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E-ALERT | Government Contracts

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THE GOVERNMENT CONTRACTS UPDATE

OMB PROPOSES REFORM OF FEDERAL POLICIES RELATING TO GRANT-MAKING

On February 1, 2013, the Office of Management and Budget (OMB) published a federal grant reform proposal entitled "Proposed Uniform Guidance: Cost Principles, Audit, and Administrative Requirements for Federal Awards." OMB proposes to streamline and consolidate eight existing OMB Circulars into a single uniform set of administrative requirements, cost principles, and audit requirements for grant recipients. OMB also proposes to clarify where separate policy provisions exist for different types of entities. The proposal includes a "crosswalk" from existing guidance to proposed guidance that identifies the proposed policy changes, clarifications, and updates to policy provisions.

Among the reforms proposed are the following:

- Reforms to Administrative Requirements: Changes to Circulars A-102, A-110, and A-89, including requiring pre-award consideration of each proposal's merit and each applicant's financial risk; establishing a general 30-day public notice requirement for funding opportunities; and consolidating the requirements for categories of information to be published in announcements of funding opportunities.
- Reforms to Cost Principles for educational institutions, state, local, and tribal governments, and non-profit entities: Changes to Circulars A-21, A-87, and A-122, including offering all entities the option of extending negotiated rates for indirect costs for up to four years, subject to approval; clarifying the circumstances under which administrative support and certain other costs should be allocated as direct costs; clarifying the threshold for allowable maximum residual inventory; and allowing for the budgeting of contingency funds.
- Reforms to Audit Requirements: Changes to Circulars A-133 and A-50, including raising the Single Audit threshold so that the Government can concentrate oversight resources on higher-dollar, higher-risk awards; streamlining the A-133 Compliance Supplement for entities undergoing a Single Audit; and strengthening guidance on audit follow-up and resolution.

While OMB's objectives appear laudable, these proposed changes, if implemented, are likely to have a significant impact on federal agencies and their grant recipients. OMB is accepting comments on the proposed reforms through May 2, 2013.

FAR COUNCIL FINALIZES THE REINSTATED "INVERTED DOMESTIC CORPORATIONS" PROHIBITION

On January 29, 2013, the FAR Council adopted, without change, an interim rule that prohibits the award of government contracts to an "inverted domestic corporation" — that is, a foreign incorporated entity or partnership that formerly was organized in the United States. The restriction extends to subsidiaries of inverted domestic corporations. The rule is intended to avoid the award of government contracts to companies that have relocated overseas to avoid U.S. tax obligations. This

rule was introduced in May 2012 to implement a section of the Consolidated Appropriations Act of 2012 and reinstates restrictions in place between 2008 and 2010. Under the rule, by submission of its offer to the government, a prime contractor represents that it is not an inverted domestic corporation or the subsidiary of such a corporation. A contracting officer may rely on this representation.

NATIONAL DEFENSE AUTHORIZATION ACT REMOVES MAXIMUM AWARD PRICE FOR WOMEN-OWNED SMALL BUSINESSES

The 2013 National Defense Authorization Act (NDAA), which we reported on in the January 11, 2013 edition of The Government Contracts Update, changed the U.S. Small Business Administration's (SBA) Women-Owned Small Business Federal Contract Program. The NDAA removed the maximum award price on contracts set aside for women-owned small businesses or economically disadvantaged women-owned small businesses. Previously, such awards could not exceed $6.5 million for manufacturing contracts and $4 million for all other contracts. The NDAA also requires the SBA to conduct another study to identify and report industries underrepresented by women-owned small businesses.

COURT OF FEDERAL CLAIMS REJECTS INDEMNIFICATION OF ENVIRONMENTAL COSTS UNDER TAX-RELATED CONTRACT CLAUSE AND FOR TERMINATED CONTRACTS

In a January 14, 2013 decision in *Shell Oil Co., et al v. United States*, the Court of Federal Claims rejected claims that World War II-era government contracts indemnified plaintiffs for $92 million in environmental clean-up costs at sites contaminated by aviation fuel. The contracts were base-price supply contracts with certain cost-adjustment clauses, including a "Taxes" clause in which the government agreed to pay for the cost of aviation fuel, as well as "any new or additional taxes, fees, or charges, which Seller may be required by any municipal, state, or federal law in the United States … to pay by reason of the production, manufacture, sale, or delivery" of the aviation fuel. The court held that the "Taxes" clause was a price-adjustment mechanism rather than an indemnification clause, and therefore, did not extend to clean-up costs. The court rejected the plaintiffs' argument that the contract provisions were similar to those that provided indemnification in *Ford Motor Co. v. United States* and *E.I DuPont de Nemours & Co. v. United States*. Further, the court held that, in any event, the plaintiffs had stipulated that the contracts were terminated in the 1940s, and the plaintiffs had no evidence, such as a termination agreement, to show that their present indemnification claims survived the termination.

The plaintiffs have appealed this most recent decision to the Federal Circuit. Notably, this Court of Federal Claims' decision signified a reversal from the trial court's 2010 ruling, which had found that the government was contractually liable for the clean-up costs. The 2010 ruling, however, was vacated by the Federal Circuit when it determined that the presiding trial judge should have recused himself. A decision from the Federal Circuit now, on the merits, may impact similarly situated plaintiffs with unclear rights under long-closed government contracts or lack of evidence relating to the preservation of claims.

MEDICAL DEVICE COMPANIES MAY SEEK AN INCREASE IN FSS CONTRACT PRICES TO ACCOMMODATE DEVICE TAX

Section 4191 of the Internal Revenue Code imposes a 2.3% excise tax on the sale of certain medical devices by the manufacturer/importer of the device. In December 2012, the IRS issued final

regulations and interim guidance regarding the determination of sale price and other issues related to the tax. The tax applies to sales of taxable medical devices made after December 31, 2012.

For Federal Supply Schedule (FSS) contracts with the federal government, contractors may be able to use the economic price adjustment clause of their FSS contract to seek a price increase that reflects the new tax. The Department of Veterans Affairs, which administers the FSS program for medical devices, recently described this process in its January 2013 newsletter.

According to the newsletter, contractors may be eligible to receive a price increase if their request meets the requirements of FAR 552.216-70, including:

- The excise tax is reflected as a change to the commercial price list upon which contract award is predicated;
- The proposed FSS percentage increase is equal to or less than the increase to the commercial list price change;
- Proposed pricing is no higher than permitted by the awarded tracking ratio;
- At least 30 days have elapsed between price increases; and
- The increase is requested at least 60 days prior to the end of the contract (including option periods).

When submitting a request for a price increase, contractors must provide (1) a copy of the commercial catalog/pricelist showing the price increase and the effective date for commercial customers; (2) a commercial sales practice format regarding the contractor's commercial pricing practice relating to the reissued or modified catalog/price-list, or a certification that no change has occurred in the data; and (3) documentation supporting the reasonableness of the price increase.

If you have any questions concerning the material discussed in this client alert, please contact the following members of our government contracts group:

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