**E-Alert | Government Contracts**

May 29, 2013

**The Government Contracts Update**

Covington & Burling LLP’s Government Contracts practice regularly delivers an update on major news, notes, and trends relevant to government contractors.

**CASE DIGEST**


On April 3, 2013, in an action brought by Cyberlock Consulting Inc. (“Cyberlock”) alleging the breach of a teaming agreement by Information Experts, Inc. (“IE”), the U.S. District Court for the Eastern District of Virginia held that the agreement at issue—which called for the parties to negotiate a subcontract after the award to IE of a federal government contract—was an unenforceable “agreement to agree.” The teaming agreement in question specified that the parties would split 51/49 percent work on an Office of Personnel Management contract upon which IE was bidding, and included an exhibit setting forth the anticipated Scope of Work and other information pertinent to Cyberlock’s performance. While Cyberlock argued that the parties’ conduct, communications, and negotiations showed that the parties intended the teaming agreement to be a binding contract requiring IE to provide Cyberlock with 49% of the awarded prime contract, the Court concluded that the teaming agreement was merely an agreement to negotiate in good faith to enter into a future subcontract. The Court noted that the teaming agreement: 1) did not set out any further details about the work anticipated to be performed by Cyberlock; 2) did not include as an exhibit the subcontract the parties intended to execute if IE was awarded the prime contract, as the parties had done in prior teaming agreements; and 3) contained prospective language and included other provisions which made it clear that the parties intended to negotiate a subcontract in the future. Such an agreement, the Court held, “is precisely the type of agreement to agree that has consistently and uniformly been held unenforceable in Virginia.”

This case sends a clear message to contractors that the terms of a teaming agreement (and any related subcontract) should be as definitive as possible prior to the award of a prime contract, and raises questions about the validity of teaming agreements that contain only standard, tentative provisions.

**Statutory Time Limits for FOIA Responses Must Be Honored** (*Coleman v. Drug Enforcement Administration*, No. 11-1999 (4th Cir. May 2, 2012))

On May 2, the U.S. Court of Appeals for the Fourth Circuit held that the United States Drug Enforcement Agency (“DEA”) violated the statutory deadline for responding to a FOIA request and remanded the case to the district court for further proceedings. In February 2008, Plaintiff John Coleman filed a FOIA request (and offered to pay $1,000 for its processing) with the DEA to obtain documents related to the scheduling of a drug under the Controlled Substances Act. Under FOIA, the DEA had 20 working days to respond to the request or provide notice that it was invoking an
extension for “unusual circumstances.” The DEA did neither, and instead took more than sixteen months to respond to Mr. Coleman’s request, eventually denying it on the grounds that the $1,000 Mr. Coleman offered to pay did not cover the estimated processing fees of $1,780.75. Mr. Coleman appealed the fee assessment to the Department of Justice’s Office of Information Policy (“OIP”), arguing that he was entitled to a fee waiver as a non-commercial requester and because the request was in the public interest. The OIP took over seven months to respond to Coleman’s appeal, eventually remanding the request back to the DEA for further consideration. After four months with no response from the DEA, Mr. Coleman filed suit in the Eastern District of Virginia.

The district court granted the DEA’s motion for summary judgment, holding that Mr. Coleman had failed to pay its fee request for the preliminary search of documents and to exhaust his administrative remedies, including appealing the denial of the fee waiver to OIP. The Fourth Circuit reversed, finding that Mr. Coleman had constructively exhausted his administrative remedies because the DEA had exceeded the statutory time limit for a response to Coleman’s claim on remand, and that nothing in FOIA requires a requester to “prepay an assessed fee before proceeding to challenge that fee.” The Court observed that “[a]lthough FOIA does not explicitly contemplate remands following administrative appeals, it is inconceivable that Congress intended to allow agencies to escape FOIA’s time limits by sitting on remanded requests indefinitely.”

Further, in response to the DEA’s argument that Mr. Coleman had not exhausted his administrative remedies with respect to the fee waiver request, the Court found that requesters are not required to make distinct arguments addressing every individual component of an adverse fee determination before obtaining judicial review of that determination. The Court noted that “[h]olding an ordinary citizen . . . to such an exacting standard would impose a burden not authorized by FOIA and would frustrate the statute’s purpose of ‘assur[ing] the availability of Government information necessary to an informed electorate.’” The OPEN Government Act of 2007—which provides federal agencies with other means of extending the 20 day response period—was not in effect at the time of Coleman’s FOIA request.


On May 6, the Court of Federal Claims enjoined USAID from issuing a contract award until it accepted and evaluated on equal terms quotations from two offerors who had originally submitted their quotations by email before the 5pm deadline on the due date, but whose quotations were not released by USAID’s server until after the deadline. As a result, USAID had rejected those quotations as untimely. When challenged, the government argued that “late is late,” and that if a solicitation required proposals to be submitted to specific email account, a proposal had to be in that addressee’s inbox in order for it to be considered timely. In response, the rejected offerors argued that their quotes should have been accepted under “Government Control” exception of FAR 52.212-1(f)(2)(i), which directs that the “late is late” rule does not apply when a proposal “was received at the Government installation designated for receipt of offers and was under the Government’s control prior to the time set for receipt of offers.” The Court agreed. Noting that these cases “somewhat painfully illustrate the thorny issues that can arise when the outmoded provisions of the [FAR] governing the delivery of electronic proposals - which date back to the last century - are applied to modern computer technology,” it held that the Government Control exception applies not only to paper filings, but also to an electronic proposal that has been received by a government server (or comparable computer) and is under the agency’s control prior to the deadline. Accordingly, the Court ruled that USAID’s refusal to accept the offerors’ proposals was arbitrary, capricious, an abuse of discretion, and contrary to law.
Supreme Court Decision Broadens Deference to Federal Agencies (City of Arlington et al. v. Federal Communications Commission et al., No. 11-1545 (S. Ct. May 20, 2013))

In what may be a landmark decision on the scope of Chevron deference to agency decisions, on May 20, 2013, the Supreme Court held that courts must apply Chevron deference to the review of an agency’s interpretation of a statutory ambiguity concerning the scope of that agency’s statutory authority (i.e., its jurisdiction). In City of Arlington, the cities of Arlington and San Antonio, Texas, sought review of a Federal Communications Commission (“FCC”) Declaratory Ruling on a provision of the Communications Act of 1934 (47 U.S.C. §332(c)(7)(B)(ii)) requiring state or local governments to act on siting applications for wireless facilities “within a reasonable period of time after the request is duly filed.” While the FCC has rulemaking and adjudication authority to administer the Act, the petitioners argued that the FCC did not have the authority to interpret ambiguous provisions of Section 332(c)(7), because the provision both contained a saving clause and provided for judicial review of a state or local authority’s wireless-siting decision. The petitioners argued that together, these “display[ed] a congressional intent to withhold from the Commission authority to interpret the limitations in §332(c)(7)(B).”

The Court rejected this argument, stating that an agency’s “power to act” and “how they are to act” is authoritatively prescribed by Congress, and as a result, the question for a court reviewing an agency decision is whether the agency has gone beyond what Congress has permitted it to do. The Court further explained that because there is no distinction between “jurisdictional” and “nonjurisdictional” interpretations, “there is no principled basis for carving out a subset of ‘jurisdictional’ questions from the Chevron framework.” The Court concluded that Chevron deference was appropriate because Congress had “unambiguously vested the FCC with general authority to administer the Communications Act through rulemaking and adjudication, and the agency interpretation at issue was promulgated in the exercise of that authority.”

While its actual impact remains to be seen, we can reasonably assume that this ruling will make it more difficult for regulated entities to challenge agency actions that are within the agency’s Congressionally-outlined scope of authority.

FROM THE HILL

Senators Introduce “Deter Cyber Theft Act”

On May 19, a bipartisan group of Senators introduced a bill aimed at combating economic and industrial espionage in the United States. The “Deter Cyber Theft Act”—co-sponsored by Senators Levin, McCain, Coburn, and Rockefeller—would require the Office of the Director of National Intelligence (“DNI”) to develop a watch list and priority watch list of foreign countries engaged in economic or industrial cyber-espionage with respect to U.S. trade secrets or proprietary information, and to submit an annual report to Congress identifying those countries. DNI would also be required to identify in that annual report: (i) technologies or proprietary information that are targets of economic or industrial espionage and, to the extent possible, have been appropriated through such espionage; (ii) articles manufactured or otherwise produced using such technologies or proprietary information; (iii) services provided using such technologies or proprietary information; and (iv) foreign entities, including state-owned entities, that request, engage in, support, facilitate, or benefit from the economic or industrial espionage. The bill also calls for the President to make it a priority for the intelligence community to collect and analyze information in order to identify such articles or entities, and to ban imports into the United States of articles manufactured or produced using stolen U.S. technologies or proprietary information, or that are made by an entity the DNI has identified as having benefited from theft of U.S. technology or proprietary information. According to Senator
Levin, the goal of these measures is to “call out those who are responsible for cyber theft and empower the president to hit the thieves where it hurts most—in their wallets, by blocking imports of products or from companies that benefit from this theft.”

**OTHER NOTEWORTHY ITEMS**

**DoD Issues Proposed Counterfeit Electronics Regulation (78 Fed Reg. 28780) (May 16, 2013).**

On May 16, the Department of Defense (“DoD”) issued a proposed rule to implement new regulations on detecting and avoiding the use of counterfeit electronics in DoD procurements. Originally due in the Fall of 2012, the proposed rule would implement parts of section 818 of the National Defense Authorization Act (“NDAA”) for Fiscal Year 2012 (Pub. L. 112-81, enacted Dec. 31, 2011), which required DoD to adopt regulations that would impose counterfeit prevention requirements on defense contractors, as well as the amendments to section 818 made in section 833 of the 2013 NDAA (Pub. L. 112-239, enacted Jan. 2, 2013). The proposed rule would require contractors to establish and maintain an acceptable counterfeit electronic part avoidance and detection system as part of the contractor’s purchasing system. Such a system would, at minimum, address nine specific criteria: 1) personnel training; 2) inspection and testing of electronic parts; 3) processes to abolish counterfeit parts proliferation; 4) mechanisms to enable traceability of parts to suppliers; 5) use and qualification of trusted suppliers; 6) reporting and quarantining of counterfeit or suspect counterfeit parts; 7) methodologies to identify suspect counterfeit parts; 8) the design, operation, and maintenance of systems to detect and avoid counterfeit and suspect counterfeit parts; and 9) the flow down of these requirements to subcontractors. The failure to establish and maintain such a system could result in disapproval of the purchasing system by the contracting officer and/or withholding of payments.

As explained in the Federal Register notice, the purpose of these requirements is to shift the burden of detecting and avoiding the use of counterfeit electronic parts in DoD procurements to contractors. In line with this objective, a new DFARS subsection would prohibit contractors from claiming as reimbursable costs the cost of counterfeit electronic parts or suspect counterfeit parts, or the cost of rework or corrective action. While the proposed rule contains a safe harbor provision allowing for costs to be reimbursed under certain circumstances, the scope of that provision is unclear as a result of an internal inconsistency in the proposed rule. The preamble to the rule states that costs are reimbursable if the contractor had an operational, DoD-approved system to detect and avoid counterfeit parts, or the parts were provided as Government-furnished property, and the contractor provided timely notice to the government. However, the text of the proposed rule limits the safe harbor provision to instances in which the contractor has a DoD-approved counterfeit detection system and the parts were provided as government-furnished property. This conflict should be addressed in comments.

The proposed rule would apply only to contracts subject to the Cost Accounting Standards (CAS), and will therefore not apply to small entities as prime contractors. However, contractors are required to flow down the anti-counterfeiting responsibilities to their subcontractors and suppliers, which may be small entities. Comments on the proposed rule are due July 15, 2013.


The Special Inspector General for Afghanistan Reconstruction (“SIGAR”) reported on May 14th that the Government of Afghanistan has levied nearly a billion dollars in business taxes on contractors...
supporting U.S. government efforts in Afghanistan, despite the fact that the contractors should have been exempt from at least some of those taxes under bilateral agreements negotiated between U.S. agencies (e.g., the DOD, State Department, and USAID) and the Afghan government. The report found that the U.S. government had itself exacerbated the problem because it “created a tax environment for contractors that differs from agency to agency and allows the Afghan government to take advantage of differences in the application of the various agreements.” The report also noted that the U.S. and Afghan governments disagree on the tax treatment of subcontractors. Afghan Ministry of Finance (“MOF”) officials contend that the agency agreements provide tax exempt status only to prime contractors, while U.S. government officials believe that the agreements provide tax exemption for all non-Afghan companies, both prime and subcontractors, supporting U.S. government efforts.

As of the date of the report, the 43 contractors in SIGAR’s sample had paid only $67 million of the $921 million in total tax assessments. As a result, the MOF has restricted certain contractors’ freedom of movement, has refused to renew business licenses, and has even arrested some contractor personnel. This issue is expected to be addressed in the upcoming negotiation of a new bilateral security agreement between the U.S. and Afghan governments. However, that agreement is not expected to take effect until sometime in 2014.

Foreign taxation in Afghanistan and other parts of the world is an issue affecting many contractors, and one that we continue to monitor.


On May 7, the Small Business Administration (“SBA”) issued an interim final rule implementing Section 1697 of the 2013 NDAA (see our February 11, 2013 Government Contracts Update), which removed the statutory dollar limit on contracts that could be set-aside for Women-Owned Small Businesses (“WOSB”) or Economically Disadvantaged Women-Owned Small Business (EDWOSBs) under the Women-Owned Small Business (“WOSB”) Program. Previously, Federal contracting officers could only set aside a contract for WOSBs or EDWOSBs if the anticipated award price of the contract did not exceed $6.5 million in the case of manufacturing contracts and $4 million in the case of all other contracts. Contracting officers may now set aside contracts under the WOSB Program at any dollar level, as long as the other set-aside requirements are met (e.g., that in the estimation of the contracting officer, the contract can be awarded at a fair and reasonable price). In addition to benefitting WOSB and EDWOSB contractors, the program is expected to assist agencies in achieving the statutorily-mandated 5% government-wide goal for procurement from WOSBs. The rule was effective as of May 7, 2013 and applies to all solicitations issued on or after the effective date. Comments are due by June 6, 2013.

Study Finds that Federal Taxpayers Employ More Low-wage Workers Than Wal-Mart and McDonalds Combined

A May 8 report from public policy organization Demos estimates that that taxpayer dollars fund nearly 2 million private-sector jobs that pay $12 an hour or less, more than McDonald’s and Wal-Mart combined. This figure encompasses U.S workers employed by government contractors, paid by federal healthcare spending, supported by Small Business Administration loans, working on federal construction grants, and maintaining buildings leased by the federal government. In contrast, Demos estimates that about 1.4 million workers earn that amount or less at Wal-Mart and McDonald’s, which are two of the largest employers of low-wage workers. Speaking about the report, co-author Amy Traub stated “[w]e found that prevailing wage laws, including the Davis-Bacon Act, the
Walsh-Healey Act, and the Service Contract Act, are not enough to ensure decent standards for all private sector workers supported by our public dollars.” Noting the disparity between the compensation levels of government contractor senior executives and their low-wage employees, the report calls for President Obama to issue an Executive Order requiring agencies to take all possible steps to raise workplace standards and ensure that companies comply with applicable labor and employment laws.

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

- Alan Pemberton +1.202.662.5642 apemberton@cov.com
- Robert Nichols +1.202.662.5328 rnickols@cov.com
- Susan Cassidy +1.202.662.5348 scassidy@cov.com
- Jennifer Plitsch +1.202.662.5611 jplitsch@cov.com
- Steven Shaw +1.202.662.5343 sshaw@cov.com
- Scott Freling +1.202.662.5244 sfreling@cov.com
- Anuj Vohra +1.202.662.5362 avohra@cov.com
- Jade Totman +1.202.662.5556 jtotman@cov.com
- Sarah Liebschutz +1.202.662.5673 sliebschutz@cov.com

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