

PCI Supply Chain Symposium

Prime Contractor Responsibility for Foreign Content: A Primer on the Buy America Act and Trade Agreements Act and Their Application to Subcontracts

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Kevin J. Slattum

Selena M. Brady

Goals

- Learn about the restrictions and application of various country of origin regimes
- Understand how the Government enforces and resolves violations
- Learn about contractor obligations and common challenges in compliance
- Gain insights to implement best practices and to avoid common pitfalls

Agenda

- Country of Origin Restrictions
- Government Enforcement
- Contractor Obligations and Challenges
- Best Practices

COUNTRY OF ORIGIN RESTRICTIONS

Buy American Act (BAA)

- Buy American Act of 1933, 41 U.S.C. § 8301, et seq.
 - See FAR 25.1; Contract Clauses at FAR 52.225-1 and -2 (certification)
- The BAA applies to U.S. government acquisitions over the micro-purchase threshold (currently \$3,500)
 - Unless the Trade Agreements Act applies and waives the BAA
- The BAA does not prohibit a federal agency from purchasing a foreign product, but imposes a price penalty on offers
 - If domestic offer is not the low offer, the contracting agency must add a certain percentage to the low offer's price before determining which offer is the lowest priced
 - For civilian contracts, 6% (large business) or 12% (small business) are added during evaluation factor, FAR 25.105
 - For DoD contracts, 50% is added during evaluation, DFARS 225.105

Buy American Act

- The BAA limits acquisition to “domestic end products” meaning products that are:
 - Manufactured in the U.S.; and
 - At least 50% of components are U.S.-made
 - FAR 25.101
- 50% component test is waived for commercially available off the shelf items (COTS) items

Buy American Act – “Manufactured”

- No definition of “Manufactured” in the BAA or the FAR
- Considered “less stringent” than the Trade Agreements Act substantial transformation test
- Tribunals have considered the following:
 - Whether there were substantial changes in physical character
 - Whether separate manufacturing stages were involved
 - Whether the article is completed in the form required by the government
- Examples:
 - General Kinetics, Inc., Cryptek Div., B-242052.2 (1991)
 - Bell Helicopter, B-195268 (1979)

Buy American Act – 50% Component Test

- **Component** = any article, mat'l, or supply incorporated directly into end product or construction mat'l, FAR 25.003
- Cost=Acquisition cost for the contractor of either (1) purchase or (2) manufacture
- Component test waived for COTS items, defined as:
 - A “commercial item”;
 - Items customarily used by the general public that have either been sold, leased, or licensed to the public, or offered as such;
 - Sold in substantial quantities in the commercial marketplace; and
 - Not modified/customized for the Government

Buy American Act - Exceptions

- Public interest
- Nonavailability
 - Class determinations, listed in FAR Part 25.104
 - Individual determinations
- Unreasonable cost
- Commissary resale
- Information technology that is a commercial item
 - “any equipment, or interconnected system(s) or subsystem(s) of equipment,” used by the agency in acquiring, storing, managing, transmitting, etc. data or information
 - Does not include equipment that contains imbedded IT used as an integral part of the product, but the principal function of which is not the acquisition, storage...of data or information

Trade Agreements Act (TAA)

- TAA = Waiver of BAA + *Prohibition* on Acquisitions of Supplies/Services from Countries Not Approved (“Designated”)
- The TAA gave authority to waive BAA requirements for certain procurements above the TAA dollar threshold



- Most of dollar thresholds are subject to revision by the U.S. Trade Representative approx. every 2 yrs.
- Implemented by FAR 52.225-5, 52.225-6 (certification)

Trade Agreements Act

FAR 25.400: TAA applicable to acquisitions covered by:

- The World Trade Organization Government Procurement Agreement
- Free Trade Agreements, including
 - NAFTA, Chile FTA, Singapore FTA, Australia FTA, Morocco FTA, CAFTA FTA (Costa Rica, Dominican Republic-Central America-U.S. Free Trade Agreement), Bahrain FTA, Oman FTA, Peru FTA, Korea FTA, Colombia FTA, Panama FTA
- Least developed country designation made by the U.S. Trade Representative pursuant to the Trade Agreements Act
- The Caribbean Trade Initiative
- The Israeli Trade Act
- The Agreement on Trade in Civil Aircraft

Trade Agreements Act - Thresholds

| Trade Agreement | Supply | Service | Construction |
|-------------------|-----------|-----------|--------------|
| WTO GPA | \$191,000 | \$191,000 | \$7,358,000 |
| Australia FTA | \$77,533 | \$77,494 | \$7,358,000 |
| Bahrain FTA | \$191,000 | \$191,000 | \$10,079,365 |
| CAFTA-DR | \$77,533 | \$77,533 | \$7,358,000 |
| Chile FTA | \$77,533 | \$77,533 | \$7,358,000 |
| Columbia FTA | \$77,533 | \$77,533 | \$7,358,000 |
| Korean FTA | \$100,000 | \$100,000 | \$7,358,000 |
| Morocco FTA | \$191,000 | \$191,000 | \$7,358,000 |
| NAFTA | | | |
| --Canada | \$25,000 | \$77,533 | \$10,079,365 |
| --Mexico | \$77,533 | \$77,533 | \$10,079,365 |
| Oman FTA | \$191,000 | \$191,000 | \$10,079,365 |
| Panama FTA | \$191,000 | \$191,000 | \$7,358,000 |
| Peru FTA | \$191,000 | \$191,000 | \$7,358,000 |
| Singapore | \$77,533 | \$77,533 | \$7,358,000 |
| Israeli Trade Act | \$50,000 | -- | -- |

Trade Agreements Act: Basic Requirement

- **Prohibits** use of products that are not U.S.-made end products or designated country end products
 - Designated countries do not include China, India, Indonesia, Malaysia, Pakistan, Russia, Thailand, among others
 - FAR 25.003 includes list of designated countries
- A designated country end product is either:
 - Wholly the growth, product or manufacture of that country; or
 - Substantially transformed in that country into a new and different article of commerce

Substantial Transformation

- Occurs when an item is transformed into a new and different article of commerce with a **name**, **character**, or **use** distinct from that of the article or articles from which it was transformed
 - a complex and meaningful operation which resulted in a change of character, use, and name
- Generally, minimal or simple assembly operations are insufficient
- Factors include the nature and number of operations involved, resources expended on design/development, degree of skill needed, etc.
- All three elements, relating to name, character, and use need not be met when determining substantial transformation. See *SDI Techs, Inc. v. U.S.*, 977 F. Supp. 1235, 1239 (Ct. Int'l Trade 1997)

Substantial Transformation

- The U.S. Customs and Border Patrol (CBP) has statutory authority to issue advisory opinions and final determinations on a product's country of origin.
 - 19 C.F.R. Part 177, Subpart B
 - Rulings for specific end products and manufacturing processes are in a searchable database available at <http://rulings.customs.gov/>.
- Reviewed on a case-by-case basis looking at totality of circumstances
 - Generally, merely packaging parts of a kit together does not constitute a substantial transformation
 - Cases have also generally held that assembly of large number of fabricated components onto a PCB involving a considerable amount of time and skill does constitute substantial transformation
- Government contracts tribunals give exceptional weight to CBP Rulings, but they do make independent determinations

Substantial Transformation - Examples

YES

- Jumbo filler paper was substantially transformed when manufactured into composition and spiral notebooks. The multi-step processes of printing, cutting, perforating, punching, sorting, counting, binding, and final assembly results in separate and distinct articles of commerce. HQ H066155 (Oct. 27, 2009)
- Components used to manufacture exercise bikes were substantially transformed because of assembly operations consisting of approximately 468 steps and over 270 U.S. and foreign components. HQ H095239 (June 2, 2010).

NO

- “Mere assembly” of components of cut fabric for a laptop case, entailing simple combining operations, trimming and joining together by sewing, does not involve sufficient skill or complexity to effect a substantial transformation. HQ958222 (July 28, 1995).
- The assembly of electrical connectors and electrical connectors with a cable did not result in a substantial transformation as the assembly involved a small number of components and were merely attached, inserted, and affixed to one another to form the components. The operations did not involve a considerable amount of time, skill, attention to detail or quality control. HQ 556020 (July 1, 1991).

Additional Country of Origin Restrictions

American Recovery and Reinvestment Act of 2009

- Applies to construction projects that use funds appropriated or otherwise provided by the Recovery Act
- Requires all of the iron, steel, and manufactured goods used as construction material to be produced or manufactured in the US
- If construction contract above the TAA threshold, manufactured construction material may be a product of a designated country

Additional Country of Origin Restrictions

- Department of Transportation - special restrictions attach to federal funds to states for mass transit and highway projects
 - Federal Aviation Administration, 49 U.S.C. § 50101
 - Federal Transit Administration, 49 U.S.C. § 5323(j), 49 C.F.R. Part 661
 - Federal Highway Administration, 23 U.S.C. § 313, 23 C.F.R. § 635.410
 - Federal Railroad Administration High Speed Rail Program, 49 U.S.C. § 24405
 - Amtrak, 49 U.S.C. § 24305
- USAID, 22 U.S.C. § 2354
- Foreign Military Financing Program

GOVERNMENT ENFORCEMENT

Enforcement Mechanisms

The Government can use multiple mechanisms to enforce country of origin restrictions, including:

- Audits and investigations
 - GAO, Agency IG, and DOJ at Federal level
 - Auditors and investigators at state/local level
- False Claims Act
- Suspension/Debarment
- Termination
- Negative Past Performance
- Bid Protests
- Mandatory Disclosures

False Claims Act (FCA)

- The civil False Claims Act is a federal law that allows the government or individuals (via *qui tam* action) to file suit against contractors, alleging fraud against the federal government
 - Prohibits the knowing submission of a false claim
 - A claim is “knowing” if it is made with actual knowledge, deliberate ignorance, or reckless disregard for its truth or falsity (i.e., failing to take steps to ensure the claim was proper)
- As of Aug. 1, 2016, FCA civil penalties range from \$10,781.40- \$21,562.80 per claim, plus 3X damages sustained by federal government because of the false claim

Recent Enforcement Actions

- **Medtronic plc (April 2015)**
 - Alleged between 2007 and 2014, Medtronic sold to the VA and DoD products it falsely certified would be made in the United States or other designated countries.
 - \$4.41 million civil penalty
- **Smith & Nephew Inc. (Sept. 2014)**
 - Paid \$8.3 million to settle a False Claims Act lawsuit stemming from a 2008 disclosure to DoD and VA regarding medical tools that did not comply with country of origin requirements.
- **Samsung Electronics America (Aug. 2014)**
 - Samsung certifies to authorized resellers with GSA contracts that they will provide TAA compliant products and resellers in turn list those products on their GSA.
 - Settlement resolves FCA allegations that from Jan. 2005 – Aug. 2013, Samsung caused resellers to violate TAA by knowingly providing inaccurate information regarding the COO of the goods
 - \$2.3 million settlement

Other Potential Problems

■ Bid Protests

- Competitor can challenge award to contractor on country of origin basis
- Successful protest can result in termination of contract
- *Wyse Technology, Inc.*, B-29745, January 24, 2006, the Government Accountability Office sustained a bid protest because the awardee did not certify that the product would comply with the TAA as required by the terms of the solicitation and the agency failed to ensure this compliance.

■ Indemnification of Resellers

- Reseller agreement may require indemnification if products are not compliant with country of origin requirements

Federal Supply Schedule (FSS) Contracts

- **May 2016** – the General Services Administration (GSA) sent thousands of FSS contract holders a notice requiring them to verify the country of origin for all products on their FSS contracts
 - GSA response to multiple Congressional inquiries and FOIA requests on failed compliance with TAA and “Made in America” designations
- The notice led many GSA schedule holders to review supply chain for TAA compliance, including products supplied by third parties
- **June 2016** -- The Department of Veteran Affairs (VA) required all TAA non-compliant pharmaceuticals be placed on an FSS contract or interim agreement
 - Implements significant change in TAA policy announced in April 2016

CONTRACTOR OBLIGATIONS AND CHALLENGES

Contractor Obligations

- Compliance with the particular country of origin regime
 - Includes supplier or vendor compliance, where applicable
- Ensure accuracy in all written and oral submissions
 - Certifications directly to federal or state agencies
 - Certifications to higher tier contractors
 - Certifications by suppliers and vendors
- Disclosing violations, if any
 - Mandatory Disclosure, FAR 52.203-13
 - “Credible Evidence” of FCA violation, overpayments

Common Challenges with Compliance

- **Determining Which Restrictions Apply**
 - Navigating the different country of origin regimes is challenging, given their complexity and differences
 - Federal contracts sometimes include conflicting information, which requires follow-up
- **Different Restrictions Results In Different Compliance of Same End Products**
 - Under the different regimes, the answers may be different for the same products. Contractors may need to undertake multiple analyses for the same products, depending on contract requirements
- **Broad Certifications**
 - Suppliers or vendors make broad certifications that do not distinguish between BAA, TAA and other standards

Common Challenges with Compliance

- **Changes To Country Of Origin**
 - Often contractors lack a good process for obtaining updated product country of origin data and details or fail to maintain records
- **Inventory and Management Issues**
 - Inventory control issues and SKU management issues leading to a mix-up of products, particularly in the event of dual sourcing
- **Flow Downs to suppliers and vendors**
 - Contractors sometimes lack a good process for flowing down the requirements or later identifying non-compliant suppliers or vendors

BEST PRACTICES

Compliance Starts with the Solicitation

Compliance must be a priority **even before** contract award

- Verify applicability of country of origin Laws - review contract solicitations for whether BAA and/or TAA are included
 - Note that both clauses should not be present, as the TAA waives the applicability of the BAA
 - When in doubt, ask questions and confirm with agency
- Prepare a bid/offer that will lead to compliance, analyzing products offered under the solicitation
- Complete a certificate, if necessary
- Be aware that laws could potentially apply to state/local projects funded by the federal government
 - Also look for any similar state/local domestic preference statutes that may be applicable
 - While largely limited to the construction context, there have been recent efforts to pass more broad domestic preference legislation

Internal Compliance Process

Vendor Compliance

- Require that vendors and suppliers offer compliant items
 - Have process for all vendors to complete a vendor questionnaire confirming the country of origin
 - Check publicly available information to confirm vendor manufacturing sites
 - Escalate issues to legal or compliance department where it appears a vendor has manufacturing operations in non-TAA designated countries
- Have a process in place to analyze quotes and purchase orders for compliant products
- Require suppliers to certify that their offers comply with the BAA/TAA and that their country-of-origin statements are accurate

Internal Compliance Process

Reseller Compliance

- Confirm whether reseller will be selling items on FSS contract, a federal contract or a state/local contract
- Ensure reseller agreements require reseller to inform contractor of BAA/TAA requirements
- Do not issue letters of supply or other certifications without proper review of products provided, if questions consult legal or compliance

Recordkeeping

- Obtain and maintain records for each vendor or supplier
 - Obtain certification of country or origin compliance from vendors and suppliers
 - Require follow-up from vendors and suppliers to provide updates of the certifications or require that they provide updated information every time a product's country of origin changes
- Maintain a system capable of tracking and archiving country of origin information for each SKU/end product
 - If applicable, when the same product is supplied by multiple sources, segregate products provided from compliant and non-compliant sources to ensure that only compliant products are delivered to federal purchasers

Ongoing Monitoring

- Ensure all teams (contracts, program, subcontracts, sourcing) know that country of origin restrictions are part of certain contracts, *before* commencing contract performance
- Regularly review or audit purchasing documents to confirm only compliant products have been purchased or otherwise acquired for the contract
- Regularly review contract file to confirm only compliant products have been provided to the Government
- Where applicable, investigate activities or omissions
- Provide training to employees annually, and as needed

Presenters



Kevin J. Slattum

kevin.slattum@pillsburylaw.com



Selena M. Brady

selena.brady@pillsburylaw.com