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E-ALERT | Government Contracts

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THE GOVERNMENT CONTRACTS UPDATE

DOL ISSUES PROPOSED RULE ON MINIMUM WAGE FOR CONTRACTORS (79 FED. REG. 34568)

On June 17, the U.S. Department of Labor ("DOL") issued a notice of proposed rulemaking ("Notice") to implement Executive Order 13658 ("the EO"), which, as previously discussed in February, establishes the Federal-contractor minimum wage at $10.10/hour for hourly workers and $4.90/hour for tipped workers. The Notice sets forth (1) the scope of the EO; (2) formulas for wages for tipped workers and annual minimum wage increases; (3) recordkeeping requirements; (4) procedures for complaints and disputes; and (5) penalties for noncompliance. The proposed rule would apply to contracts awarded under solicitations issued on or after January 1, 2015, or to contracts awarded outside the solicitation process on or after January 1, 2015. The Notice also proposes a mandatory FAR clause to be included in covered contracts, which would be flowed down to subcontractors. As discussed below, contractors should determine whether their future contracts could include the relevant clause, and thus begin planning measures for compliance.

Scope. According to the Notice, workers "performing on or in connection with a covered contract" must be paid at least the specified minimum wage. Covered contracts include those (1) for construction covered by the Davis-Bacon Act ("DBA"); (2) for services covered by the Service Contract Act ("SCA"); (3) for concessions, including any concessions excluded from coverage under the SCA at 29 C.F.R. § 4.133(b); or (4) entered into with the Federal Government in connection with Federal property or lands related to offering services for Federal employees, their dependents, or the general public. The Notice further clarifies that a contract "in connection with Federal property" and "related to offering services" includes any contract under which the Federal Government grants a right to use Federal property, such as a lease in a Federal building with a private restaurant, credit union, or fitness center. Supply contracts are not covered. And even if a contract meets one of the conditions in (1) through (4) above, the following additional limitations would apply: (a) the clause would not be mandatory for contracts with independent agencies (as defined at 44 U.S.C. § 3502(5)); (b) the clause would only apply to contracts requiring performance in whole or in part within the United States; and (c) the clause would only apply to workers whose wages are otherwise governed by the Fair Labor Standards Act ("FLSA"), the DBA, or the SCA. The Notice broadly defines "contract" as any "agreement between two or more parties creating obligations that are enforceable or otherwise recognizable at law."

Determining wages for tipped workers and annual increases. Although the Notice sets the tipped minimum wage at $4.90/hour for 2015 (currently it is only $2.13/hour under the FLSA), if a tipped employee does not make the equivalent of the hourly minimum wage (i.e., $10.10/hour) in a given workweek, the contractor must increase the cash wage paid to the employee so the amount of the tipped wage and any tips received is equal to what he or she would have received at the hourly minimum wage ($10.10/hour for 2015). Starting in 2016, the Secretary of Labor would (1) increase the hourly minimum wage based on increases in the Consumer Price Index; and (2) increase the

tipped minimum wage by $0.95/hour until it reaches 70% of the hourly minimum wage. Fringe benefits would not be able to be used to satisfy minimum wage obligations.

Recordkeeping Requirements. Contractors and subcontractors subject to the Notice would have to make and maintain records containing: (1) the name, address, and social security number of each relevant worker; (2) the rates of paid wages; (3) the number of hours worked on a daily and weekly basis; and (4) any deductions to wages. The records would be subject to inspection by DOL for up to three years after the completion of a covered contract.

Procedures for complaints and disputes. The Notice states that there is no private right of action to enforce the proposed rule, though the Notice cautions that it is not is intended to preclude a relator from filing suit in connection with the proposed rule under the False Claims Act, 31 U.S.C. § 3730, or the Federal Government from pursuing criminal prosecution under the fraud statute, 18 U.S.C. § 1001. Moreover, anyone would be able to file a complaint with DOL if a violation of the proposed rule has occurred. Workers filing such complaints are protected by anti-retaliation provisions outlined in the Notice. If a dispute arises, contractors may seek a hearing before a DOL Administrative Law Judge. The Judge's findings could be appealed to an Administrative Review Board.

Penalties for noncompliance. A contracting agency would be able to withhold payment for services by the amount of unpaid wages, terminate the contract, and/or suspend a noncompliant contractor. In addition, if the Secretary of Labor found that a contractor has "disregarded its obligations" under the EO, the contractor would be ineligible for any contract or subcontract subject to the EO for up to three years.

According to DOL, the current average hourly wage for affected workers is $8.79/hour. The proposed rule will increase wages for workers by a total of approximately $100 million in 2015. Separately, DOL estimated that the costs of implementing the rule will be approximately $25 million (based on an assumption that it will take "one hour" for each contractor to implement the rule). Comments on the rule are due by July 17, 2014.

HHS ATTEMPTS TO CONTINUE 340B PRICING FOR ORPHAN DRUGS USED OUTSIDE ORPHAN DESIGNATIONS

As we previously reported, on May 23, the U.S. District Court for the District of Columbia vacated a U.S. Department of Health and Human Services ("HHS") regulation that attempted to clarify Section 340B of the Public Health Service Act. Under 340B, the majority of covered hospitals may not obtain the 340B discounts for "orphan drugs" (drugs that are designated for the treatment of rare diseases or conditions). HHS had taken the position that this exclusion would only apply if the orphan drugs were used to treat the disease or condition specified in their orphan designations. (E.g., under the HHS rule, a hospital could obtain 340B discounts for a drug that received an orphan designation for treating a rare cancer if the hospital used the drug to treat indigestion.) The Court, however, held that HHS lacked authority to clarify Section 340B of the Public Health Service Act. Nonetheless, the Court left open the possibility that HHS could issue guidance regarding the scope of the orphan drug exclusion.

After the ruling, HHS issued a statement indicating it "continues to stand by the interpretation described in its published final rule. . . ." In press statements, HHS officials confirmed that orphan drug manufacturers refusing to comply with HHS' policy (i.e., charging orphan-drug prices for non-orphan indications) may have to provide refunds to covered hospitals and clinics, or may face termination of their pharmaceutical pricing agreements required for Medicaid coverage. The plaintiff

in the district court case has asked that the Court either issue a ruling that HHS' interpretive policy cannot survive the Court's ruling, or order further briefing on the issue.

HOUSE PASSES $570 BILLION DEFENSE SPENDING BILL (H.R. 4870)

On June 20, the House of Representatives passed the FY2015 Department of Defense Appropriations Act (H.R. 4870), which provides $491 billion in discretionary funding and $79.4 billion for overseas contingency operations. The Senate is currently developing its own defense appropriations bill, which will be reconciled with H.R. 4870. Notable amendments to the House bill include the following prohibitions:

- Contracts could not be awarded to any person who has been found to violate the FLSA in the past five years pursuant to 41 U.S.C. § 2313(c)(1), which relates to a finding of violations in certain criminal, civil, or administrative proceedings;
- Funds previously provided for the Afghanistan Infrastructure Fund (which was criticized by the Special Inspector General for Afghanistan Reconstruction) could not be spent;
- The A-10 and KC-10 aircraft fleets could not be retired and certain military bases could not be closed;
- Directive 293 issued by OFCCP could not be implemented. Directive 293, which has already been rescinded by OFCCP, stated that contracts under TRICARE, Medicare, and the Federal Employees Health Benefits Program would trigger OFCCP jurisdiction;
- Funding could not be used for several energy-efficiency programs, biofuels, and the Administration's climate-change agenda; and
- Contracts could not be awarded to corporations headquartered or chartered in Bermuda, the Cayman Islands, or Ireland that were previously incorporated in the United States.

DHA ANNOUNCES NEW ID/IQ TO REPLACE PRIOR HEALTH IT PROCUREMENT VEHICLE

Shifting its acquisition strategy, the Defense Health Agency has announced that it will replace an existing multiple-award indefinite-quantity/indefinite-delivery ("ID/IQ") contract vehicle in effect since 2003 for information technology ("IT") acquisitions. The vehicle, called Department of Defense Systems Integration, Design, Development, Operations, and Maintenance Services 3 ("D/SIDDOMS 3"), provided the Military Health System ("MHS"), its components, and the Department of Veterans Affairs the ability to order services, equipment, materials, and facilities to design, test, and operate IT systems and system components.

Reports had indicated that DHA's purchasing strategy would shift work away from the D/SIDDOMS vehicle, and to multiple-award contracts, such as the Chief Information Officer-Solutions and Partners 3 ("CIO-SP3") contract vehicle (which has 54 qualified vendors), or to CIO-SP3's small business complement (which has 94 vendors). However, based on DHA's shift, more than $600 million in task orders expiring after July 1, 2014, may be competed under the new vehicle. Vendors interested in bidding under the new vehicle can attend an industry day on July 10 at the Ronald Reagan Building in Washington, D.C. DHA plans to release a draft RFP prior to July 10, 2014.

DOL RESPONDS TO QUESTIONS ON VEVRAA AND SECTION 503 REGULATIONS

On June 18, the Office of Federal Contract Compliance Programs ("OFCCP") within DOL posted a new set of Frequently Asked Questions ("FAQs") responding to questions received from contractors on regulations implementing the Vietnam Era Veterans' Readjustment Assistance Act ("VEVRAA") and

Section 503 of the Rehabilitation Act ("Section 503"). Section 503 prohibits Federal contractors and subcontractors from discriminating against individuals with disabilities, and it requires these employers to affirmatively act to recruit, hire, promote, and retain these individuals. VEVRAA requires covered Federal Government contractors and subcontractors to affirmatively act to employ and advance in employment-specified categories the veterans protected by the Act, and it prohibits discrimination against such veterans. Amended DOL regulations implementing these statutes went into effect on March 24, 2014.

The new FAQs relating to Section 503 clarify that Section 503 regulations do not require contractors to hire "a less qualified candidate instead of the best qualified candidate for the purposes of affirmative action." The new FAQs also address questions about how to count employees' step or ladder movements, appropriate methods for self-identification, and how non-responses to self-identification questions should be treated. The new FAQs relating to VEEVRA address how to count an employees' step or ladder movements, how to count partial self-identifications, and the applicable definition of the word "hire" for the purposes of data collection analyses.

FAA APPROVES FIRST COMMERCIAL DRONE OPERATION OVER LAND IN THE UNITED STATES

On June 10, the Federal Aviation Administration ("FAA") announced that it had authorized the first commercial drone operation over land in the United States. The approval permits an energy company to survey pipelines, roads, and equipment at the oilfield at Prudhoe Bay, Alaska. The FAA had previously authorized operations over Arctic waters in that area, and the approval this week was heralded by U.S. Department of Transportation Secretary Anthony Foxx as "another important step toward broader commercial use of unmanned aircraft." More information can be found on our Global Policy Watch blog post here.

CASE DIGEST

Ninth Circuit Allows Construction Second-Tier Subcontractor To Seek Long-Overdue Payments from Prime (*Ramona Equip. Rental, Inc. v. Carolina Casualty Ins.*, No. 12-55156 (9th Cir. June 20, 2014))

On June 20, the U.S. Court of Appeals for the Ninth Circuit held that a second-tier subcontractor was entitled under the Miller Act, 40 U.S.C. §§ 3131-3134, to all unpaid invoices on a construction contract, even though the subcontractor waited more than six months to make a claim for some of the invoices. The Miller Act requires prime contractors on Federal construction projects to post a bond. A contractor (such as a second-tier subcontractor) having no contractual relationship with the prime contractor may bring suit seeking payment on the bond upon giving written notice to the prime within 90 days of the "date on which . . . the last of the [performance] for which the claim is made."

In this case, the second-tier subcontractor entered into 89 equipment rental agreements over the span of six months under an open book account with the first-tier subcontractor. It received payments on only 11 agreements from the first-tier subcontractor before the prime's contract with the first-tier subcontractor was terminated. The second-tier subcontractor then issued a notice to the prime contractor, seeking payments for all remaining equipment rentals (even those past due by over 90 days), arguing that the Miller Act notice requirement is satisfied for all unpaid invoices if a single unpaid invoice falls within the 90-day window. The Ninth Circuit agreed (over a dissent), rejecting arguments that the Miller Act requires a 90-day notice after each unpaid invoice, and that the purpose of the notice provision is to protect the prime contractor from unforeseen obligations. The Ninth Circuit also rejected arguments that the second-tier subcontractor should have mitigated its damages by notifying the prime contractor sooner, and that the prime contractor faced "double

liability" for the unpaid invoices. The Ninth Circuit reasoned that the prime contractor still owed funds to the first-tier contractor; moreover, the notice provision notwithstanding, the overall purpose of the Miller Act is to provide recovery for suppliers who have provided materials, but have not received compensation.

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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