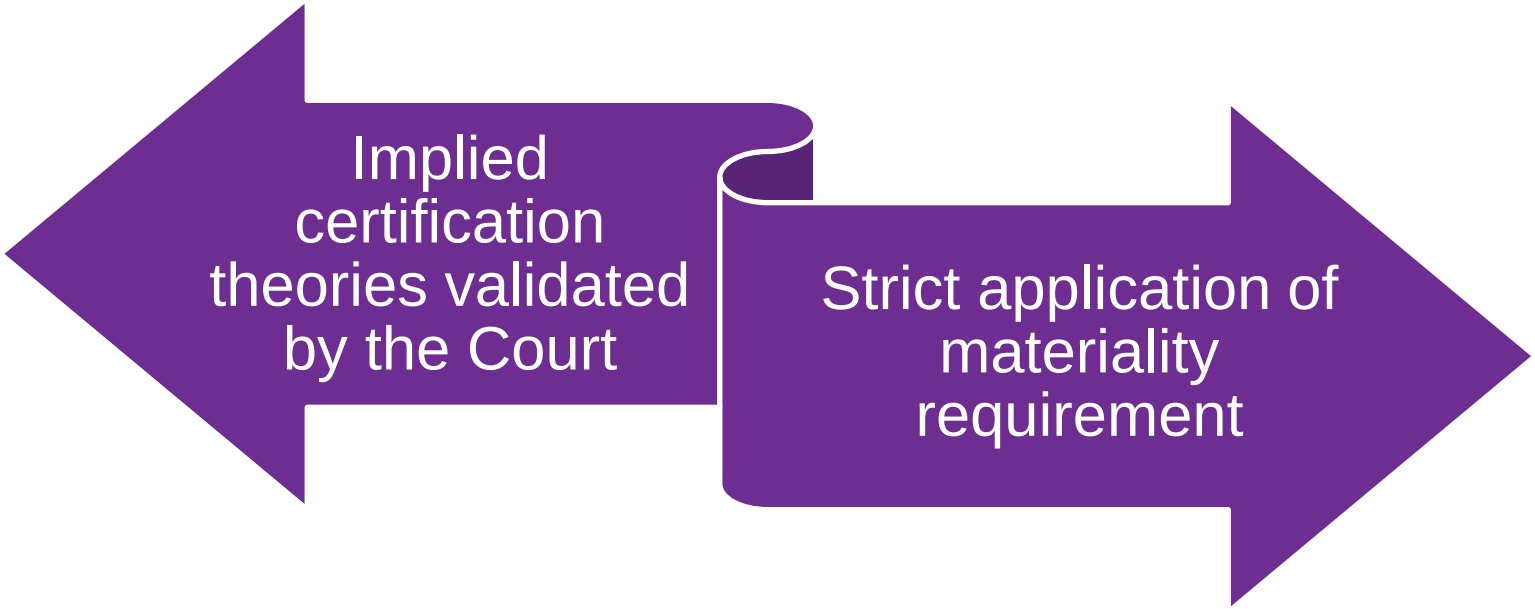
- DOJ recovered over $4.7B in settlements and judgments
  - Fifth year exceeding $3.5B
  - Government contracts recoveries totaled $.5B in FY 2016
  - $1B recovered in non-intervened cases
- Whistleblowers filed 702 *qui tam* suits
  - Slight increase from 638 in 2015
  - DOJ recovered $2.9B from *qui tam* cases
  - Whistleblower awards totaled $519M
- Marked and steady increase since FCA was expanded in 2010

Implied Certification at the Supreme Court

- Implied certification drives significant FCA recoveries
- Creates significant risk to contractors that is hard to quantify; turns contract breach into fraud
- Supreme Court in *Escobar* had the opportunity in 2016 to rein in this risk but validated use of implied certification as appropriate under FCA; proving old adage that "bad facts make bad law"

Implied Certification after *Escobar*

- Supreme Court held in *Escobar* that implied certification is a valid theory but
  - Claim must make specific representation about goods or services
  - Contractor noncompliance must be material to payment claim



Escobar Invigorates FCA Materiality Requirement

- Supreme Court emphasized that materiality is a "rigorous" and "demanding" standard that limits scope of an implied certification
  - FCA is not "an all-purpose anti-fraud statute . . . or a vehicle for punishing garden-variety breaches of contract or regulatory violations"
  - Misrepresentation not always material if government designates compliance with provision as necessary for payment
  - Government having option not to pay ≠ materiality (it may)
  - "Materiality . . . Cannot be found where noncompliance is minor or insubstantial"

Escobar Invigorates FCA Materiality Requirement

- If defendant knows that the government consistently refuses payment for particular noncompliance = possible materiality
- But, if evidence that government has actual knowledge of requirement violation or past violations (with no change in position) and pays claims anyway ≠ materiality
  - Breathing new life into the "government knowledge" defense

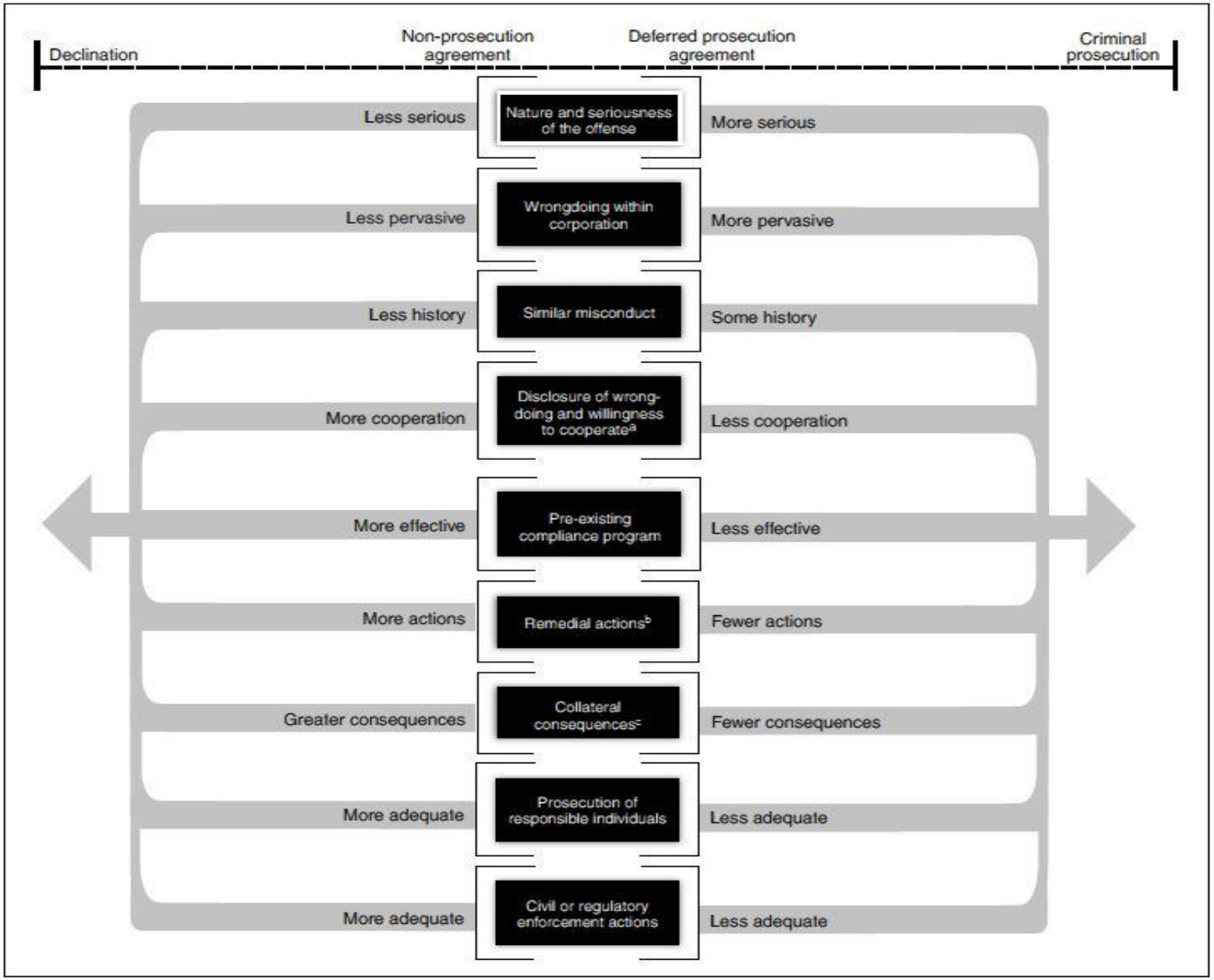
FCA Developments

Recent Settlements/Cases: Examples of Conduct

- $4.6M settlement for using defective steel rebar and quality control failures at nuclear facility (Apr. 24, 2017)
- $1.8M settlement for billing for hours not worked on contract with NIH (Mar. 13, 2017)
- $45M settlement by large technology under GSA schedule contracts for: (i) failing to disclose commercial discounting practices at time of negotiation; and (ii) failing to reduce schedule prices when commercial pricing was lowered after award (Mar. 10, 2017)
- $5.275M settlement by DOE contractor for alleged inflation of overtime and premium pay (Jan. 23, 2017)
- Complaint against Dyncorp for knowingly billing excessive and unsubstantiated subcontract costs and applying mark up (July 19, 2016)

FCA Developments
Statistical Sampling

- Courts faced with use of representative samples to establish
  - Falsity
  - Damages
- *Lawton v. Takeda Pharmaceuticals* (1st Cir. Nov. 22, 2016): rejected relator's attempt to rely upon statistical evidence that Medicare and Medicaid funds were used to pay for prescription drugs



Source: GAO analysis of DOJ's Principles of Federal Prosecution of Business Organizations.

The Best Defense Is a Good Offense

- Develop a Bulletproof Compliance Program
  - High-level commitment from company's board and senior management (i.e. devoting adequate resources to compliance)
  - Well thought-out code of conduct
  - Written policies and procedures for implementing the Code of Conduct
  - Fair and accurate financial recording
  - Periodic risk-based review
  - Proper oversight and independence (i.e. a robust compliance department)
  - Training and guidance (especially to the "little people in the field")
  - Internal reporting and investigation
  - Enforcement and discipline
  - Monitoring and testing
  - Including of third-party relationships, M&A targets

New DOJ Compliance Counsel Position

- In Nov. 2015, DOJ created a compliance counsel position
- Position's mandate is to subject companies' claims about their compliance programs to "rigorous analysis"
  - Companies can receive a sentencing break if they have an effective compliance program under the U.S. Sentencing Guidelines
  - *See* Sue Reisinger, Report: *Justice Dept. Names Chen to Controversial Compliance Counsel Post Corporate Counsel* (Sept. 21, 2015), available at http://www.corpcounsel.com/id=1202737784530/Report-Justice-Dept-Names-Chen-to-Controversial-Compliance-Counsel-Post

DOJ Interview

- Hui Chen: "I think of compliance assessment in a way that may be similar to how an insurance company might risk-assess a car and driver: The various components of the compliance function, such as data analysis and controls and due diligence, are like the control panel, seat-belts, and air bags … None of those … will stop a reckless driver who ignores all the warning signs or drives drunk. So I would argue that, in order to assess a compliance program, not only do you want to check if the panel lights and safety devices are working, but you want to look at the driver's behavior. The driver is the leadership and key stakeholders of the company: Do they pay attention to warnings? Do they maintain the car on schedule? Do they have any qualms about driving while drunk?"

Ethics & Compliance Initiative, *DOJ's Andrew Weissmann and Hi Chen Talk Corporate Compliance in Exclusive Interview* (Feb. 1, 2016), available at https://www.ethics.org/blogs/laura-jacobus/2016/02/01/doj-interview.

Compliance Programs Are Under Scrutiny

- DOJ's Fraud section recently released guidance regarding the factors it considers when evaluating the effectiveness of corporate compliance programs at https://www.justice.gov/criminal-fraud/page/file/937501/download
  - First guidance issued from the Trump Administration
  - Suggests that the government may demand more rigorous compliance programs and corporate investment in compliance to get cooperation credit

Questions?

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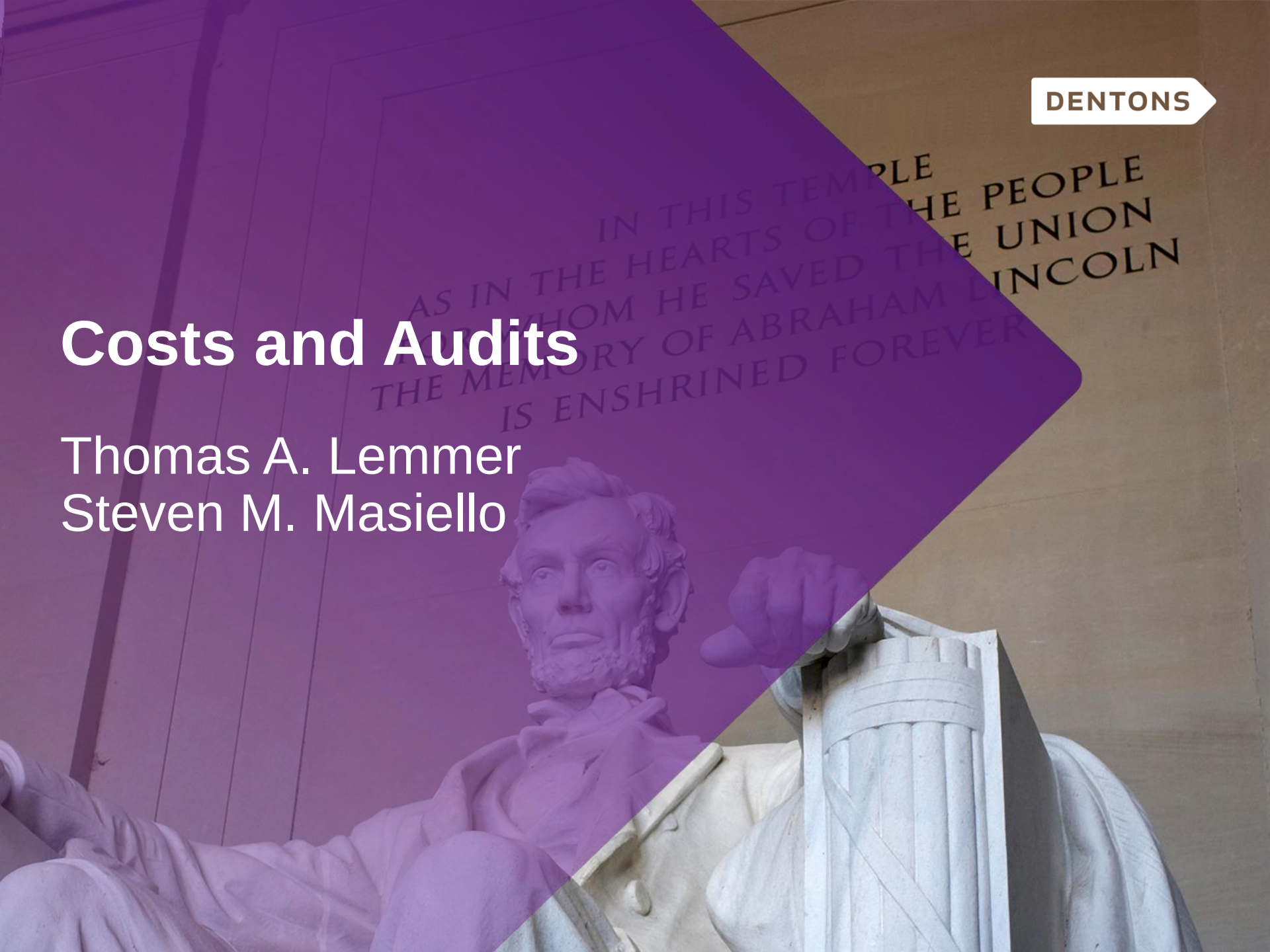

Costs and Audits

Thomas A. Lemmer
Steven M. Masiello

Overview

- IR&D regulatory developments
  - Proposed rule: DFAR 2016-D017
  - Final rule: DFARS 2016-D002
- Statute of limitations
- Cost allowability
- CAS
- Audit trends

Proposed DOD IR&D Rule

- DFARS Case 2016-D017: Proposed Rule, IR&D Expenses, 81 Fed. Reg. 78,014 (Nov. 4, 2016)
  - Requires contractors to
    - Describe the nature and value of prospective IR&D projects
    - Provide cost or pricing data with competitive procurements
  - "[I]ntended purpose of IR&D" is not to gain a price advantage in a specific competitive bid
  - Ignores that contractors are permitted to use IR&D, undertaken at their own risk, to gain a relative price and technical advantage (*Raytheon Co. v. United States*, 809 F.3d 590, 593 (Fed. Cir. 2015))
  - DARC report due date extended to May 17, 2017

Potential, significant uncertainty in near future

DOD Final IR&D Cost Allowability Rule

- DFARS Pt. 231/DFARS Case 2016-D002
  - Effective Nov. 4, 2016
  - Applies to major contractors (more than $11M in IR&D and B&P costs to covered-contracts in prior fiscal year)
  - Requires contractors to communicate new IR&D efforts to appropriate DOD personnel prior to initiation of the investment
  - Facilitates DOD providing industry with feedback

DOD IR&D Final Cost Allowability Rule (cont.)

- IR&D cost allowability contingent on compliance with reporting and oversight requirements
  - Beginning in FY2017, IR&D costs only allowable on DOD contracts if prior to incurring IR&D costs, contractors
    - Provide summary IR&D information to ACO and DCAA
    - Communicate proposed IR&D to DOD through "technical interchange"
    - Deviation for 2017 allows the interchange at any time
  - FY2018: technical interchange must occur prior to start of IR&D project
    - 2018 forward: interchange before incur costs
    - Mechanics are not clear
    - Is it déjà vu to era of government control?

Contractors must engage DOD on IR&D projects

Statute of Limitations

- Contractor submitted vouchers and government paid vouchers, eight years later government asserted costs were unallowable based on audit findings; Board held SOL barred government claim (*Sparton DeLeon Springs, LLC*, ASBCA No. 60416, 17-1 BCA ¶ 36,601)
- Government's failure to challenge costs in prior audits is not enough to bar the government from challenging such costs in the future, instead it requires an unequivocal statement from the government regarding the allowability (*Tech. Sys., Inc.*, ASBCA No. 59577, 2017 WL 372985 (A.S.B.C.A. Jan. 12, 2017))

SOL "claim accrual" authority remains convoluted with uncertain boundaries

Cost Allowability

Multi-Employer Pension Plan Withdrawal Costs

- Entered into fixed-price contract subject to the SCA (FAR 52.222-41, -43)
- Agreed to participate in a multi-employer pension plan
- Deemed withdrawal from plan created withdrawal liability
- Requested a contract adjustment under the SCA
- Federal Circuit denied contract adjustment because withdrawal liability was contractor choice and not due to change in a wage determination

Call Henry, Inc. v. United States, No. 2016-1732, 2017 WL 1521788 (Fed. Cir. Apr. 28, 2017)

Multi-employer pension plan withdrawal liability must be managed

Cost Allowability
Subcontract Costs Under T&M Contracts

- Based on FAR Pt. 42, DCAA questioned a range of claimed subcontractor costs under T&M contract, arguing breach of the following duties
  - Pt. 42 not a term of the prime contract
  - Pt. 42 did not impose any of the alleged cost disallowances

Lockheed Martin Integrated Sys., Inc., ASBCA No. 59508, 17-1 BCA ¶ 36,597

Cost disallowance must have a contractual basis

Cost Allowability
Billing for Subcontract Costs

- Elimination of the "Paid Cost Rule" permits primes to invoice for subcontract/vendor costs before payment in limited circumstances (FAR 52.216-7(b), 52.232-16(a)(2), 52.232-7(a)(2)
  - Pay in accordance with subcontract terms and
  - "Ordinarily" within 30 days of invoicing the government

Cost Allowability
Billing for Subcontract Costs (cont.)

- Potential issues
  - Does "ordinarily" mean 100% of the time?
  - Impact of subcontract terms that require payment by 45 or 60 days?
- Recent uptick in compliance issues under this requirement
  - Cost disallowances
  - Fraud

Ensure that adequate policies and procedures exist and are followed

Subcontractor Costs
Small Businesses

- New FAR 52.242-5 rule
  - Prime contractors must "self-report" reduced or untimely payments to small business subcontractors
  - Explain circumstances
- Contractors with history of "unjustified" reduced or untimely payments may be reported to FAPIIS

Pay your small-business subcontractors on time and implement policy that requires self-reporting

CAS

- CAS Board
  - Met Sept. 29, 2016 for first time since Feb. 2013
  - Addressed proposed changes to exemptions pending since 2011 and 2012; neither substantive
  - Impact of 2017 NDAA uncertain

CAS (cont.)

- Contractor classified a building lease as an operating lease
- Government failed to state a claim for a CAS 404 noncompliance because CAS 404, by its plain language, applies only to tangible capital assets and leases are intangible assets
- Also found that CAS Board intended to allow contractor to determine whether a lease should be treated as a capital lease or an operating lease

Exelis, Inc., ASBCA No. 60131, 16-1 BCA ¶ 36,485

Established limitation on CAS; not all financial accounting issues are CAS governed

Audit Trends
Intercompany Transfers

- FAR 31.205-26(e)
  - Auditors frequently question commercial item transfers between affiliates at price
    - Not the transferor's established practice to transfer at price
    - The item is not a commercial item
    - No affirmative commercial item determination (CID)
- Permitted to transfer at price based on an "established practice" of pricing interorganizational transfers (*A-T Sols., Inc.*, ASBCA No. 59338, 2017 WL 706919 (A.S.B.C.A. Feb. 8, 2017)

Policies and procedures and comply with them

Audit Trends (cont.)

- DCMA's use of decrements as a cost disallowance tool
  - Using decrements to recover alleged unsupported or unallowable costs
  - Government may not unilaterally set final indirect cost rates or disallow direct costs based on decrements
  - Contractors should insist that government cost disallowance claims are supported by specific facts

Must be a logical nexus between disallowance and conduct

Audit Trends (cont.)

- DCAA claims its "only" 18 months behind on its cost audits
- DCAA Cost Audit Manual Reorganization
  - Download old DCAA manual; no longer available on DCAA website
- DCAA emphasis on contractor inclusion of "expressly unallowable costs" continues
  - FAR 42.709 imposes penalties for including expressly unallowable costs in final indirect cost rate proposals

Audit Trends (cont.)

- Hazard and incentive pay uplifts
  - Questioning amounts in excess of DOS allowances
  - DOS allowances are not typically incorporated into contract terms
  - Danger pay not limited to 40 hours a week; include a clear hazard pay policy in proposal or contract indicating whether State Department rates apply

    CACI Int'l Inc. & CACI Techs., Inc., ASBCA No. 60171, 16-1 BCA ¶ 36,442

Audit Trends (cont.)

- Executive compensation
  - DCAA focusing on whether executives are incentivized to control costs
    - Historically, DCAA questioned whether the basis of the award was supported
    - Recently, DCAA has shifted to questioning whether such costs are reasonable

Questions?

DENTONS