



# Government Contracting Update Series

*Stay Current on Federal Contracting Changes & Developments*

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# Agenda

- Regulatory Update
  - Executive Orders Impacting the Federal Regulatory Process
  - Federal Acquisition Regulation (FAR)
  - Defense Federal Acquisition Regulation Supplement (DFARS)
- Notable Legal Decisions

# Regulatory Update

## Executive Order (January 20, 2017) Regulatory Freeze Pending Review

- Send no new regulations to the office of the Federal Register (OFR) until a department or agency head appointed by the President reviews and approves the regulation
- Immediately withdraw any regulations that have been sent to the OFR but not published
- Temporarily postpone the effective dates for rules that have been published in the OFR but have not taken effect to 60 days from the date of the EO for the purpose of reviewing questions of fact, law and policy
- All subject to exceptions including emergency situations or other urgent circumstances relating to health, safety, financial, or national security matters and any regulations subject to statutory or judicial deadlines

## Executive Order (January 30, 2017) Reducing Regulations and Controlling Regulatory Costs

- Requires Executive Departments and Agencies to identify at least two prior regulations to be eliminated to offset the costs of any new regulations
- FY 2017 - Total incremental costs of all new regulations, including repealed regulations, shall be no greater than zero
- FY 2018 and beyond – OMB Director will set the “total amount of incremental costs that will be allowed for each agency in issuing new regulations and repealing regulations for the next fiscal year”
- Exempts rules that are:
  - Required by law
  - Issued with respect to a military, national security, or foreign affairs function of the US
  - Related to agency organization, management, or personnel, or
  - Any other category of regulation exempted by the OMB Director

# Fair Pay and Safe Workplaces (FAR Case 2014-025)

## Amended Final Rule

- FAR Council issued a final rule implementing EO 13673, Fair Pay and Safe Workplaces, on August 25, 2016 (81 FR 58653)
- Eastern District of Texas issued a preliminary injunction on October 24, 2016
  - Prohibits use of FAR clauses for disclosure and restrictions on arbitration
  - Paycheck transparency provision of clause allowed (FAR 52.222-60)
- FAR Council issued memorandum instructing agencies not to use FAR clauses on disclosures and mandatory arbitration on October 25, 2016
- FAR Council amended the final rule on December 16, 2017 to include caveats throughout the rule for each section, provision, and clause that was enjoined by the terms of the Court Order
  1. Contractors must disclose labor law “violations”; included non-final decisions – **STOPPED BY PRELIMINARY INJUNCTION**
  2. Restrictions of the use arbitration with employees for select legal matters - **STOPPED BY PRELIMINARY INJUNCTION**
  3. Paycheck Transparency: specific information required in employees’ and independent contractors’ paychecks – Effective January 1, 2017

# Paid Sick Leave for Federal Contractors (FAR 2017-001) Interim Rule - *Effective January 1, 2017*

- Key Requirements:
  - Minimum annual accrual of 56 hours of sick leave provided to covered employees; 56 hours can be carried over
  - Use of sick leave: specific events identified such as caring for parent, time spent related to domestic violence, sexual assault, or stalking
  - Various employee notification requirements (e.g. posters, notification of rights)
- Covered Contracts: contracts covered by Davis-Bacon Act (DBA) or Service Contract Act (SCA), concessions contracts (contract to use Federal property), contract in connection with Federal property to provide services to Federal employees
- Covered Employees: not all employees of a company; if employee is working on a covered contract and their wages are governed by DBA, SCA, or FLSA
  - Includes employees exempt from FLSA's minimum wage and overtime provisions
  - Includes employees who spend 20% or more of their time in connection with covered contract

Source: Federal Register 81 FR 91627, December 16, 2016

# Contractor Employee Internal Confidentiality Agreements or Statements (FAR 2015-012)

## Final Rule - *Effective January 19, 2017*

- Implements portions of the Consolidated and Further Continuing Appropriations Act of 2015
- Prohibits use of funds, appropriated or otherwise made available, for a contract with any entity that requires employees or subcontractors to sign an internal confidentiality agreement that restricts such employees or subcontractors from lawfully reporting waste, fraud, or abuse to the Government
- Applicable to all solicitations and contracts using FY 2015 or subsequent fiscal year funds that do not already contain a comparable provision/clause

Source: Federal Register 82 FR 4732 January 19, 2017

## 2017 NDAA Sec. 822, Enhanced Competition Requirements Draft Proposed FAR Rule

- Sec. 822 requires:
  - Adequate “competition that results in at least two or more responsive and viable competing bids” is required instead of “price competition” to be exempt from certified cost and pricing data requirements
  - Prime contracts subject to TINA, are responsible for determining whether a subcontractor is exempt under the new “adequate competition” standard
  - Only applicable to DoD, NASA, and the Coast Guard
- FAR Case 2017-006, Exception from Certified Cost or Pricing Data Requirements – Adequate Competition

## 2017 NDAA

### Other Acquisition Related Provisions with New or Pending FAR Cases

Sec.	Title	Synopsis	FAR Case #
816 and 1641	Amendments to Special Emergency Procurement Authority	816 Adds international disaster assistance and emergency or disaster under the Stafford Act 1641 Adds special procurement authority to facilitate defense against or recover from a cyber attack	2017-009
825	Exception to Requirement to Include Cost or Price to the Governments as a Factor in the Evaluation of Proposals for Certain Multiple-Award Task or Delivery Order Contracts	Eliminates the requirement for cost or pricing data for multiple award task or delivery contracts for the same or similar services where the agency intends to award a contract to each qualifying offer	2017-0010
823	Revision to Effective Date of Senior Executive Compensation for Allowable Cost Limitations	Repeals retroactive applicability of 2012 NDAA applicability to contracts	TBD
835	Protection of Task Order Competition	Raises threshold from \$10 to \$25M for protests applicable to DoD, NASA, and the Coast Guard	2017-007

# DFARS IR&D Regulatory Changes

- **IR&D Final Rule: DFARS Case 2016-D002 (Effective November 4, 2016)**
  - For IR&D to be allowable contractors must communicate project with Government prior to expending costs
  - Communication must be documented in DTIC
  - DoD issued a class deviation indicating for FY 2017 the discussion does not have to incur prior to the start of the IR&D project (discussion still must occur) (Class Deviation 2017-O0002)
  - DCMA issued guidance telling ACOs they should inform contractors the communication should be with the Office of the Assistant Secretary of Defense for Research and Engineering (“OASD R&E”)
- **IR&D Proposed Rule: DFARS Case 2016-D006**
  - Contractors’ bid price in competitive procurements will be adjusted for its amount of IR&D investment
  - Proposed Rule is in response to Better Buying Power 3.0 which raised a concern that contractors are reducing their bid price because of promised future IR&D expenditures
  - Only applicable to major defense acquisition programs and major automated information systems

Source: Federal Register 81 FR 78,008, November 4, 2016 and 81 FR 78,014, November 4, 2016

# 2017 NDAA Sec. 824, Treatment of Independent Research and Development Costs on Certain Contracts

## Draft Proposed DFARS Rule

### ➤ Sec. 824 requires:

- 2372, Independent Research and Development Costs – Allowable Costs
  - Requires separate reporting of IR&D
  - Prohibits DoD from implementing regulations that “infringe of the independence of a contractor to choose which technologies to pursue” for IR&D if the contractor’s Chief Executive Officer determines that the expenditures will advance DoD’s need for future technology and advanced capabilities
- 2372a, Bid and Proposal Costs – Allowable Costs
  - Requires separate reporting of B&P
  - Establishes goal to limit DoD reimbursable B&P costs to not more than 1% of the total aggregate industry sales to DoD
  - DoD may not limit payments of allowable B&P costs to meet the goal

### ➤ DFARS Case 2017-D018, Treatment of Incurred IR&D Costs

## 2017 NDAA Sec. 811, Modified Restrictions on Undefined Contractual Actions (UCAs) Draft Proposed DFARS Rule

### ➤ Sec. 811

- Profit on UCAs should accurately reflect the cost risk to the contractor that existed on the date the contractor submitted the qualifying proposal, not date of definitization
- Prohibits contractual extensions > 90 days without a written determination of Secretary of Military Department, Head of Defense agency or Combatant Command, or USD(AT&L)
- Generally prohibits the use of UCAs for FMS

### ➤ DFARS Case 2017-D022, Undefined Contract Actions

## 2017 NDAA Sec. 813, Use of LPTAs Draft Proposed DFARS Rule

### ➤ Sec. 813

- Limits the use of LPTAs in circumstances that would deny the DoD benefits of cost and technical tradeoffs in source selection
- Prohibits, to the maximum extent practicable, the use of LPTAs for acquisition of:
  - IT services, cybersecurity services, systems engineering and technical assistance services, audit or audit readiness service, or other knowledge-based professional services
  - Personal protective equipment
  - Knowledge-based training or logistic services in contingency operations or other operations outside the US, including Afghanistan or Iraq
- New reporting requirement and justification requirement for LPTA awards > \$10M

### ➤ DFARS Case 2017-D017, Use of LPTA Source Selection

# 2017 NDAA Sec. 831, Preference for Performance-Based Contract Payments (PBPs) Draft Proposed DFARS Rule

## ➤ Sec. 831

- Establishes a preference for PBPs
- Requires payments to be based on the “achievement of performance outcomes,” NOT costs incurred
- Imposes commercial best practices eligibility criteria for nontraditional defense contractors and other private sector companies
- Prohibits Government-unique accounting systems or practices but requires accounting system compliance with Generally Accepted Accounting Principles (GAAP)
- Does NOT grant DCAA authority to audit for compliance with GAAP

## ➤ DFARS Case 2017-D019, Performance-Based Payments

# 2017 NDAA Sec. 893, Amendments to Contractor Business Systems Draft Proposed DFARS Rule

## ➤ Sec. 893

- Requires the development of “clear and specific business systems requirements that are identified and made publically available”
- 3<sup>rd</sup> Party Independent Auditors
  - If CPA attests to internal controls pursuant to Sec. 404(b) of Sarbanes-Oxley Act of 2002, contractor can provide “CPA certified documentation” that the contractor meets the business system requirements and no further review by DoD
  - Non-covered contractors review limited to confirmation that the contractor uses the same contractor business systems for its Government and commercial work and that the outputs of the business systems are reasonable based on statistical sampling
- Further limits applicability to contractors with covered contracts with the USG > 1% of total gross revenue

## ➤ DFARS Case 2017-D021, Contractor Business Systems

## 2017 NDAA Sec. 820, Defense Cost Accounting Standards Draft Proposed FAR/ DFARS Rule TBD

- **Sec. 820 – For existing Cost Accounting Standards Board (CASB)**
  - Ensure that cost accounting standards used by Federal Contractors rely, to the maximum extent practicable, on commercial standards and accounting practices and systems
  - Continually review and conform standards, where practicable, to GAAP
  - Annually review disputes involving the standards brought before the Board or Federal courts and consider whether clarity is needed to avoid future disputes
  - Meet at least once each quarter and publish a notice an agenda in the Federal Register before each meeting
  - Annual report describing actions taken to conform standards to GAAP and minimize the burden on contractors

## 2017 NDAA Sec. 820, Defense Cost Accounting Standards Continued

### ➤ Sec. 820 – New Defense Cost Accounting Standards Board (CASB)

- Duties:
  - Review and recommend changes to the CASB
  - Exclusive authority for DoD to “implement” CAS to achieve uniformity and consistency in the standards governing measurement, assignment, and allocation of costs to DoD contracts
  - Develop standards to ensure that the “commercial operations performed by Government employees” at DoD adhere cost accounting standards (CAS or GAAP) that inform managerial decisionmaking

## 2017 NDAA Sec. 820, Defense Cost Accounting Standards Continued

### ➤ Sec. 820 – Auditing Requirements

- Subject to other provisions of law, Defense contractors “may present” and DCAA “shall accept” without performing additional audits, a summary of audit findings prepared by a commercial auditor if the:
  - Auditor performed an audit of the allowability, measurement, assignment to accounting periods, and allocation of indirect costs, and
  - Audit was performed using relevant commercial accounting standards (such as GAAP) and relevant commercial auditing standards
- DCAA must rely on the 3<sup>rd</sup> party indirect cost audits but may audit the direct costs of DoD contracts
- But if the company has a predominance of cost-type contracts as a percentage of sales, DCAA can audit both direct and indirect costs

## 2017 NDAA

### Other Acquisition Related Provisions with Pending DFARS Cases

2017 NDAA Sec.	Title	Synopsis	DFARS Case #
821	Increased Micro-Purchase Threshold Applicable to DoD Procurements	Establishes a \$5,000 micro-purchase threshold for DoD	2017-D027
829/ 830	Preference for Fixed-Price Contracts/Requirement to Use Firm Fixed-Price Contracts for FMS	Establishes preference for FP contracts and requires review and approval for certain contract types and specified thresholds/Requires FFP for FMS unless exception or waiver	2017-0024/25
836	Contract Closeout Authority	Permits closeout of certain contracts or groups of contracts without completing a reconciliation audit or other effort	2017-D026
871, 872, 876-878	Acquisition of Commercial Items	Multiple requirements	2017-D020

# **Notable Legal Decisions**

## Notable Legal Decisions

*Lockheed Martin Integrated Systems, Inc.*, ASBCA Nos. 59508, 59509 (Dec. 20, 2016)

- Two government claims totaling ~\$117M arising from subcontracts
  - Contracting Officer's Final Decision on direct subcontract costs rested on DCAA audit, and Government complaint provided nothing more than conclusory statement that its claim was "based on the difference between appellant's proposed amounts and actual costs under the subcontracts."
    - Failure to state a claim:
      - Audit report did not explain grounds on which assist audits questioned subcontractor costs
      - Provides no facts to substantiate the differences between the LM proposal and the subcontract costs
      - Contracting Officer's Final Decision cited no fact – only the DCAA's unsupported conclusions
      - Neither the Government's Complaint nor the Contracting Officer's Final Decision contained sufficient factual or legal allegations to state a claim

## Notable Legal Decisions

### *Lockheed Martin Integrated Systems, Inc.*, ASBCA Nos. 59508, 59509 (Dec. 20, 2016)

Contracting Officer Final Decision alleged breach of contract: failure to manage subcontractors per FAR 42.202(e)(2)

- Both Complaint and Contracting Officer Final Decision relied heavily on DCAA Audit
  - asserted obligation to retain documentation substantiating invoices for subcontractor direct labor
  - asserted obligation to retain documentation showing LMSI caused subcontractors to make incurred cost submissions and to audit them or get DCAA to audit them
- FAR 42.202(e)(2) not incorporated by reference in the contract
  - Contractor had not obligation or duty
  - No inherent or implied obligation
- Contracting Officer's Final Decision and the Complaint did not cite a contract provision giving rise to an obligation
- Government did not allege that LMIS failed to maintain records per Audit Clause or Payments Clause
- Government made a patent mischaracterization of a Board decision for purposes of demonstrating an obligation to manage subcontractors.
- Government "has gone forward with a claim for over \$100,000,000 that is based on nothing more than a plainly invalid legal theory."

## Notable Legal Decisions

- *Sparton DeLeon Springs, LLC*, ASBCA No. 60416 (Dec. 28, 2016)
- Statute of Limitations involving intra-company costs
- Government claimed that costs were unallowable and insufficiently supported
  - Costs were not included in Schedule I or any updates to Schedule I
  - Government had paid the costs by interim vouchers, which included the costs at issue and information related to the intra-company costs
    - Insufficient support would have been evident by interim vouchers, as well as the subsequent final vouchers
    - Government knew or should have known when it paid the interim vouchers, which was more than six years prior to the Government claim.
  - Government's right to adjust overpayments under the Allowable Cost & Payment clause does not trump the statute of limitations
  - Delay in auditing the interim vouchers does not suspend the statute of limitations

## Notable Legal Decisions

- *Technology Systems Inc.*, ASBCA No. 59577 (Jan. 12, 2017)
  
- Five-member panel decision with dissent. – Allowability of several types of cost
  - Major procedural/doctrinal issues: Doctrine of Retroactive Disallowance; Course of Dealing; Statute of Limitations
  - Cost types: Consultant Services; Depreciation; Executive Bonuses; Legal Fees; Subcontractor costs

## Notable Legal Decisions

### Majority

- Doctrine of Retroactive
- Disallowance is a form of estoppel that requires showing of Government affirmative misconduct – not demonstrated

### Dissent

- Doctrine of Retroactive Disallowance is different from estoppel (only prevents recovery for previous approvals up to notice that government is imposing a new standard) and does not require affirmative misconduct.
  - Here the government changed the acceptable documentary support for the first time.
  - Retroactive Disallowance would make the costs allowable.

## Notable Legal Decisions

### Majority

- Course of Dealing: sequence of previous conduct between the parties to an agreement which establishes a common basis of understanding
  - DCAA's failure to question certain costs in prior audits does not equate to course of dealing
  - Would require DCAA to question every cost
  - Silence cannot reasonably be a common understanding

### Dissent

- Course of Dealing: Actions of DCAA and DCMA were imputed to the Navy & its contract
  - DCAA audited to FAR part 31, which had not changed significantly from 2002- 2007
  - Both sides understood the significance of the audits, the standards imposed, and the acceptance without question in prior years – shows mutuality
  - Prior audits and desk reviews created prior understanding about sufficient documentation

## Notable Legal Decisions

### Majority

- Statute of Limitations
- Cannot run prior to submission of Incurred Cost Proposal – could not be approved or disapproved until submitted
- Knowing particulars about the type of costs from prior year audits “might” have a bearing whether government knew or should have known of dubious costs
- Claim was filed one week shy of the six year limitation

### Dissent

- Statute of Limitations
- Government claim was one week within the six years from the ICP

## Notable Legal Decisions

### Majority

- Consultant Services: Marketing
  - FAR 31.205-33(f) : evidence of agreements, invoices/billings, work product
  - “Shall” does not require work product where none was created
  - Invoices, agreements and testimony were enough to meet the standard for allowability
  - DCAM – should not insist on work product if other evidence demonstrates nature of work performed

### Dissent

- Consultant Services
  - Would have been allowable under retroactive disallowance or course of dealing

## Notable Legal Decisions

### Majority

- Depreciation
- Practice in 2007 ICP was inconsistent with prior long-term practice; therefore, unallowable under FAR 31.205-11(c)

### Dissent

- Depreciation
- Allowable under Retroactive Disallowance or Course of Dealing

## Notable Legal Decisions

### Majority

- Travel
- Costs unallowable to the extent exceeded per-diem
- Saving government money was not proven, and is not an exception under FAR 31.205-45(a)(3)(ii)

### Dissent

- Travel
- Would disallow costs above per diem as expressly unallowable – excluded from retroactive disallowance and course of dealing

## Notable Legal Decisions

### Majority

- Executive Bonuses
- One-page memorandum was “utterly lacking in clearly defined criteria for making bonus decisions” – left to the unfettered decision of those receiving the benefits
- Lack of specificity and constraints rendered unallowable under FAR 31.206-6(f)

### Dissent

- Executive Bonuses
- Allowable
- Formality demanded by DCMA was unreasonable for a company with less than 20 employees
- Agreement existed prior to 2007
- Testimony as evidence
- Consistent application is an alternative to an actual agreement

## Notable Legal Decisions

### Majority

- Legal Fees
- Legal fees for an investigation were not expensed to the wrong year
  - Costs had been segregated per FAR 31.205-47(g)
  - Contractor was reasonable in waiting for return of documents as confirmation that investigation was over and could expense in that period, rather than period when notified that investigation was over

### Dissent

- Legal Fees
- Notice of terminated investigation, involving two parties was not provided to both and was unclear; therefore, reasonable to wait for documents returned until claiming legal fees

## Notable Legal Decisions

### Majority

- Subcontract costs
- Unallowable – were not rpe-approved by the ACO per subcontract clause incorporated into the contract.

### Dissent

- Subcontract Costs
- Allowable per Retroactive Disallowance or Course of Dealing.

## Contact Information

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