



## 29TH ANNUAL OUNCE OF PREVENTION SEMINAR

Weathering the  
Rough Seas of  
Regulation



# The Unprecedented Year and the Consequences of Austerity

# Overview

- Congressional Budgeting by Sequester, Continuing Resolutions, and Debt-Ceiling Debates
- Executive Branch Issues and Implementation
- Impacts on Acquisition Policy, Business and the Marketplace
- Effects on Contract Administration and Disputes
- Labor/Employment Challenges
- Strategic Considerations for Appropriations

# Budgeting by Sequester, Continuing Resolutions, and Debt-Ceiling Debates

Mike Gill

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# Topics

- Budget Control Act of 2011 and American Taxpayer Relief Act of 2012
- 2013 Budget and Sequestration
- 2014 Budget and Sequestration
- Will This Get Fixed? How?

# BCA and ATRA

- Budget Control Act of 2011
  - Required savings of \$1.2T (\$984B) over nine years
  - \$55B Defense (050) \$55B non-defense each year
- American Taxpayer Relief Act of 2012
  - Reduced 2013 sequester to \$85B
  - \$42B Defense (050) \$42B non-defense for 2013

# 2013 Budget and Sequestration

- ATRA reduced sequestration amount to \$85B
- Most pro-rated to 2014 – 2021 (further reduction in caps)
- Sequestration versus Downward Adjusted Caps
  - Sequestration affects 2013 non-exempt mandatory and discretionary spending
  - Sequestration affects 2013- 2021 non-exempt mandatory spending
  - Adjusted downward caps affect 2014 non-exempt discretionary spending

# 2014 Budget and Sequestration

- On April 10, 2013, OMB released the FY 2014 sequestration preview report that established the revised discretionary spending limits for 2014 and is the order for mandatory sequestration beginning October 1, 2013.
- 50% Defense (050), 50% Non-Defense
- Mandatory Spending
  - Sequestration of non-exempt mandatory spending will take place upon OMB confirmation
- Discretionary Spending
  - Congress must appropriate within caps
  - Congress can be very flexible in appropriations while under cuts
  - Sequestration if Congress does not appropriate within caps (across “PPA”)
  - Dilemma of unpopular programs / better to have sequestration?



# Debt Limit Crisis Timeline

Dec. 31, 2012

Debt Limit Reached

U.S. hits \$16.4T debt limit; U.S. Treasury Secretary takes “extraordinary measures” to avoid default.

Jan. 1, 2013

Congress Passes American Taxpayer Relief Act

Sequester delayed by two months (March 1, 2013); Congress postpones debt reduction deal and negotiations to raise the debt ceiling

January 31, 2013

Congress Passes Bill to Suspend Debt Ceiling

Congress passes legislation to suspend the debt ceiling until May 18, 2013

April 10, 2013

OMB Releases 2014 Preview Report

OMB report establishes mandatory sequestration order for non-exempt established the revised discretionary spending limits for 2014 and is the order for mandatory sequestration beginning October 1<sup>st</sup>

May 19, 2013

U.S. Debt Ceiling Reinstated

The debt ceiling will come back into effect on May 19, at which point the Treasury will begin to take “extraordinary measures” to keep the government running.

Autumn, 2013

U.S. Faces Threat of Default

If no action is taken to suspend or raise the debt ceiling and Congress fails to reach a debt reduction deal, the U.S. could default on its debt obligations.

October 1, 2013

Sequestration of 2014 Non-Exempt Mandatory Programs Begins

# Will This Get Fixed? How?

- Option 1: “Grand Bargain”
- Improving Economy provides impetus for renewed negotiations on structural reforms to spending and revenue.
- PAYGO Act of 2010
  - PAYGO limits new mandatory spending (4% Medicare limit)
  - BCA limits non-exempt mandatory and discretionary spending (2% Medicare limit)
- Resulting agreement leads to Congress enacting legislation nullifying the BCA.
  - But increased revenue alone does not nullify sequestration mechanics.

# Will This Get Fixed? How?

- Option 2: “Responsible Government”
- Congress appropriates within caps for FY 2014 through 2021, cutting some programs substantially while preserving or increasing others.
- President utilizes ability to transfer between accounts.
  - But non-exempt mandatory spending still subject to sequestration (see Grand Bargain Solution)
  - But separation between defense and non-defense (2013 House Budget Not a Solution)

# Will This Get Fixed? No.

- Option 3: “Punt”
  - Congress and President continue with budget gridlock.
  - BCA continues to affect all accounts, piecemeal adjustments (see FAA account shifting authority).

# Questions?

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# Executive Branch Issues Relating to Sequestration

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# Executive Branch Issues

- Implementation of Sequestration
- Recent Developments
  - FY13 Appropriations
  - Increased Use of Incremental Funding

# Implementation of Sequestration

- Sequester requires uniform cuts to each PPA
- PPA is not uniformly defined across government
- Led to speculation that cuts would apply down to the contract level
- Post-sequestration guidance indicates that this is not the case





**UNCLASSIFIED**

## **Fiscal Planning Guidance for Budgetary Uncertainty**

16 January 2013

mitigation spend plans, you must take all possible steps to mitigate harmful effects associated with this budgetary uncertainty and to maintain a strong defense.

a. A Presidential order for Sequestration on 1 March 2013 will specify reductions to total budgetary resources in each budget account (appropriation) based upon estimates provided to the Office of Management and Budget (OMB) by the Under Secretary of Defense (Comptroller) [USD (C)]. The Balanced Budget and Emergency Deficit Control Act of 1985 (BBEDCA) requires that this reduction be applied equally to each “Program, Project and Activity” (PPA) within these accounts. For the purposes of the BBEDCA, PPA is defined as the appropriation level for operating accounts and at the R-1, P-1 and C-1 budget line item level for investment accounts. The President has exempted Military Personnel accounts from targeted sequestration reductions in FY 2013. For planning, the budget reduction estimate for FY 2013 is approximately 10.5 percent. However, this estimate is likely to change depending on the date of the sequestration order and the amount of available resources given the rate of budget execution.

Source: U.S. Dep’t of the Army, *Fiscal Planning Guidance for Budgetary Uncertainty* at 14 (Jan. 16, 2013).

# Implementation (cont'd)

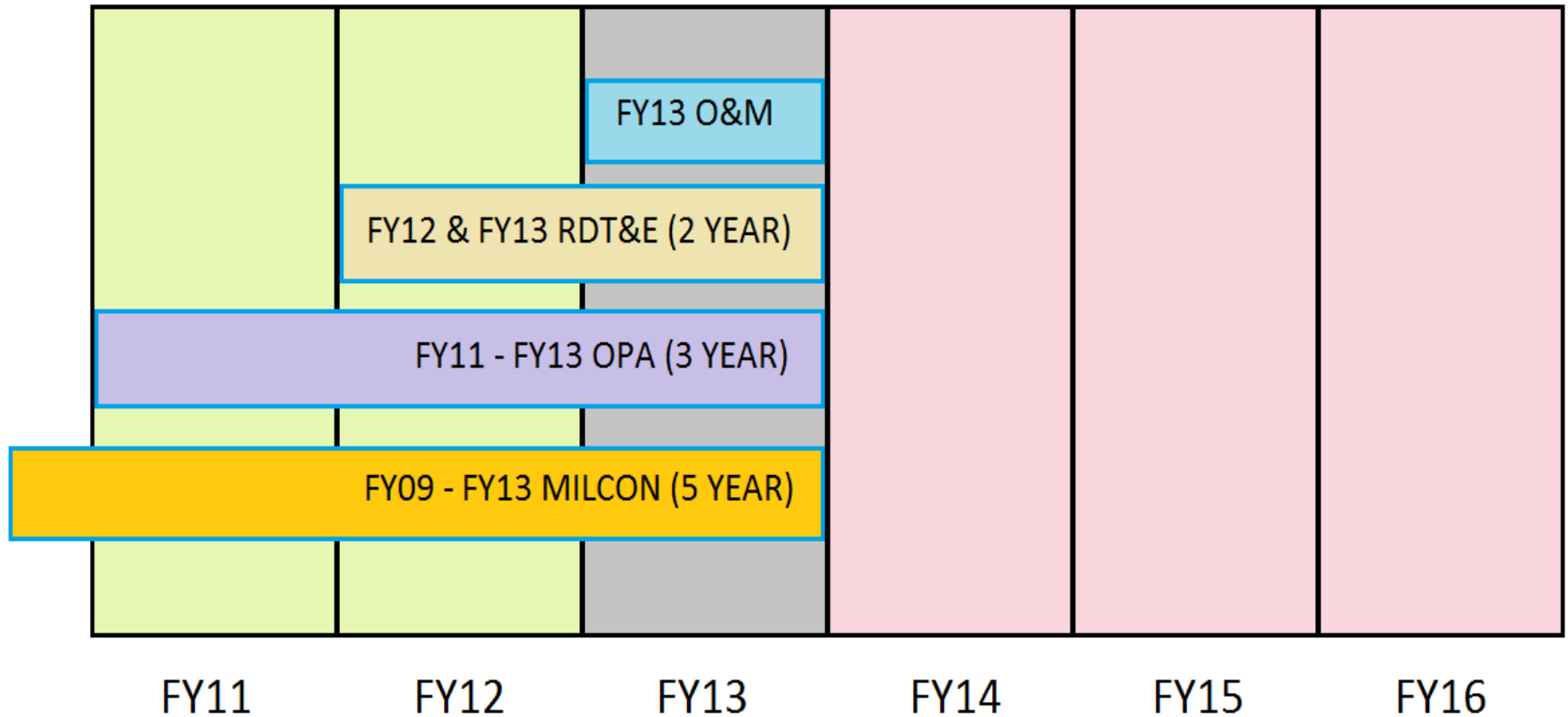
- Only 18 operating accounts in all of DoD, so sequestration for these accounts is applied at a very high level
  - E.g., O&M, Army; O&M, Air Force; O&M, Navy; etc.
- Thousands of P-1, R-1, and C-1 budget line items, but still a very high programmatic level to apply cuts (example below)

```
Line
  No      Item Nomenclature
Budget Activity 01: Proc Ammo, Navy
Navy Ammunition
  1 General Purpose Bombs
  2 Airborne Rockets, All Types
  3 Machine Gun Ammunition
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# Implementation (cont'd)

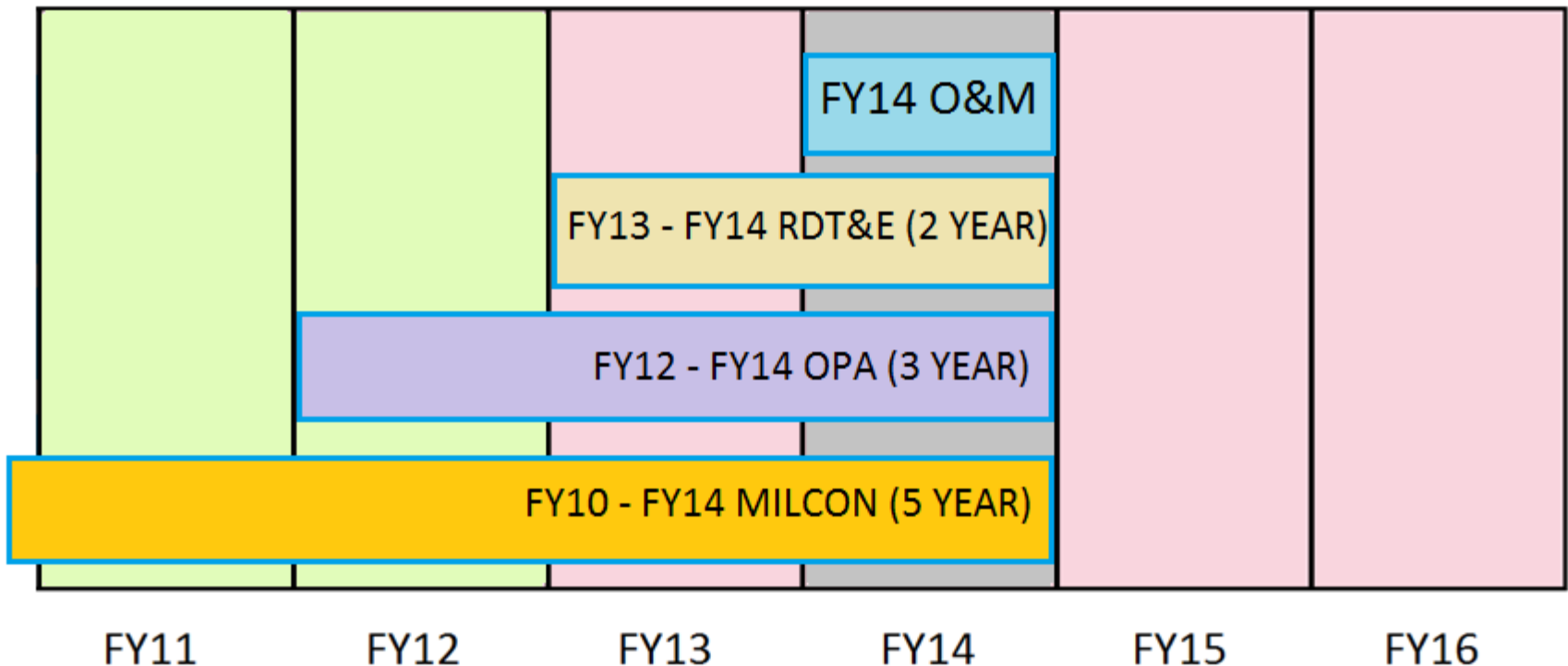
- Impacts to date have been modest
  - Sequester requires reduced spending over the course of the year, not all at once
  - Impacts lessened by FY13 Consolidated & Further Continuing Appropriations Act
  - DoD has used reprogramming authority
- Impacts will likely be felt hardest in 4Q13 and beyond
  - 4Q13: Agency FY13 appropriations begin to run dry
  - FY14 and beyond: Multi-year appropriations expire

# Example – Army Impacts in 4Q13



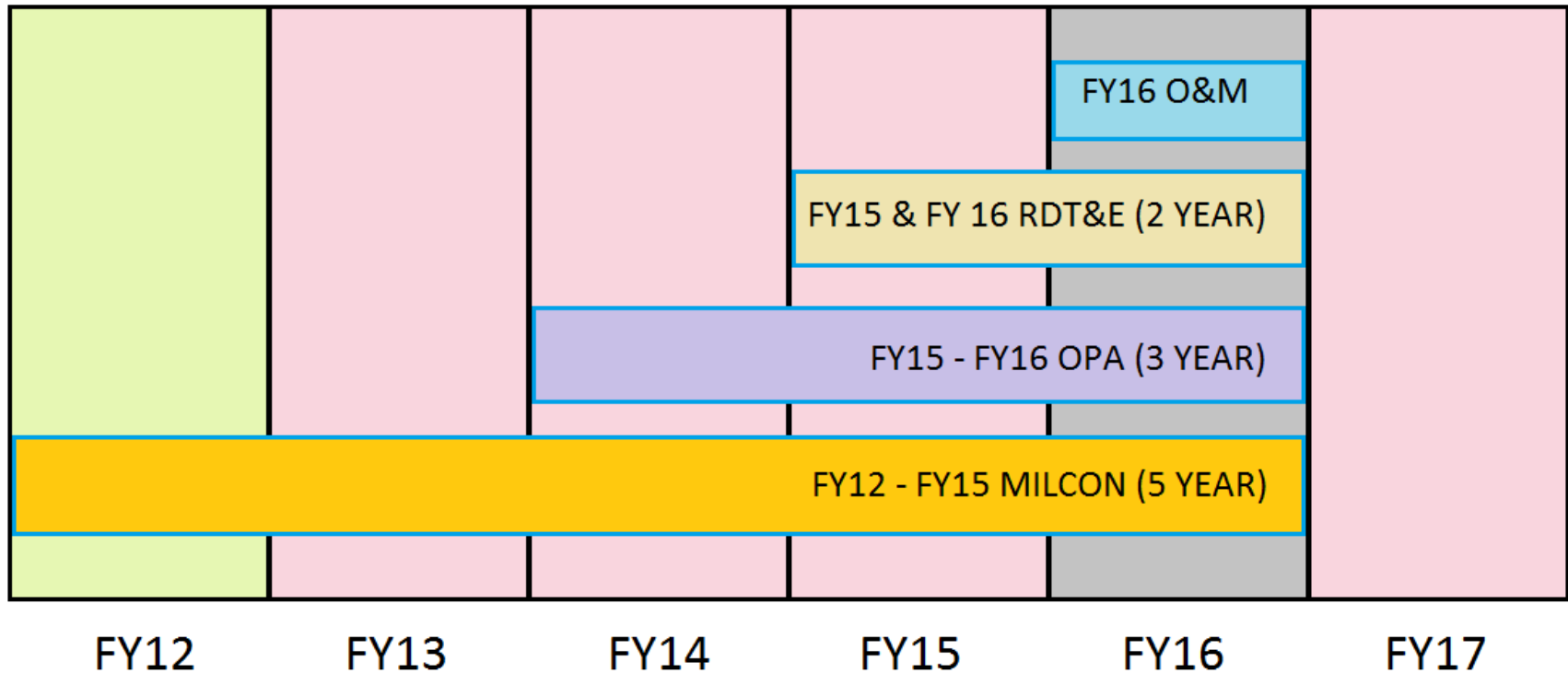
*In FY13, significant funding is still available from prior years, and this prior-year funding was not subject to sequester cuts.*

# Army Example – FY14 (cont'd)



*Each year after FY13, there will be less funding available from the pre-sequestration era, so there will be a smaller pool of prior-year un-sequestered funds to ease impacts.*

# Army Example – FY16 (cont'd)



*Each year after FY13, there will be less funding available from the pre-sequestration era, so there will not be a pool of prior-year un-sequestered funds to ease impacts.*

# Recent Developments (cont'd)

- FY13 Consolidated & Further Continuing Appropriations Act
  - Provides FY13 funding for DoD, Commerce, DOJ, DHS, MILCON, VA, and science agencies
  - Act had the effect of lifting the CR prohibition on DoD “new starts”
    - Prohibition against “new starts” appears in most CRs
    - Prohibited DoD from spending CR money for new production, increases in production, or the initiation, resumption, or continuation of any project for which funds and authority did not exist in FY12
    - Meant that DoD projects requiring specific authorization and appropriations were stalled during CR (e.g., military construction)
  - Lifting of “new starts” prohibition likely responsible in part for spike in DoD contract awards at end of March
    - \$12.1B in 1/13 → \$23.1B in 2/13 → \$39.4B in 3/13

# Recent Developments (cont'd)

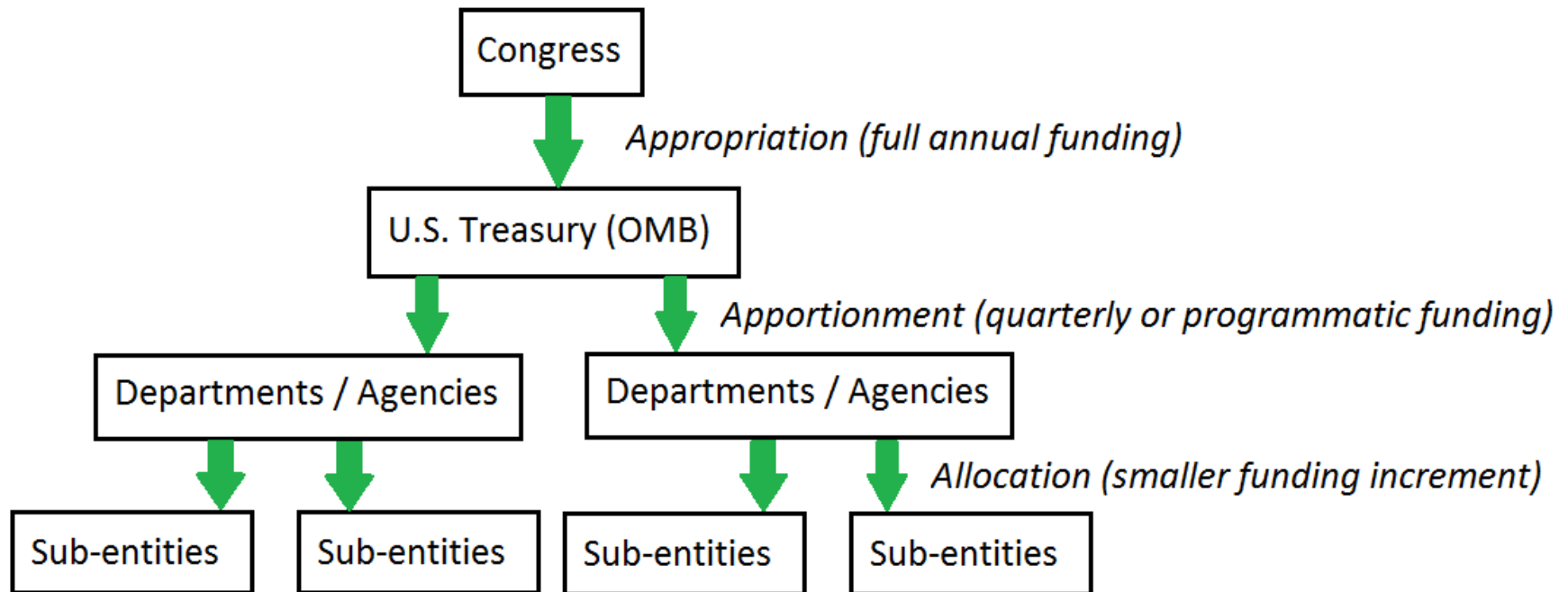
- Increased Use of Incremental Funding
  - General rule is that agency must obligate full funding at time of contract award
  - Incremental funding is exception that allows agency to obligate funding for single contract in multiple steps
  - Typically used in cost-reimbursement contracts for high-cost projects over multiple years
  - But now, DoD is using incremental funding authority (FAR 52.232-22) to make multiple obligations for single contract *within the same year*



# Recent Developments (cont'd)

- Increased Use of Incremental Funding (cont'd)
  - Likely owes to the way the money flows within government
    - Congress *appropriates* funds to U.S. Treasury annually
    - OMB then *apportions* funds from U.S. Treasury to Departments on quarterly or programmatic basis
    - Departments then *allot* funds down to subordinate agencies
    - End result is that agencies typically have only a fraction of full-year funding on hand at any time
    - Apportionments and allotments likely stingier in recent months to ensure that agency spending stays within (1) CR limits and (2) sequestration limits
  - Takeaway: Money for same-year incrementally funded contracts is there; it just may not have made it down to the agency yet

# Recent Developments (cont'd)



# Recent Developments (cont'd)

- Increased Use of Incremental Funding (cont'd)
  - Will likely result in spike in FAR 52.232-22(c) notifications (required when costs projected in next 60 days exceed 75% of amount allotted to the contract to date)
  - Frustrates government's ability to conduct long-term planning

# Questions?

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# Impacts on Acquisition Policy, Business and the Marketplace

W. Stanfield Johnson

# Impacts on Acquisition Policy

- Expect more risk allocation to contractors and intensification of current acquisition reforms to protect scarce funds. For example:
  - Fixed Price Contracting, plus special risk allocation clauses (including in cost reimbursement contracts)
  - Competition – Low Price Technically Acceptable
  - “Tailored” Commercial Item Contracts, plus required cost information

# Impacts on Acquisition Policy

- More Oversight, including Business System Reviews and withholds; “do not pay” mentality
- Reduced Service Contracting
- Strategic Sourcing, with IT as a commodity
- But don't expect rebuild of competent acquisition workforce

# Impacts on Acquisition Policy

- Key Features of FY 2013 NDAA:
- §802 – Review and justification of pass-through contracts
- §804 – Review and modification of profit policy
- §811 – Limit on use of cost type contracts for production of MDAPs (exceptions, but for portions of contracts)



# Impacts on Acquisition Policy

- Key Features of FY 2013 NDAA:
- §823 – Life-cycle management and product support requirements
- §824 – Government performance of critical acquisition functions
- §825 – Competition in acquisition of major subsystem and subassemblies – alternative of “breakout” and GFE

# Impacts on Acquisition Policy

- Key Features of FY 2013 NDAA:
- §831 – Guidance and training for evaluation of price reasonableness
- §832 – DCAA access to internal audit reports for “evaluation of contractor business systems”
- §851 – Database on price trends of items and services under Federal contracts

# Impacts on Acquisition Policy

- Key Features of DoD Better Buying Power 2.0:
- Mandate affordability; enforce affordability caps; control requirements
- “Should cost” management – “set cost targets below independent cost estimates”
- Reassess contractor profitability and incentives
- “Appropriate contract types” – refining BBP 1.0 (“one sizes does not fit all”); FPI in “early stages of transition from development to production”

# Impacts on Acquisition Policy

- Key Features of DoD Better Buying Power 2.0:
- Define value in “best value” competitions
- In LPTA, define TA to ensure needed quality
- “Superior supplier” incentive program
- Maintain competitive environments, and develop IP strategy “while competition still exists”
- Leverage Industry’s IR&D
- Increase small business opportunities

# Impacts on Acquisition Policy

- Key Features of DoD Better Buying Power 2.0:
- Improve tradecraft in services acquisitions; “greatest potential for cost reduction”; define and prevent “creep” of requirements
- Improve professionalism in “total acquisition workforce,” increase “cost consciousness”
- Reduce “backlog” of DCAA audits
- Eliminate non-value added requirements and processes
- Increase “defense exportability features” in initial designs

# Impacts on Acquisition Policy

- Government panelist at Professional Service Council's Marketview 2012. "We have decided that the vast majority of what we buy is appropriately bought on a low price, technically acceptable basis." "We are going to require that any component that seeks to use a 'best value' approach justify their reasons for doing so." "If you're thinking about margins, you're thinking about the wrong thing. The fiscal environment is such that you should only be thinking about booking revenue, not margins" (as quoted by Stan Soloway in Washington Technology, April 13, 2012).

# Business and Marketplace Impacts

- DoD Dear “Industry Partner” Letter (Mar. 4, 2013)
- “The reality of sequestration is now upon us....Given the uncertainty we face, the Department will take action in the near term to mitigate budget execution risk to the extent possible; however, damage to the Department and to industry is unfortunately inevitable at this point....Defense industry companies should anticipate that the automatic across-the-board cuts will cause the Department to reduce both the quantities of equipment and the level of service that we acquire for the balance of this Fiscal year and perhaps beyond.”

# Business and Marketplace Impacts

- One consequence of the extreme program instability associated with this funding uncertainty, is the impossibility of sound business planning. With programs uncertain and incumbency devalued in an intense competitive environment, a contractor that relies on “anticipated” work is at risk. This may require particular care by publicly held companies, but it poses problems for all contractors.



# Business and Marketplace Impacts

- The Obvious Bottom Lines:
- Downsizing of procurement budgets will mean less government business
- Programs and contracts will be deferred, interrupted, abandoned, cancelled, terminated, and reduced
- Though the Government demand will remain substantial, the existing supply exceeds the funded demand

# Business and Marketplace Impacts

- The result will be a reduced and damaged contractor base
- The result will also be a much less desirable government customer and marketplace.
- 2013 begins the difficult, disruptive transition period to the downsized marketplace.

# Business and Marketplace Impacts

- The specific impacts of this transition on the government's contractor base is complex because it is composed of many different sectors and difficult to predict because the combination of circumstances is unprecedented. However, here are some observations:

# Business and Marketplace Impacts

- Impacts on Contractor Base
- Disruption and loss of talented, trained workforce; disputes
- Supply chain disruption and loss; disputes
- Cost of disruption and potential loss of quality
- Lack of resources for R&D; freezing of innovation
- Unabsorbed infrastructure and overhead costs

# Business and Marketplace Impacts

- Impacts on Contractor Base
- Reduced profitability and risk of loss
- New requirements for independent financing
- Reduced valuations
- No horizontal consolidation, but search for new, profitable business (targeted acquisitions, make-instead of buy, foreign sales)

# Business and Marketplace Impacts

- DoD Industrial Base Policy\*
- “Committed to maintain the health and productivity of the industrial base”; needs to “adapt its industrial base considerations and actions to the emerging fiscal realisms.”
- Not concerned about major primes; but “this vast majority” of the base “act as suppliers”; “companies at any tier, and of any size, may offer critical or hard-to-value products”
- “We do expect some niche firms to face difficulty due to decreased demand” and will “attempt...if necessary, to mitigate these issues.”

– \*Brett Lambert, HASC Testimony, November 20

# Business and Marketplace Impacts

- “Commercial” Suppliers may withdraw due to reduced, unstable demand, on top of the degradation of 1990s “commercial item” policies designed to encourage their participation.

# Business and Marketplace Impacts

- Service Contractors will feel the biggest impact of budget austerity, because of flexibility of cuts in O&M funding as well as pre-existing criticism of perceived excessive outsourcing and undisciplined contracting.



# Business and Marketplace Impacts

- Small Business is promised a substantial piece of the reduced market (by legislation and policy) but budget limitations, coupled with objections from non-small business suppliers, may have a chilling effect on these policies. In addition, the planned strategic sourcing initiatives threaten small business opportunities.

# Business and Marketplace Impacts

- Loss of a major contract or expected business, reducing resources and the base over which a contractor's overhead is spread, will impair its ability to win future business in the expected price-driven competitions. For contractors dependent on government business, the new competitions, will essentially be battles for business base. It is predictable that many contractors will take the necessary risks and bid seeking revenues, not margins.

# Questions?

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# Enhanced Challenges For Contract Administration and Dispute Resolution

J. Chris Haile

# Challenges for Industry

- Increased Focus on Fraud and Oversight
- Cancellations, delays, and restructuring
- Pressure to provide concessions after performance begins
- Incremental funding and funding gaps
- Constraints and burdens on Government personnel
- Scarce funding for negotiated equitable adjustments

# Impacts on Investigation Policy

- Expect further intensification of programs against procurement “fraud, waste, and abuse” to protect and reclaim scarce funds. For example:
- Increased coordination of “fraud” remedies between DOJ/IGs and acquisition officials
- Significant IG influence
- More requirements for disclosures, cooperation, and certifications
- Aggressive DOJ FCA interpretations (implied certifications and fictitious damages)
- FAPIIS and past performance
- Automatic and aggressive “fact-based” suspension and debarment

# Increased Regulation And Oversight

- Example: FY 2013 NDAA
- §827-828 – Enhancement of whistleblower protections for contractor employees; pilot program
- §829 – Extension of contractor conflict of interest limits
- §848 – Special provisions concerning overseas contingency operations-responsibilities of CIGIE and Lead Inspector General
- §852 – FAPIIS information to include information on any parent, subsidiary, or successor entities
- §853 – Ensuring inclusion of past performance information for source selection decisions
- §861 – Requirements for SDOs of DOD, DHS, and USAID, including documenting “the basis for any final decision taken pursuant to a formal referral” and “policies” for considering

# Cancellations, Delays, and Contract Restructuring

- The Government will continue to address budget challenges in part by slowing, restructuring, or terminating contract work.
- Those most likely to see substantial impacts are lower-priority, higher-cost, and underperforming projects. But contractors are seeing the effects more broadly.



# Cancellations, Delays, and Contract Restructuring

- Impacts are taking a variety of forms:
  - performance delays / stretch outs
  - Requests for concessions
  - Deductive changes
  - Terminations for convenience
  - Termination for default

# Delays

- Standard form contracts give the Government the right to issue a Stop Work Order for 90 days (or more by agreement) and give the contractor an equitable adjustment remedy. FAR 52.242-15.
- When the period ends the contractor is required to resume work or the Contracting Officer is required to terminate the work covered by the order, either for default or convenience. The contractor is also given a remedy for Government delay of work, but without profit. FAR 52.242-17.
- Projecting the impacts and calculating the costs of delay will be complicated and more likely disputed by a customer seeking to conserve funds.

# Bilateral Agreements - Risks

- The Government has sought bilateral agreements to change or restructure contracts in order to save (or at least reduce the cost of) programs.
- Risks for contractors include waiver and/or release of claims. See *Amertex Enterprises, Ltd. v. U.S.*, 1997 WL 73789 (Fed. Cir. 1997) (unpublished), reh'g denied, 108 F.3d 1372, cert. denied, 522 U.S. 1075 (1998) (agreement to perform waived damages remedy for cardinal change, even without a release); *Bell BCI Co. v. U.S.*, 570 F.3d 1337, reh'g denied (Fed. Cir. 2009), (modification interpreted as releasing cumulative impact claim).
  - Contractors agreeing to perform on restructured terms should consider reserving rights with respect to, or not assume the risk of, unaddressed potential impacts and damages, as well as to preserve any pre-existing claims.

# Bilateral Agreements - Coercion

- What if the Government says: “sign this deal or we will cancel your contract.” May the contractor later plead economic coercion or duress?
- Avoiding releases based on duress may require an extremely high burden of proof.
  - Compare: *Systems Technology Assoc., Inc., v. U.S.*, 699 F.2d 1383 (Fed. Cir. 1983) (coercive threat “violates notions of fair dealing”) to *Am-Pro Protective Agency v. U.S.*, 281 F.3d 1234 (Fed. Cir. 2001) (indicating subjective bad faith is required)

# Termination For Convenience

- With a fixed price contract, recovery of performance costs and profit is limited by the total contract price.
- In the termination settlement of a loss contract, no profit is recovered, and cost recovery is subject to reduction based on the loss percentage.
- These put greater emphasis on the need to address contract changes promptly during performance.

# Termination For Convenience – Contracts Subject to Funding

- Contracts with “Limitation of Cost” or “Limitation of Funds” provisions require contractor notice where funds are running out and put the risk of continued performance on the contractor.
- Relieves the Government of liability for “costs incurred in excess of” allotted funding “[e]xcept as required by other provisions of this contract, specifically citing and stated to be an exception to this clause.”

# Performing in the Absence of Funding

- The need to keep programs going may persuade contractors to perform in the absence of, or in advance of appropriations, particularly where a limitation of funding clause permits subsequently appropriated funds to be applied to prior performance. FAR 52.232.20(f).
- The Anti Deficiency Act prohibits the “acceptance of voluntary services,” 31 U.S.C. §1342, and encouraging a contractor to perform in the absence of funds violates the Act. 48 CFR §32.704(3); see also DoD IG D-2008-079 (AF Management of Incremental Funds).

# Partial Terminations/Deductive Changes

- A de-scoping of contracts to save funds will raise the issue whether such action should be treated as a partial termination or a deductive change.
  - This is a fact dependent issue, but a usual guideline is whether a line item or quantity is deleted or a specification is deleted.
  - Often, if the deleted requirement is profitable, the contractor would prefer a deductive change, because the price would be reduced on an actual cost basis.
  - The issue may be complicated by potential downstream performance impacts of the work deletion. Impacts on subcontract pricing and supplier chain complications must be considered with respect to these and other government actions.



# Default Termination Issues

- The Government is increasingly likely to terminate for default when the contractor is delinquent or deemed unlikely to perform to contract requirements.
- The Government may avoid termination costs and even reclaiming scarce funds.

# A Contractor's Duty to Proceed

- The government's required program changes and "restructuring" to fit available funding may exceed its unilateral contract rights, such as the limits of the Changes clause, either the listed items that can be changed or the "general scope of the work." See FAR 52.243-1.
- Prior to the Contract Disputes Act, a "cardinal change" was deemed a breach, the resulting dispute was not seen as "arising under the contract," and thus the contractor was not obligated to perform. But see *Alliant Techsystems, Inc. v. U.S.*, 178 F.3d 1260, reh'g denied, 186 F.3d 1379 (1999) (change to option delivery schedule rendered exercise ineffective, but contractor was required to perform under Disputes clause because option change was not a cardinal change).

# A Contractor's Duty to Proceed

- Many contracts likely to be restructured contain the alternate “all disputes” clause adopted in the regulatory implementation of the CDA. FAR 52.233-1, Alternate I (disputes “relating to the contract”).

# Constraints and Burdens on Government Personnel

- Staffing constraints increase burdens on contracting personnel
- Slower response times
- Challenges to obtaining necessary focus
- Periods of budget uncertainty can paralyze contracting personnel and processes

# Challenges To REA Settlements

- Contracting officers have diminished ability to fund settlement of meritorious requests for equitable adjustment.
- This may slow or stop the negotiations process.
- In some cases, resolution by submission of a claim and resort to the Judgment Fund may be the only viable option for recovery.

# Payment From the Judgment Fund

- The Judgment Fund, is a “permanent, indefinite appropriation” to pay judgments and awards under the Tucker Act and the Contract Disputes Act, 31 U.S.C. §1304.
- Under current practice, settlements by procuring agencies are paid from the Judgment Fund when a Board of Contract Appeals, having jurisdiction, embodies the settlement in an award.

# Payment From the Judgment Fund (cont'd)

- Payment from the Judgment Fund is not a violation of the Anti Deficiency Act.
  - See, e.g., *Samish Indian Nation v. U.S.*, 657 F.3d 1330 (Fed. Cir. 2011) (Judgment Fund “established to pay monetary damage judgments against the Government when other funds are unavailable”). The Circuit cited *Ferris v. U.S.*, 27 Ct. Cl. 542 (1892) (an appropriation “merely imposes limitations upon the government’s own agents; ...its insufficiency does not...cancel its obligations, nor defeat the rights of other parties.”).
  - See also, the Supreme Court decision in *Salazar v. Ramah Navaho Chapter*, (June 18, 2012).
  - The procuring agencies’ obligation under the CDA to reimburse the fund, 41 U.S.C §612, is an internal government issue; lack of appropriation for this purpose does not affect the rights of contractors. See GAO-08-295R, Judgment Fund Reimbursements (February 2008) (reporting failure to reimburse CDA judgments).

# Questions?

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# Labor / Employment Challenges

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# WARN Act Issues

- Triggering Events
  - Mass layoff
  - ‘plant closing’
- Conditional Notice
- Litigation Issues
- Particular concerns for unionized employers

# Reductions in Force

- Begin with the end in mind
  - Determine goal (e.g. reduce X headcount, reduce X dollars, eliminate particular programs, etc.)
  - Establish selection process from the outset
  - Appropriate decisional units and OWBPA notices
- Adverse impact analyses
  - Race (minorities and individual races), gender, age, other?
  - Conducted pursuant to attorney-client privilege
  - Preserve final RIF documentation and justifications

# Whistleblower Protection Laws

- Increased focus on whistleblower protection
  - FCA, SOX, Dodd Frank, ARRA, PPACA
  - 20+ other federal whistleblower laws enforced by OSHA
  - State whistleblower protection laws
- NDAA revisions
  - Extends to civilian contractors and subcontractors
  - Internal reporting included in protected activity
  - Expansion of protected disclosures
  - Reprisal at agency's request is not a safe harbor
  - Employee notification required

# Regulatory Initiatives

- Department of Labor (DOL):
  - Independent contractor/employee misclassification
  - Wage hour enforcement
- Equal Employment Opportunity Commission (EEOC)
  - new emphasis on class wide systemic employment issues
  - Challenges to employer wellness programs

# Regulatory Initiatives (cont'd)

- National Labor Relations Board (NLRB)
  - New concerns even for non-union employers
    - Code of Conduct policies
    - Social media policies

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# Strategic Considerations for Appropriations

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## *Protect the Line*

We saw real impacts on defense contractors with the release of the FY 2014 President's budget. Contracts were terminated early. Whole programs were cancelled. This is just the beginning in a tough budget environment. If you aren't at the table, you are on the menu.

- Precision Tracking Space System (PTSS): **terminated**
- Expeditionary Combat Support System (ECSS): **terminated**
- Standard Missile-3 Block IIB (SM-3 IIB): **restructured** “to focus on common kill vehicle technology”
- Ground Combat Vehicle (GCV): **restructured** with the lengthening of the Technology Development (TD) and Engineering, Manufacturing, and Development (EMD) phases



http://www.gpo.gov/fdsys/pkg/CREC-2013-03-11/pdf/CREC-2013-03-11.pdf

gpo.gov

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7	<b>AH-64 APACHE BLOCK IIIA REMAN</b> Unjustified unit cost increase	<b>577,115</b>	<b>527,115</b> -50,000
8	<b>AH-64 APACHE BLOCK IIIA REMAN (AP-CY)</b> Excess advance procurement	<b>107,707</b>	<b>101,707</b> -6,000
9	<b>AH-64 APACHE BLOCK IIIB NEW BUILD</b> Additional aircraft	<b>153,993</b>	<b>224,993</b> 71,000
10	<b>AH-64 APACHE BLOCK IIIB NEW BUILD (AP-CY)</b> Excess advance procurement	<b>146,121</b>	<b>135,421</b> -10,700
13	<b>UH-60 BLACKHAWK (MYP)</b> Program increase - only for the Army National Guard	<b>1,107,087</b>	<b>1,306,087</b> 199,000
15	<b>CH-47 HELICOPTER</b> Additional aircraft	<b>1,076,036</b>	<b>1,186,036</b> 110,000
18	<b>MQ-1 PAYLOAD - UAS</b> Army requested transfer to RDTE,A line 131 for EMAARS	<b>231,508</b>	<b>184,608</b> -46,900
23	<b>CH-47 CARGO HELICOPTER MODS</b> Cargo on/off loading system with ballistic protection	<b>39,135</b>	<b>87,935</b> 48,800
26	<b>UTILITY HELICOPTER MODS</b> UH-60 A to L conversion - only for the Army National Guard	<b>73,804</b>	<b>183,804</b> 110,000
27	<b>KIOWA WARRIOR</b> OH-58 recap Cockpit and sensor upgrade program - ahead of need	<b>192,484</b>	<b>119,584</b> -37,200 -35,700
32	<b>RQ-7 UAV MODS</b> Ahead of need	<b>104,339</b>	<b>29,265</b> -75,074

Done



## PLUS the Line

In spite of a shrinking defense budget, a well executed political strategy coupled with addressing a programmatic need has brought to light the “new” earmark.

113-HR933-EcState.pdf - Adobe Reader

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222 (1 of 3) 130%

Tools Sign Comment

	Budget Request	Commerce
<b>1 UNIVERSITY RESEARCH INITIATIVES</b>	<b>113,690</b>	<b>133,690</b>
Program increase - cooperative based university research program		20,000
<b>3 DEFENSE RESEARCH SCIENCES</b>	<b>473,070</b>	<b>482,070</b>
Nanotechnology research		9,000
<b>4 POWER PROJECTION APPLIED RESEARCH</b>	<b>89,189</b>	<b>99,189</b>
Program increase - power projection applied research		10,000
<b>5 FORCE PROTECTION APPLIED RESEARCH</b>	<b>143,301</b>	<b>209,301</b>
Alternative energy research		40,000
Materials research and technology		13,000
Power generation and storage research		13,000
<b>10 OCEAN WARFIGHTING ENVIRONMENT APPLIED RESEARCH</b>	<b>49,635</b>	<b>64,635</b>
Program increase - AGOR mid-life refit		15,000
<b>19 ELECTROMAGNETIC SYSTEMS ADVANCED TECHNOLOGY</b>	<b>54,858</b>	<b>63,858</b>
Advanced radar research		9,000
<b>FUTURE NAVAL CAPABILITIES ADVANCED TECHNOLOGY DEVELOPMENT</b>	<b>256,382</b>	<b>288,382</b>
Technology transition - restore unjustified reduction		32,000
<b>23 WARFIGHTER PROTECTION ADVANCED TECHNOLOGY</b>	<b>3,880</b>	<b>42,580</b>
Program increase - bone marrow registry program		31,500
Program increase - tactical athlete program		7,200
<b>24 UNDERSEA WARFARE ADVANCED TECHNOLOGY</b>	<b>0</b>	<b>10,000</b>
Program increase - ASW research		10,000
<b>35 SURFACE AND SHALLOW WATER MINE COUNTERMEASURES</b>	<b>190,622</b>	<b>188,622</b>
Excess to need		-2,000
<b>43 SURFACE ASW</b>	<b>6,704</b>	<b>4,504</b>
Program execution		-2,200



## ***CREATE the Line***

- Introduce new technology solutions to unanswered or emerging DOD needs (obesity, orphan diseases, cybersecurity)
- Identify legislative vehicles to craft and support the military need
- Identify willing program managers
- Leverage support of Congressional Champions
- Introduce to prime defense contractors and develop coordinated outreach plan with prime contactors
- Request/support changes to SOW augmentation plan, contracts, and other documents

FY 2013 NDAA: SEC. 216. ADVANCED ROTORCRAFT INITIATIVE.

*(a) In General- Not later than 180 days after the date of the enactment of this Act, the Under Secretary of Defense for Acquisition, Technology, and Logistics shall, in consultation with the military departments and the Defense Advanced Research Projects Agency, submit to the congressional defense committees a report setting forth a strategy for the use of integrated platform design teams and agile prototyping approaches for the development of advanced rotorcraft capabilities.*

*(b) Elements- The strategy required by subsection (a) shall include the following:*

*(1) Mechanisms for establishing agile prototyping practices and programs, including rotorcraft X-planes, and an identification of the resources required for such purposes.*

*(2) The X-Plane Rotorcraft program of the Defense Advanced Research Projects Agency with performance objectives beyond those of the Joint Multi-role development program, including at least two competing teams.*

*(3) Approaches, including potential competitive prize awards, to encourage the development of advanced rotorcraft capabilities to address challenge problems such as nap-of-earth automated flight, urban operation near buildings, slope landings, automated autorotation or power-off recovery, and automated selection of landing areas.*

# Questions?

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# **General Counsel Panel**

**Christian Bonat, Sikorsky Military Systems**

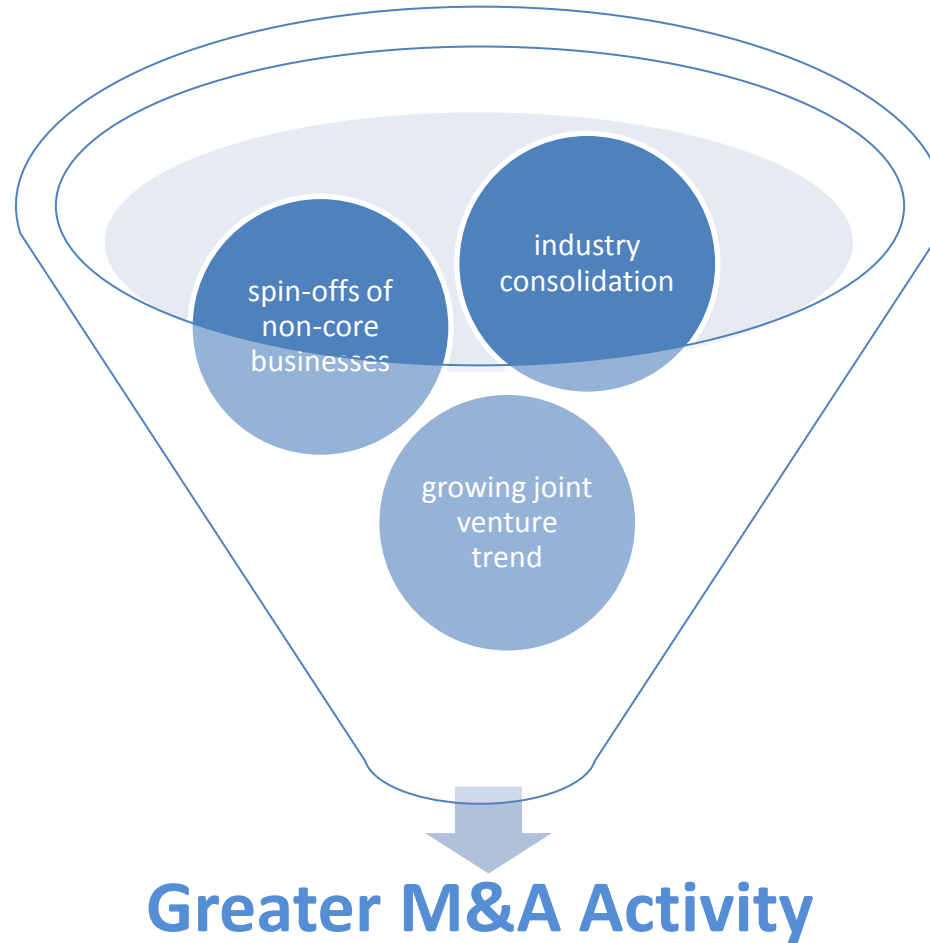
**Alice Eldridge, BAE Systems**

**Beth Newsom, Lockheed Martin Corporation**

# **Emerging M&A Trends in the Current Market: How Sequestration and Other Industry Factors are Shaping the Way Deals are Done--or Not**

**Morris DeFeo  
Kelly Howard  
Karen Hermann**

# Why M&A?





# Due Diligence

## Traditional Focus

- Valuation
  - EBITDA
  - Revenue waterfall
- Potential Risks –
  - Audits
  - Claims
  - Investigations

## New Heightened Focus

- Valuation
  - Backlog and program assessment
  - In-sourcing risks
  - Risks of termination for convenience or non-renewal
  - Margin sustainability
- Potential Risks --
  - Cyber security vulnerabilities
  - Deficiencies in business processes and procedures
  - Successor liability
  - Contingent liabilities

# Anxiety-Ridden Risk Allocation

## Representations and Warranties

- More rigid, less qualified representations
- Particularly, compliance with laws, certifications, terminations for default, disputes or outstanding claims

## Emphasis on Closing Conditions / Deal Certainty

- Detailed Material Adverse Change provisions

## Greater Indemnification Protection

- Higher caps / longer escrows

## More Reliance on Deferred or Contingent Deal Consideration

- Earn-outs
- Management Incentives

# Other Transaction Structures

## Key Drivers:

- Reduce costs
- Increase likelihood-of-win percentage

## Benefits:

- Ability to enter international playing fields otherwise closed to foreign participants
- Obtain the advantage of a potential acquisition target's offering without the acquisition costs and risks

## Risks/Challenges:

- Tension among co-owners regarding governance, equity/profit allocation, etc.
- Risk of deadlock
- Risk of default by co-owner
- Internal control/compliance issues

# Questions?

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# Chasing International Procurement Markets

Alan W. H. Gourley

Maysa Verzola

Adelicia R. Cliffe

# Mitigating Int'l Contracting Risk

- Foreign Intermediaries
- Offset Obligations
- Investment Protection
- International Arbitration



# Foreign Intermediaries

- Payment Terms
  - Contingent Fees are lawful!
  - Cost Allowability & Reporting are the issues
- Brokering Activities
  - US & EU
  - DDTC Preparing Final Rule
    - Narrows persons and activities
    - Start of brokering remains unclear
- Anti-corruption compliance & due diligence
  - Compliance certifications are not enough!



# Offset Obligations

- Understanding Performance
  - What earns credits?
  - How calculated?
  - Nature of involvement with local partner (Are you investing?)
- Corruption Risks
  - See Due Diligence and Corruption Risk in Offset Programmes (TI-UK 2012)

# Anti-Corruption

- DOJ's increased willingness to pursue foreign intermediaries
  - Also use Money Laundering statutes
- DOJ/SEC Guidance on FCPA (Nov 2012)
  - Compendium of prior government guidance and positions
- DOJ Opinion 12-01 (Sept 18, 2012)
  - Royal family member not acting as a Foreign Official

# Investment Protections

- How do you get protections?
  - Bilateral Investment Treaties (BITS) & some multilateral regimes
  - Plan investment to take advantage
- What protections?
  - Expropriation
  - National Treatment/Most Favored Nation
  - Fair & Equitable Treatment
  - Full Protection & Security
- Enforcement through Investor-State arbitration

# International Commercial Arbitration

- Think before you sign!
  - Institutional vs. Ad Hoc
  - Choice of Law/Site of Arbitration
  - Number, qualifications and process for selecting arbitrators
  - Interim measures
- No one size fits all

# Brazil: Land of Opportunity



**Maysa Abrahão Tavares Verzola**

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# How big is Brazil?

## Brazil in numbers



- Territorial Area:**  
8,515,767 km<sup>2</sup>
- Coastline:**  
7,367 km
- Population:**  
194 million
- Form of Government:**  
Democratic Republic,  
with a presidential system
- Nominal GDP:**  
R\$: 4.4 trillion  
US\$: 2.25 trillion
- GDP per capita in:**  
R\$: 22.4 thousand  
US\$: 11.4 thousand
- Risk rating by major agencies:**  
Moody's: Baa2  
S & P: BBB  
Fitch : BBB

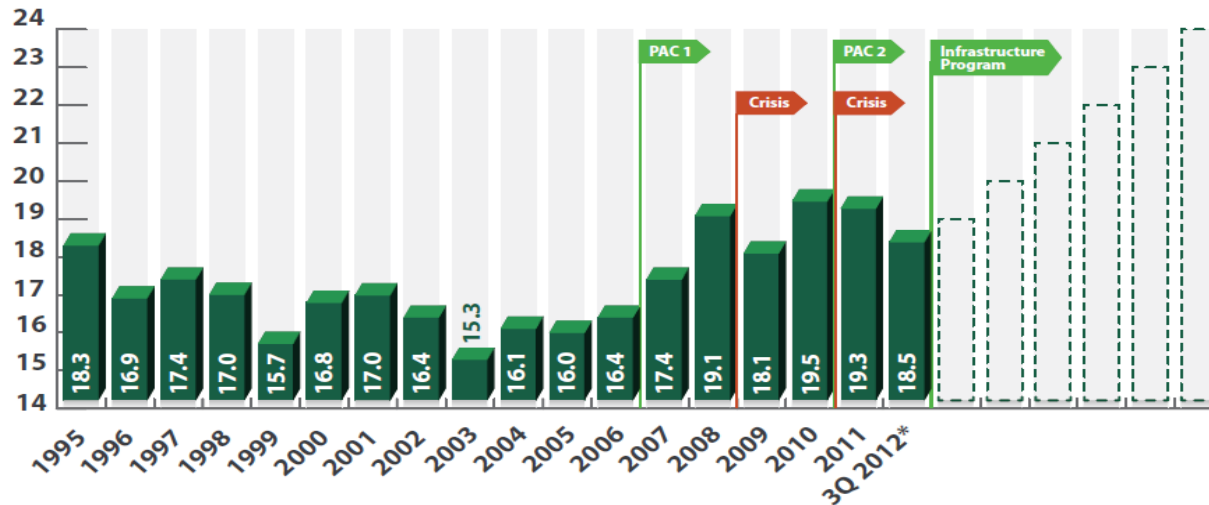
*Source: Brazilian Institute of Geography and Statistics (IBGE) and Brazilian Central Bank  
Produced by: Ministry of Finance*

# Government Spending

## Increased investment as a government priority

One of the main challenges of the Brazilian economy is increasing its investment rate. As of 2008 it has reached new heights, which have fluctuated between 18% and 20% of GDP. The goal of the Government is to increase gross fixed capital formation even further in order to ensure sustainability to the acceleration of economic growth.

Gross Fixed Capital Formation, as % of GDP



\* 4-Quarter accumulated up to 3<sup>rd</sup> quarter of 2012











Source: Brazilian Institute of Geography and Statistics (IBGE)

Produced by: Ministry of Finance

# Major Investment Programs

## Large investment programs

Several major infrastructure programs were announced over the last two years, with investments adding around US\$ 235 billion over the coming years, not to mention the major urban infrastructure works required for the 2014 World Cup and the 2016 Olympics.

Investment in scheduled concessions (estimate)	US\$ billion
<b>Logistics</b>	<b>121.0</b>
Roads 	21.0
Railways 	45.5
Ports 	27.3
High Speed Train (TAV) 	17.8
Airports 	9.4*
<b>Energy</b>	<b>74.0</b>
Hydro 	39.9
Wind, Biomass and Small Hydro 	19.0
Thermal 	1.4
Distribution 	13.7
Oil & Gas 	40.0
<b>Total</b>	<b>235.0</b>

\* Includes estimated investment in regional airports  
In January 2013, the exchange rate was approximately US\$ 1 = R\$ 2.00

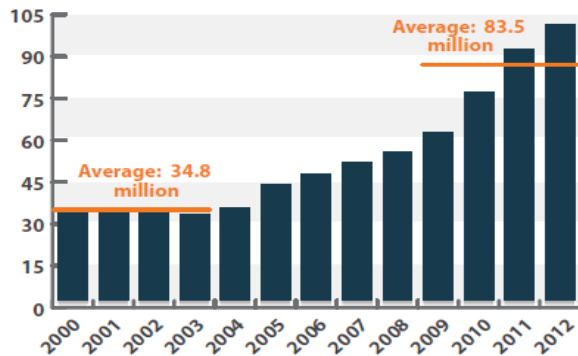
Source: National Logistics & Planning Company (EPL), Energy Research Company (EPE), Ministry of Mining and Energy (MME) and Ministry of Finance  
Produced by: Ministry of Finance



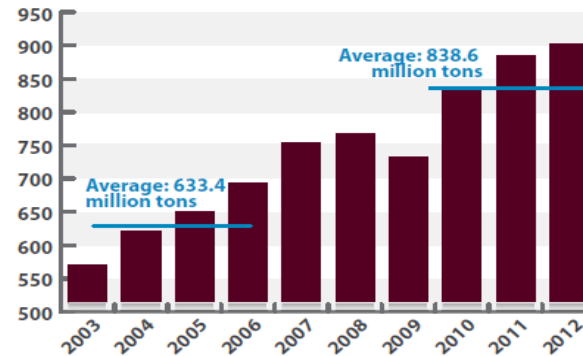
# Infrastructure Demand - Transportation

## Demand for infrastructure

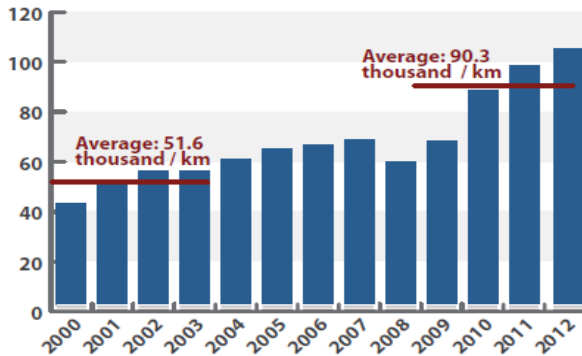
**Airline industry, in million passengers**



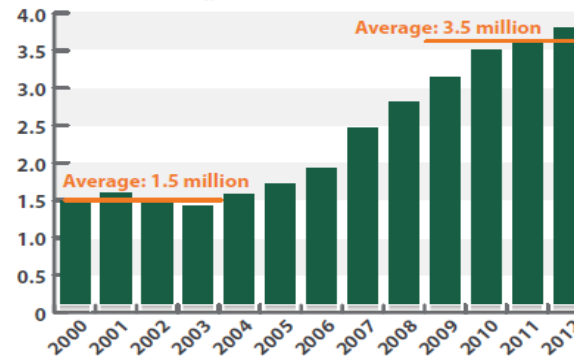
**Total cargo handling in ports, in million tons**



**Thousand vehicles per km on highways under concession**



**New vehicles (buses, trucks, light commercial vehicles and cars), in million**



Source: National Agency for Civil Aviation (ANAC), National Agency for Aquatic Transportation (ANTAQ), Brazilian Association of Highway Concessionaires (ABCR) and Brazilian Association of Automotive Vehicle Manufactures (ANFAVEA)  
 Produced by: Ministry of Finance

# Public Procurements Government Contracts

**GOAL:** assure compliance of principle of equality + most advantageous tender to Public Administration (price and technique)

General principles:

- equality
- honesty
- abidance by the bid document
- sustainable national development
- objective judgment
- lowest price

# Public Procurements in Brazil

- Different types:
  - Basic Legislation – Federal Law n. 8,666/93
  - Special Regimes – Upcoming Sporting Events
  - Permissions and Concessions – Fed. Law n. 8,987/95
  - Public-Private Partnerships – Fed. Law n. 10,079/04
  - Acquisitions by Defense Sector
  - Acquisitions by Petrobras
  - Acquisition of standardized goods

## Public Procurements in Brazil

- Pre-Contract Phases:
  - Request for Tenders
    - Challenging tender documents
  - Qualifying for Tenders
    - Challenging tenders

## Public Procurements in Brazil

- Post-Contract Disputes:
  - Economic-financial equilibrium
  - Contract penalties
  - Administrative penalties

Brazilian companies have some advantages:

- Minimum national content
- Preference margin of 25% in price

**SOLUTION** - JVs or consortia with Brazilian companies / local subsidiaries

# Export Control Reform (“ECR”)

- How far have we come?
  - Rebuilding the control lists
  - Transition rules
  - “Specially designed”
- Prospects for completion

# Rebuilding of the control lists

- Inching towards more positive lists
  - “Final” rules covering 3 categories
    - Aircraft and Related Articles and Gas Turbines Engines and Associated Equipment now final
  - 9 other proposed rules
  - Some difficult ones remain:
    - Cat. XI - Satellites
    - Cat. IX – Training Equipment, Cat. X – Protective Equipment
    - Cat. XII - Sensors



# First final rules (“the beast”)

- April 16, 2013, State and Commerce each published first final rules:
  - 3 categories
  - “Transition” rules – 180 days and beyond
  - Common definition of “specially designed”
    - The touchstone for moderating control creep

# Transition rules

- New categories/jurisdiction effective 180 days after publication
- Dual licensing
- Grandfathering of licenses
- Future of Commodity Jurisdiction (“CJ”) Determinations
- Application of Strategic Trade Authorization (“STA”) license exception to items moving from the USML to the CCL
  - Limitations and compliance requirements

# “Specially designed”

- Previous lack of common terminology or of definitions
  - Led to unpredictability
  - Regulatory creep as even insignificant changes could result in capture under licensing regime – particularly USML

# “Specially designed”

- New harmonized definition of “specially designed” seeks to provide objective criteria for control
- Employs a “catch and release” concept
  - “Catches” items that, as a result of development, have properties peculiarly responsible for achieving or exceeding the controlled performance levels, characteristics, or functions described in the relevant USML or ECCN entry
  - “Releases” certain parts, components, accessories, attachments, and software for use from control if certain conditions are met
    - e.g., the item has the same function, performance capabilities, and the same or “equivalent” form and fit as a commodity or software used in or with an item in production and not enumerated the USML

# Prospects for completion?

- Near horizon
  - Revised definition “defense services”
  - DDTC guidance on CJ requests
- Far horizon
  - Single List
  - Single Agency

# Questions?

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# Managing the Cyber Threat Crisis

Cyber Threats & Enforcement Risks for  
Corporate Boards & Officers

David Z. Bodenheimer





# Digital Pearl Harbor

DoD Secretary  
Panetta



**“cyber Pearl Harbor” (2012)**

DHS Secretary  
Napolitano



**“cyberattack” data like 9/11 (2012)**

FBI Director  
Mueller



**“greatest threat to our country” (2012)**

# Cyber Theft & Espionage: Why Corporate Boards & Officers Need to Worry Now



Secrets  
Gone?



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# Cyber Theft & Espionage



- Intelligence Warnings
- The loss of intellectual property due to cyber attacks amounts to the “greatest transfer of wealth in human history.”
- (Gen. Keith Alexander, U.S. Cyber Command Chief & NSA Director, July 2012)
- More Warnings
- Counterintelligence Executive Report (Oct. 2011)
- GAO Report & Testimony (June 2012)
- Defense Security Service Trend Analysis (2012)
- National Intelligence Estimate (2013)
- Mandiant Investigative Report (2013)

# Foreign Cyber Threats



- 40,000 Hackers: “There are forty thousand Chinese hackers who are collecting intelligence off U.S. information systems and those of our partners.” (Adm. McConnell, Jan. 2008)
- Daily Attacks. “A defence force source said yesterday that attacks initiated from China occurred almost on a daily basis.” (Australian Defense Force, Apr. 2009)
- Classified Data Compromised. “A China-based cyber espionage network had accessed 1200 computers in 103 countries containing classified documents.” (Munk Centre for Int’l Studies, Apr. 2009)
- China’s Cyber Spy House



FIGURE 7: Unit 61398 Center Building 208 Datong (rear view, possible generator exhausts visible) Image Copyright 2013 city8.com

# Data Losses & Cyber Breach

- 2x Library of Congress
- → 38 terabytes of lost data
- “As an example of the threat, one American company had 38 terabytes of sensitive data and intellectual property exfiltrated from its computers – equivalent to nearly double the amount of text contained in the Library of Congress.”
- [Sen. Whitehouse, May 10, 2010]
- It’s Personal
- “As an example, in 2008, [China’s] APT1 compromised the network of a company involved in a wholesale industry. . . . Over the following 2.5 years, APT1 stole an unknown number of files from the victim and repeatedly accessed the email accounts of several executives, including the CEO and General Counsel.”
- [Mandiant Report (Feb. 2013)]



# IP Cyber Losses



- One Company's IP Loss
- "For example, a 2011 FBI report noted, "company was the victim of an intrusion and lost 10 years' worth of research and development data –valued at \$1 billion – virtually overnight."
- CRS Report, 2013  
Cybersecurity Executive Order (Mar. 2013)
- \$1 Trillion IP Losses
- "Last year alone, cyber criminals stole intellectual property from businesses worldwide worth up to \$1 trillion." (President Obama, 2009)





# Stock Price Losses



- Investors Really Care
- 70% of investors – interested in reviewing corporate cyber practices
- 80% of investors – likely would not invest if history of cyber attacks
- Zogby Analytics Survey (Mar. 2013)
- Stock Prices Hammered
- 9% Stock Loss – after Global Payments breach (before trading halted)
- 84% Stock Loss – after Chinese firm took AMSC's source code



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# Cybered M&A Deals



- Infiltrated M&A Deals
- \$2.4 Billion Huiyuan Deal. Coca Cola's deal collapsed after hackers took key files
- \$40 Billion BHP Deal. BHP Billiton Ltd's bid to acquire Potash Corp. collapsed after cyber theft
- "Coke Gets Hacked and Doesn't Tell Anyone," Bloomberg.com (Nov. 2012)
- Nat. Counter Intel Report
- "Information was pilfered from the corporate networks of a US Fortune 500 manufacturing company during business negotiations in which that company was looking to acquire a Chinese firm . . . . [T]his may have helped the Chinese firm attain a better negotiating and pricing position." [National Counter-intelligence Executive, Oct. 2011]



# Cybered Negotiations



- \$1.3 Billion Left on Table
- “In one case, officials estimated the cost of lost data from a British company . . . Jonathan Evans, head of Britain’s MI5 domestic security service, said . . . digital intruders targeting a ‘major London listed company’ had caused a loss of 800 million pounds (\$1.3 billion), in part because of the resulting disadvantage in ‘contractual negotiations.’”
- “China-Based Hacking of 760 Companies Shows Cyber Cold War,” Bloomberg.com (Dec. 2011)
- Double-Digit Losses
- After China’s APT1 compromised the network of a company in the wholesale industry, “major news organizations reported that China had successfully negotiated a double-digit decrease in price per unit with the victim organization for one of its major commodities.”
- Mandiant Report (Feb. 2013)

# Cybered Operations

- 30,000 Dead Computers
- “In August 2012, a series of cyber attacks were directed against Saudi Aramco, the world’s largest oil and gas producer and most valuable company. The attacks compromised 30,000 of the company’s computers and the code was apparently designed to disrupt or halt the production of oil.”
- [CRS, 2013 Cybersecurity Executive Order, Mar. 2013]
- Iranian Cyber Attacks
- Bank of America & J.P. Morgan Chase Cyber Attacks. “I don’t believe these were just hackers,” [Sen.]Lieberman said . . . . “I believe this was done by Iran and the Qods force, which has its own developing cyber attack capacity.”
- “In a ‘highly classified’ report last week the Joint Chiefs of Staff’s Intelligence Directorate, or J-2, confirmed continuing Iranian cyber attacks against U.S. financial institutions, NBC said.”
- [Matt Egan, FoxBusiness, Sept. 24, 2012]



# How Do You Know When Your Company is a Cyber Target?



# Who's a Cyber Target?



- McAfee Survey
  - 60% reported “chronic and recurring loss” of sensitive information
- CSIS Report
  - 85% energy/power sector experienced “network intrusions”
- Mandiant Report
  - 141 companies in 20 major industries compromised by cyber intrusions (Mandiant Report)
- 2 Types of Companies
- “There are only two types of companies: Those that have been hacked, and those that will be. Even that is merging into one category: Those that have been hacked and will be again.”
- FBI Director
- Robert Mueller
- (Mar. 2012)



# Who's a Cyber Target?



- Top Cyber Targets
- Information Technology
- Communications
- Military Technology
- Aerospace
- Dual Use Technology
- Healthcare & Pharma
- Agricultural Technology



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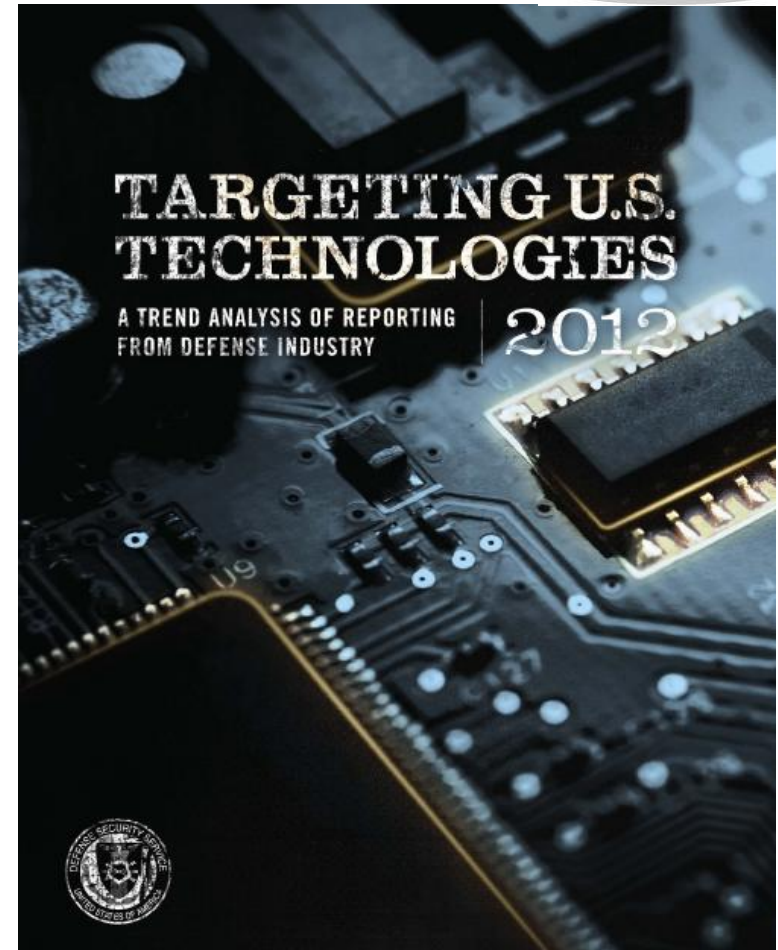


# Who's a Cyber Target?



## TOP TARGETED TECHNOLOGIES\*

-  INFORMATION SYSTEMS
-  LASERS, OPTICS, AND SENSORS
-  AERONAUTICS SYSTEMS
-  ELECTRONICS
-  ARMAMENTS AND ENERGETIC MATERIALS
-  SPACE SYSTEMS
-  MARINE SYSTEMS
-  POSITIONING, NAVIGATION, AND TIME
-  MATERIALS AND PROCESSES
-  GROUND SYSTEMS
-  INFORMATION SECURITY
-  PROCESSING AND MANUFACTURING



# Who's Attacking Who?



## Who are the Hackers?

- Foreign Nations →
- Organized Crime →
- Terrorists →
- Hactivists →
- Hackers for Hire →

## What are the Targets?

- Cyber Espionage (IP)
- ID Theft (personal data)
- Critical Infrastructure
- Political Disruption
- All of the Above



# Who Are the Enforcers Coming After You – After a Security Breach?



Secrets  
Gone?





# Cyber Risks – SEC Scrutiny

- SEC Scrutiny
  - - Disclose material risks?
- Impact
  - → SEC scrutiny or actions
- “Cyber risk management is a critical corporate responsibility. Federal securities law requires publicly traded companies to disclose ‘material’ risks and events, including cyber risks and network breaches. A review of past disclosures suggests that a significant number of companies are failing to meet these requirements.” [Senate Commerce News Release, May 12, 2011]
- SEC Disclosure Duty
  - Division of Corporation Finance Securities and Exchange Commission
  - CF Disclosure Guidance: Topic No. 2 Cybersecurity
  - Date: October 13, 2011
  - Summary: This guidance provides the Division of Corporation Finance's views regarding disclosure obligations relating to cybersecurity risks and cyber incidents
- Disclosure Duties
  - Risk of Cyber Incidents
  - Prior Security Breaches
  - Adequacy of Preventative Measures



# Cyber Risks – Shareholders

- Disclose Risks – Or Not?
- Rock & a Hard Place?
- \$20 Million Suit. Countrywide's lax "internal procedures" & security breach [Courthouse News, Apr. 5, 2010]
- \$7.2 Million/Incident. "average cost of a data breach hit \$7.2 million last year" [NYT, Dec. 2011]
- Shareholder Actions
- Delaware case law (corporate director's good faith duties re information & reporting systems, plus potential liability for damages)
- National Counterintelligence Executive Report (Oct. 2011)

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# Cyber Risks – Congress

- Congressional Inquiry
- Sen. Rockefeller's Letter
- 300 CEOs Responded
- Did Your CEO Respond?
- What did your CEO say?
- Is your company doing it?
- Will a plaintiff get hold of it?

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September 19, 2012

## Fortune 500 CEO USA

I was profoundly disappointed that the United States Senate's effort to pass comprehensive cybersecurity legislation was blocked by a partisan filibuster last month. The cyber threats we face are real and immediate, and Congress's failure to pass legislation this year leaves the country increasingly vulnerable to a catastrophic cyber attack. Because of the urgency of the need to address this threat, in August following the Senate's failure to act, I urged President Obama to use his authority to implement cybersecurity protections for our country through an Executive Order.

To help me understand your company's views on cybersecurity, I ask that you provide responses to the following questions by Friday, October 19, 2012.

1. Has your company adopted a set of best practices to address its own cybersecurity needs?
2. If so, how were these cybersecurity practices developed?
3. Were they developed by the company solely, or were they developed outside the company? If developed outside the company, please list the institution, association, or entity that developed them.

# Cyber Risks – DoD Contracts

- NDAA § 941
- - “cleared defense contractors”
- “Rapid Reporting”
- “technique or method use in such penetration”
- “sample of malicious software”
- “summary of information . . . potentially compromised”
- DoD “Access”
- DoD access to contractor network & data for forensics analysis
- Limited purpose & trade secrets

## NATIONAL DEFENSE AUTHORIZATION ACT FOR FISCAL YEAR 2013

### SEC. 941. REPORTS TO DEPARTMENT OF DEFENSE ON PENETRATIONS OF NETWORKS AND INFORMATION SYSTEMS OF CERTAIN CONTRACTORS.

(a) PROCEDURES FOR REPORTING PENETRATIONS.—The Secretary of Defense shall establish procedures that require each cleared defense contractor to report to a component of the Department of Defense designated by the Secretary for purposes of such procedures when a network or information system of such contractor that meets the criteria established pursuant to subsection (b) is successfully penetrated.

#### (b) NETWORKS AND INFORMATION SYSTEMS SUBJECT TO REPORTING.—

(1) RAPID REPORTING.—The procedures established pursuant to subsection (a) shall require each cleared defense contractor to rapidly report to a component of the Department of Defense designated pursuant to subsection (a) of each successful penetration of the network or information systems of such contractor that meet the criteria established pursuant to subsection (b). Each such report shall include the following:

(A) A description of the technique or method used in such penetration.

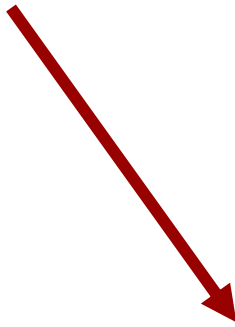
(B) A sample of the malicious software, if discovered and isolated by the contractor, involved in such penetration.

(C) A summary of information created by or for the Department in connection with any Department program that has been potentially compromised due to such penetration.

(2) ACCESS TO EQUIPMENT AND INFORMATION BY DEPARTMENT OF DEFENSE PERSONNEL.—The procedures established pursuant to subsection (a) shall—

# Cyber Risks – Executive Order

- Information Sharing
- → Should you be sharing?
- Yes?
- Critical for identifying threats
- Essential tool for cybersecurity
- No? -- Safe Harbors?
- Investigation due to reporting?
- Lawsuit triggered by sharing?
- Antitrust issue for B-2-B sharing?



- Executive Order

The White House

Office of the Press Secretary

---

For Immediate Release

February 12, 2013

## Executive Order -- Improving Critical Infrastructure Cybersecurity

Sec. 4. Cybersecurity Information Sharing. (a) It is the policy of the United States Government to increase the volume, timeliness, and quality of cyber threat information shared with U.S. private sector entities so that these entities may better protect and defend themselves against cyber threats. Within 120 days of the date of this order, the Attorney General, the Secretary of Homeland Security (the "Secretary"), and the Director of National Intelligence shall each issue instructions consistent with their authorities and with the requirements of section 12(c) of this order to ensure the timely production of unclassified reports of cyber threats to the U.S. homeland that identify a specific targeted entity. The instructions shall address the need to protect intelligence and law enforcement sources, methods, operations, and investigations.

# Cyber Risks – Info Sharing

- Sharing Data with Feds
- What do you say when the Feds come knocking?
  - - Authority to share data?
  - - Potential 3rd party liability?
  - - Privacy issues?
- Potential Exposure
  - - Attorney-client privilege?
  - - FOIA protection?
  - - Use for other investigations?
- 
- \$50 Billion Lawsuit
- “One lawsuit alone, filed May 12 by a purported national class of Verizon customers, seeks \$50 billion in damages.”
- [“Court Will Decide State Secrets Issues First in NSA Phone Surveillance Class Action Suit,” Privacy Law Watch, June 9, 2006]






# Cyber Risks – FCA Actions

- Cyber Fraud Risks
- - What did you tell the Federal agency?
- Failed Cybersecurity
- → False Claims Act suit
- “PLASTILAM, INC. failed to take sufficient steps to safeguard confidential data, including the names and Social Security numbers of over 100 Medicare beneficiaries. The investigation revealed that a number of misprinted beneficiary cards were discarded, whole, in an unsecured dumpster.”



 The United States Attorney's Office  
**District of Massachusetts**

FOR IMMEDIATE RELEASE  
JUNE 7, 2010  
WWW.USDOJ.GOV/USAO/MA  
E-MAIL: USAMA.MEDIA@USDOJ.GOV

SALEM PRINTING BUSINESS TO PAY \$25,000 FOR IMPROPER DATA SECURITY PRACTICES AND DISPOSAL OF MEDICARE BENEFICIARY CARDS

BOSTON, Mass. - The United States has reached a settlement with a Salem printing business in connection with potential civil penalty claims under the False Claims Act. United States Attorney Carmen M. Ortiz and J. Anthony Ogden, Inspector General of the United States Government Printing Office (GPO-OIG), announced today that PLASTILAM, INC., a printing business located in Salem, Mass., has reached a settlement with the Government, in connection with potential civil penalty claims under the False Claims Act, investigated by GPO-OIG and the U.S. Attorney's Office.

Based upon facts developed in the course of the investigation, the United States contended that between August 2007 and August 2008, while working on a GPO contract to produce plastic Medicare beneficiary cards, PLASTILAM, INC. failed to take sufficient steps to safeguard confidential data, including the names and Social Security numbers of over 100 Medicare beneficiaries. The investigation revealed that a number of misprinted beneficiary cards were discarded, whole, in an unsecured dumpster. These cards were later scattered around a local park by area children before being recovered by local police.

PLASTILAM, INC. has agreed to pay \$25,000 in settlement of the United States' penalty claims, without admitting wrongdoing or liability. Based upon the Government's investigation, it does not appear that any of the improperly safeguarded information was released deliberately, nor does it appear that any of the data was misused or stolen.

"We are committed to protecting the public by holding federal contractors who handle sensitive personal data, to the highest standards," said U.S. Attorney Ortiz. "Contractors who work with sensitive data must exercise vigilance in handling these materials. They must understand that even those data breaches are not due to deliberate misconduct, will be swiftly investigated and met with appropriate consequences."

Inspector General Ogden said, "The GPO OIG takes seriously allegations of improper conduct by GPO contractors, especially those responsible for the handling and protection of sensitive information, such as citizens' personally identifiable information (PII). I applaud the efforts of our investigators and the Department of Justice in bringing this matter to a meaningful resolution. While this is just one in a series of contract investigations our office is pursuing, this settlement should send a message that the breach of data security requirements and the compromise of PII will not be tolerated, and that we will hold accountable those administering and performing contracts for GPO."

The investigation leading to the settlement was conducted by the Office of the Inspector General of the U.S. Government Printing Office. It was prosecuted by Assistant U.S. Attorney Zachary A. Cunha of Ortiz's Civil Division.

# Questions?

David Bodenheimer

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"Securing cyberspace is one of the most important and urgent challenges of our time."

Senator Jay Rockefeller, Chairman of the Senate Commerce, Science and Transportation Committee

May 2011

# CF Disclosure Guidance: Topic No. 2

- Corporation Finance issues guidance October 13, 2011
- Deliberate attacks or unintentional events
- Theft of financial assets, intellectual property, or other sensitive information belonging to registrants

# CF Disclosure Guidance: Topic No. 2

- Remediation costs
- Increased cybersecurity protection costs
- Lost revenues
- Litigation
- Reputational damage adversely affecting customer or investor confidence

# CF Disclosure Guidance: Topic No. 2

- Material risks
- Cyber incidents
- Cyber incidents that may be undetected
- Insurance coverage

# SEC – Big 6

- Risk factors
- MD&A
- Description of business
- Legal proceedings
- Financial Statement disclosures
- Disclosure Controls & Procedures

# Evolution of Disclosure

- Facebook
- Comment Letters
  - Disclose specific cybersecurity breaches
  - Cybersecurity risks should stand alone
  - All material breaches should be disclosed
- Recent Form 10-K Disclosures

# Why Do Shareholders Care?

- Key current issue
- Costs
- Company value
- Litigation

# Board of Directors

- The Tone is set at the Top
- Risk Management
- Insurance
- Business Judgment Rule & Fiduciary Duties
- Officers



# Cyber Threats and Due Diligence

- Increased focus in transactions
- Understanding the risks
- Key component of company value

# Conclusions

- Key business issue
- SEC focus
- Costs
- Liability
- Best practices flowing down to private companies

# Questions?

Bryan Brewer

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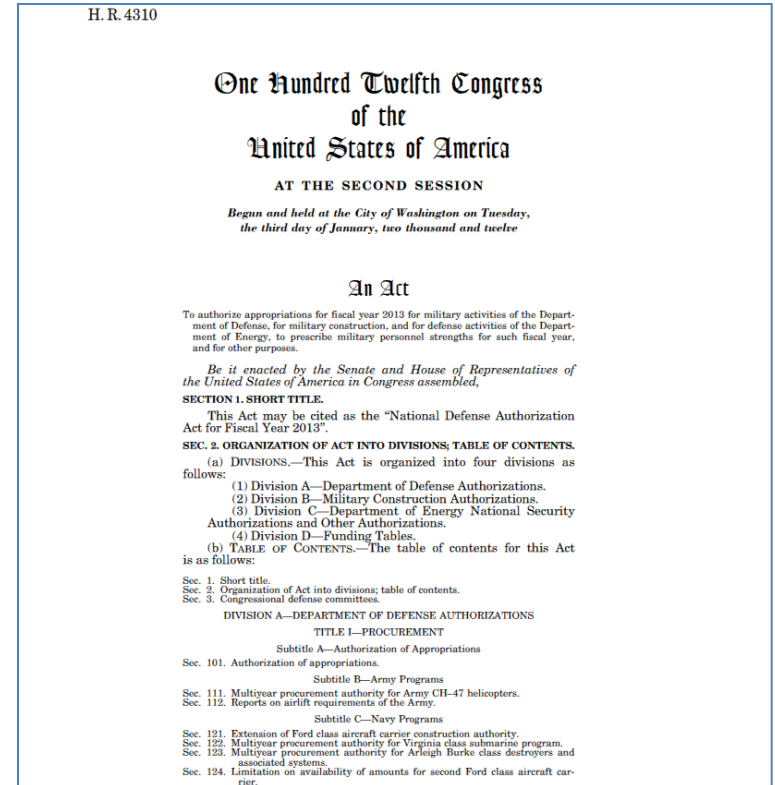
[bbrewer@crowell.com](mailto:bbrewer@crowell.com)

# Managing the Cyber Threat Crisis New Rules, Regulations and Solicitations

Gordon Griffin

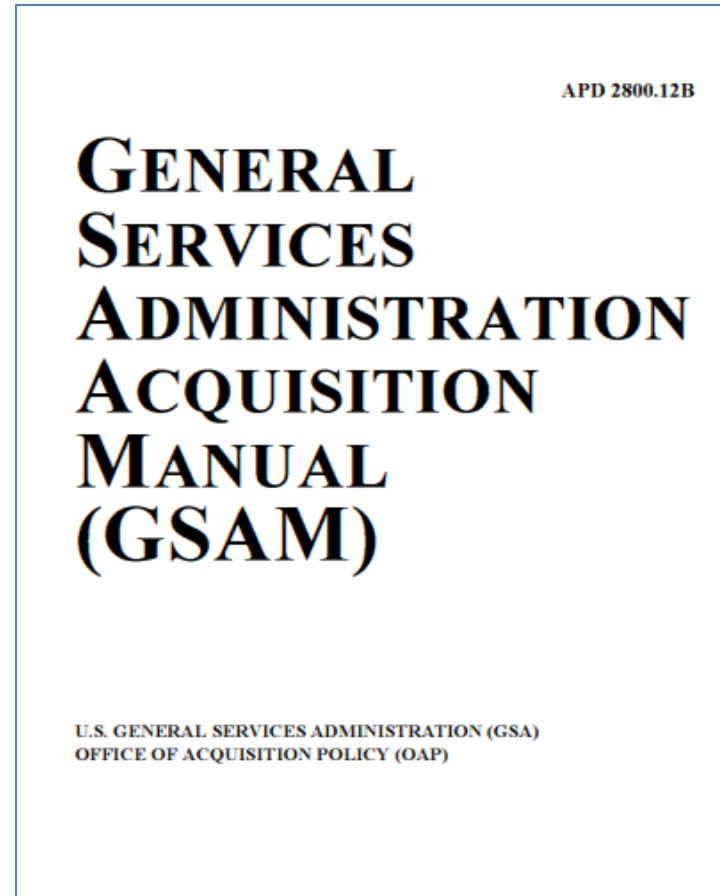
# Audits

- “[DOD regulations] shall include mechanisms for Department of Defense personnel to, upon request, obtain access to equipment or information of a cleared defense contractor necessary to conduct forensic analysis in addition to any analysis conducted by such contractor.”



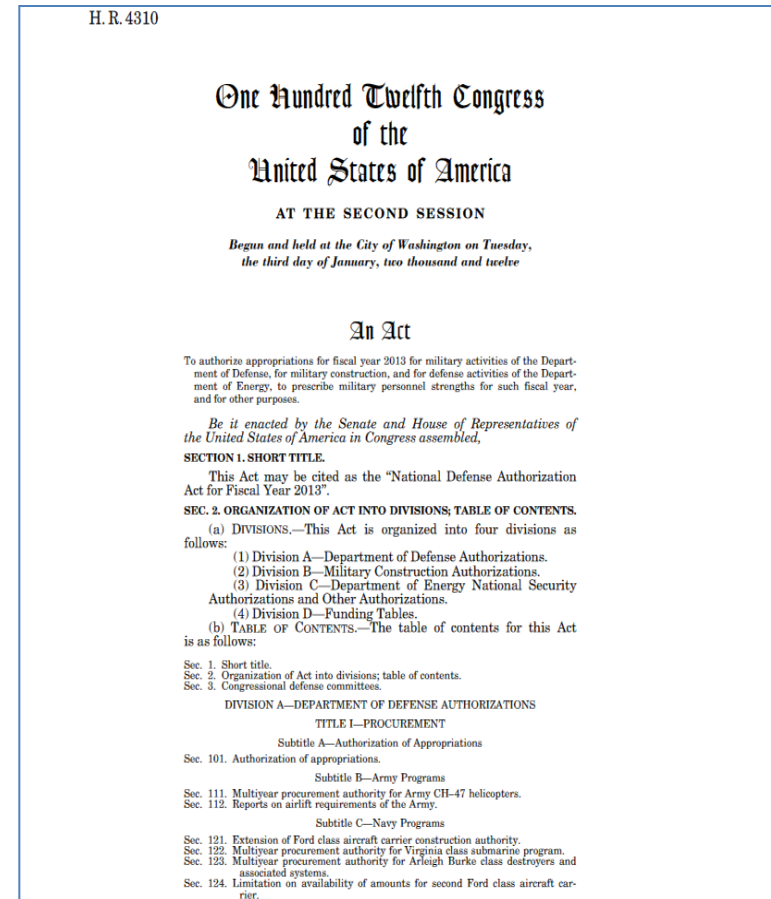
# Audits - Continued

- “The Contractor shall afford GSA access to the Contractor’s and subcontractors’ facilities, installations, operations, documentation, databases, IT systems and devices, and personnel used in performance of the contract, regardless of the location. Access shall be provided to the extent required, in GSA’s judgment, to conduct an inspection, evaluation, investigation or audit, including vulnerability testing to safeguard against threats and hazards to the integrity, availability and confidentiality of GSA data or to the function of information technology systems operated on behalf of GSA, and to preserve evidence of computer crime.”



# Breach Notification

- “The Secretary of Defense shall establish procedures that require each cleared defense contractor to report to a component of the Department of Defense designated by the Secretary for purposes of such procedures when a network or information system of such contractor that meets the criteria established pursuant to subsection (b) is successfully penetrated.”



# Continuing Resolution – Supply Chain

- Sec. 516. (a) None of the funds appropriated or otherwise made available under this Act may be used by the Departments of Commerce and Justice, the National Aeronautics and Space Administration, or the National Science Foundation to acquire an information technology system unless the head of the entity involved, in consultation with the Federal Bureau of Investigation or other appropriate Federal entity, has made an assessment of any associated risk of cyber-espionage or sabotage associated with the acquisition of such system, including any risk associated with such system being produced, manufactured or assembled by one or more entities that are owned, directed or subsidized by the People's Republic of China.

160

One Hundred Thirteenth Congress  
of the  
United States of America

AT THE FIRST SESSION

*Began and held at the City of Washington on Thursday,  
the third day of January, two thousand and thirteen*

An Act

Making consolidated appropriations and further continuing appropriations for the  
fiscal year ending September 30, 2013, and for other purposes.

*Be it enacted by the Senate and House of Representatives of  
the United States of America in Congress assembled,*

SHORT TITLE

SECTION 1. This Act may be cited as the "Consolidated and  
Further Continuing Appropriations Act, 2013".

TABLE OF CONTENTS

SEC. 2. The table of contents of this Act is as follows:

Sec. 1. Short title.  
Sec. 2. Table of contents.  
Sec. 3. References.  
Sec. 4. Explanatory statement.  
Sec. 5. Availability of funds.

DIVISION A—AGRICULTURE, RURAL DEVELOPMENT, FOOD AND DRUG  
ADMINISTRATION, AND RELATED AGENCIES APPROPRIATIONS ACT, 2013

Title I—Agricultural Programs  
Title II—Conservation Programs  
Title III—Rural Development Programs  
Title IV—Domestic Food Programs  
Title V—Foreign Assistance and Related Programs  
Title VI—Related Agency and Food and Drug Administration  
Title VII—General provisions

DIVISION B—COMMERCE, JUSTICE, SCIENCE, AND RELATED AGENCIES  
APPROPRIATIONS ACT, 2013

Title I—Department of Commerce  
Title II—Department of Justice  
Title III—Science  
Title IV—Related agencies  
Title V—General provisions

DIVISION C—DEPARTMENT OF DEFENSE APPROPRIATIONS ACT, 2013

Title I—Military Personnel  
Title II—Operation and Maintenance  
Title III—Procurement  
Title IV—Research, Development, Test and Evaluation  
Title V—Revolving and Management Funds  
Title VI—Other Department of Defense Programs  
Title VII—Related agencies  
Title VIII—General provisions  
Title IX—Overseas contingency operations

DIVISION D—DEPARTMENT OF HOMELAND SECURITY APPROPRIATIONS  
ACT, 2013

Title I—Departmental management and operations



# HIPAA Regulations

- January 25, 2013, HIPAA Rule makes several changes:
  - Breach Notification Rule
  - Security Rule
  - Business Associate Liability

Violation category—Section 1176(a)(1)	Each violation	All such violations of an identical provision in a calendar year
(A) Did Not Know .....	\$100–\$50,000	\$1,500,000
(B) Reasonable Cause .....	1,000–50,000	1,500,000
(C)(i) Willful Neglect-Corrected .....	10,000–50,000	1,500,000
(C)(ii) Willful Neglect-Not Corrected .....	50,000	1,500,000

# Liquidated Damages & Penalty Provisions

- HHS Solicitation:
  - “In the event of a breach, the contractor shall be liable for \$500 per effected user. The contractor shall be liable for the Government’s costs to notify and/or remediate the breach of private personal data with FOH customers. Based on the nature of the breach, the Government shall define a remediation plan, and the contract shall support the defined actions. In addition to restitution for the labor efforts to coordinate the notification, this remediation shall include the cost of providing credit protection to all effected people.”

# Solicitations

- CMS – State Based Exchanges
  - “The Business Associate shall report any violation in use or disclosure involving PHI or any security incident to CMS within one (1) hour of discovery in accordance with the ‘CMS Guide for the Incident Reporting Process.’”

# Solicitations – Continued

- GSA – Occupational Health Review
  - “The Contractor shall comply with GSA Order CIO 2100.1 GSA Information Technology (IT) Security Policy and GSA Order ADM 9732.1D Suitability and Personnel Security. GSA separates the risk levels for personnel working on Federal computer systems into three categories: Low Risk, Moderate Risk, and High Risk. Criteria for determining which risk level a particular contract employee falls into are shown in Figure A-1 of GSA Order ADM 9732.1D.”

# Solicitations – Continued

- Department of Commerce – Document Destruction
  - “The contractor shall afford DOC, including the Office of Inspector General, access to the contractor's and subcontractor's facilities, installations, operations, documentation, databases, and personnel used in performance of the contract. Access shall be provided to the extent required to carry out a program of IT inspection, investigation, and audit to safeguard against threats and hazards to the integrity, availability, and confidentiality of DOC data or to the function of computer systems operated on behalf of DOC, and to preserve evidence of computer crime.”

# Solicitations – Continued

- HHS – Rx Database
  - “This contract requires the Contractor to develop, host, and/or maintain a Federal information system at the Contractor’s or any subcontractors’ facility. The Contractor shall submit an annual information security assessment using NIST SP 800-53, Recommended Security Controls for Federal Information Systems. The assessments shall be due annually within 30 days after the anniversary date of the contract, with the final assessment due at contract completion.”

# Solicitations – Continued

- Department of Commerce – NIST Enterprise
  - “Contract employees may be barred from working on the premises of a facility for any of the following:
    - (3) Improper Conduct once performing on the contract, including criminal, infamous, dishonest, immoral, or notoriously disgraceful conduct or other conduct prejudicial to the Government regardless of whether the conduct directly related to the contract.”

# Questions?

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# Bid Protests: Trends and Developments

Tom Humphrey  
Dan Forman  
Derek Mullins  
Olivia Lynch

# GAO Protest Statistics

<b>Fiscal Year</b>	<b>2012</b>	<b>2011</b>	<b>2010</b>	<b>2009</b>	<b>2008</b>	<b>2007</b>	<b>2006</b>
Cases Filed	2,475	2,353	2,299	1989	1652	1411	1326
Cases Closed	2,495	2,292	2,226	1920	1582	1394	1275
Merits Decision	570	417	441	315	291	335	251
Sustains	106	67	82	57	60	91	72
Sustain Rate	18.6%	16%	19%	18%	21%	27%	29%
Effectiveness Rate (reported)	42%	42%	42%	45%	42%	38%	39%
ADR (cases used)	106	140	159	149	78	62	91
ADR Success Rate	80%	82%	80%	93%	78%	85%	96%
Hearings	6.17% (56)	8% (46)	10% (61)	12% (65)	6% (32)	8% (41)	11% (51)

# COFC Protest Statistics

Calendar Year	2012	2011	2010	2009	2008	2007	2006
Protests Filed	99	98	88	74	79	81	64
<i>Pre-award</i>	42	29	19	22	23	18	9
<i>Post-award</i>	57	69	69	52	56	63	55
Protest Decisions	78	82	71	57	39	53	74
<i>Published</i>	66	73	64	50	38	50	55
<i>Un-published</i>	12	9	7	7	1	3	19

# Bid Protest Statistics

- Number of GAO protests filed continued at record levels, up 5% from last year
- GAO Sustain Rate inches up, but remains far below highs from 2006-2007
  - Effectiveness Rate remains constant
- Large increase in GAO decisions on the merits
  - Possible slowing of agency corrective actions?
- Minimal increase in COFC protests over past year
  - Percentage of pre-award protests has increased relative to post-award protests
- Potential effects of Sequestration on future statistics

# OCI

- Eroding Viability of OCI Protests
  - *AT&T Government Solutions*, B-407720, B-407720.2, Jan. 30, 2013, 2013 CPD ¶ 45
    - After finding during ADR that Agency failed to meaningfully consider impaired objectivity and unequal access OCIs, and 3 days before 100-day deadline, Agency issued OCI waiver and GAO dismissed as academic without further consideration.
  - *McTech Corp.*, B-406100, B-406100.2, Feb. 8, 2012, 2012 CPD ¶ 97
    - Citing COFC decision in *Turner Construction*, GAO finds that Agency can introduce post-hoc analysis to defend contemporaneous OCI conclusions.

# OCI (cont'd)

- But not yet a free pass for the Government
  - *NikSoft Sys. Corp.*, B-406179, Feb. 29, 2012, 2012 CPD ¶ 104
    - Agency moves to dismiss for lack of standing on ground that protester has an OCI problem. GAO rejects argument finding that Agency OCI argument not based on “hard facts.”

# OCI (cont'd)

- Timeliness of OCI Protests – Pre- or Post-Award?
  - *CRAssociates, Inc. v. United States*, 102 Fed. Cl. 698 (2012), aff'd per curiam, *CRAssociates, Inc. v. United States*, 475 F.App'x 341 (Fed. Cir. 2012)
    - Dismissing as untimely post-award protest that awardee had unequal access OCI where Agency rejected protesters request during competition to amend Solicitation to resolve unfair advantage.
  - *Guident Technologies, Inc.*, B-405112.3, Jun. 4, 2012, 2012 CPD ¶ 166
    - Finding impaired objectivity OCI timely and distinguishing *CRAssociates* on basis that COFC case challenged fairness of ground rules whereas *Guident* was challenging award decision.

# Discussions

- Nature of Discussions
  - *Tipton Textile Rental, Inc.*, B-406372, May 9, 2012, 2012 CPD ¶ 156
    - Requests for additional information during phone calls, site visit, and follow-up emails constituted discussions and therefore had to be meaningful.
  - *Metropolitan Interpreters and Translators, Inc.*, B-403912.4, et al., May 31, 2011, 2012 CPD ¶ 130
    - Agency's discussions with, and receipt of a FPR from, one offeror as part of corrective action, without allowing other offerors the same opportunity, violated FAR requirement for a common cut-off date but did not prejudice protester.
  - *Booz Allen Hamilton, Inc.*, B-405993, B-405993.2, Jan. 19, 2012, 2012 CPD ¶ 30
    - DCAA's post-FPR exchanges with awardee during rate verification audits, during which the awardee provided additional cost data, constituted clarifications, not discussions. Therefore, Agency did not conduct unequal discussions. But see *ERIE Strayer Co.*, B-406131, Feb. 21, 2012, 2012 CPD ¶ 101.



# Discussions

- Award Without Discussions
  - *ITT Systems Corp.*, B-405865, B-405865.2, Jan. 6, 2012, 2012 CPD ¶ 44
    - GAO confirms that it generally will not review an agency's decision not to hold discussions.

# Challenges to GAO Sustains and to Agency Corrective Actions

- Jurisdiction
  - *Systems Application & Techs., Inc. v United States*, 691 F.3d 1374 (Fed. Cir. 2012)
    - Upholding COFC’s exercise of jurisdiction over an awardee’s protest of a proposed corrective action to terminate the award, amend the solicitation, and recompet the contract, under the Tucker Act. Rejecting the Government’s argument that the protest by the original awardee was not ripe.
- GAO Sustains
  - Reviewed based on agency decision to follow the recommendation
  - Standard is whether the GAO decision is irrational
  - *CBY Design Builders v. United States*, 105 Fed. Cl. 303 (2012)
    - Lengthy discussion of nature of COFC review
    - Found one aspect of GAO decision irrational, but upheld the corrective action
- Agency Corrective Actions
  - *CBY Design Builders v. United States*, 105 Fed. Cl. 303 (2012)
    - Allowing Agency to take broader-than-necessary corrective action. Also upholding Agency’s decision to address another issue, which had been raised at GAO but not sustained.
  - *Sierra Nevada Corp. v. United States*, No. 12-375C, 2012 WL 5378163 (Fed. Cl. Nov. 1, 2012)
    - Rejecting the narrow standard for reviewing the propriety of corrective action as targeted to the identified defect (propounded in *Sheridan Corp. v. United States*). Instead, examined the Agency’s corrective action under a “reasonable in all circumstances” standard.

# Past Performance

- “Too Close at Hand” Doctrine
  - *FN Manufacturing LLC, B-407936 et al.*, Apr. 19, 2013, 2013 WL 1802013
    - GAO refuses to extend doctrine to information that an offeror failed to include in its proposal

# Questions?

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# Suspension & Debarment Mitigating the Increased Risk

Angela Styles

Peter Eyre

Richard Arnholt

James Peyster

# Introduction

- Latest Statistics and Legislative Developments
- Blossoming Causes
- Best Practices
- Mandatory Disclosure

# Continued Increase in S/D Activity

	FY 2010	FY 2011	FY 2012
<b><u>Air Force</u></b>			
Suspensions	83	148	83
Proposed Debarments	159	139	401
Debarments	111	80	266
<b><u>Army</u></b>			
Suspensions	133	112	195
Proposed Debarments	170	235	284
Debarments	125	179	186
<b><u>Navy</u></b>			
Suspensions	25	24	47
Proposed Debarments	78	80	152
Debarments	38	92	146

# Continued Increase in S/D Activity

- More show cause letters
- More referrals
  - Focus on coordination of remedies, automatic/mandatory referrals, and parallel proceedings
- More actions focused on individuals
- More active civilian agency S/D programs
  - DHS, Education, Transportation, VA



# Legislative Developments

- Recent mandatory exclusions:
  - VA debarment for firms that misrepresent status for purpose of VA's Veterans First Contracting program
  - Generally prohibit use of funds to enter contracts or other agreements with corporations that have unpaid federal tax liability, or that have been convicted of a felony under federal law within the preceding 24 months, unless the agency has determined that such action is not “necessary to protect the interests of the Government”
- Renewed focus on enforcement of existing mandatory exclusions?

# Legislative Developments

- SUSPEND Act
  - On February 7, 2013, House Oversight Committee released discussion draft of legislation that would consolidate more than forty civilian agency suspension and debarment offices
  - Would create centralized "Board of Civilian Suspension and Debarment" in GSA on October 1, 2014
  - Focus on expedited processes and public availability of proceedings

# The Expanding and Diversifying World of Suspension and Debarment

- One size does not fit all; little coordination between agencies leads to differing goals and philosophies
- Different agencies employing significantly different approaches to S/D process
  - Amount of focus on individuals vs. companies
  - Frequency of use of show cause letters vs. direct notices of proposed S/D
  - Different views on acceptable remedial measures

# S/D Officials Moving into New Areas of Law

- S/D Process no longer reserved for criminal convictions, FCA violations, and clear cases of fraud
- SDOs becoming bolder about expanding the interpretation of § 9.406-2(a)(5):
  - “(5) Commission of any other offense indicating a **lack of business integrity or business honesty** that seriously and directly affects the present responsibility of a Government contractor or subcontractor.”
- **This is where it starts to get scary...**

# Case Study: Suspension of MCR Federal LLC

- Background
  - MCR was a participant in an Air Force Procurement
  - Contracting Officer inadvertently sent MCR's point of contact an e-mail with source selection sensitive attachments relating to the evaluation of a competitor and information about that competitor's proposal
  - MCR point-of-contact forwarded e-mail to MCR employees without realizing what it was
  - Air Force attempted to recall the e-mail 10 minutes later
  - MCR took two days before it fully quarantined the e-mail
  - Recipients of the e-mail continued to work on MCR's proposal revisions during this two-day period (and after)

# Case Study: Suspension of MCR Federal LLC

- Air Force Suspension and Debarment Official (SDO) concluded that MCR's conduct was potentially in violation of the Procurement Integrity Act
- The Procurement Integrity Act ("PIA"); 41 U.S.C §§ 2101 et seq. prohibits a contractor from obtaining procurement information:
  - “Except as provided by law, a person shall not knowingly obtain contractor bid or proposal information or source selection information before the award of a Federal agency procurement contract to which the information relates.” (§ 2101(b))

# Case Study: Suspension of MCR Federal LLC

- Interpretation of PIA conveyed by Air Force has been rejected by the Court of Federal Claims in the bid protest context
- *The GEO Group, Inc v. U.S.*, 100 Fed.Cl. 223 (2011) narrows the definition of “person” in delineating the scope of the PIA’s ban on a obtaining competitively sensitive information:
  - “Read in context, however, [§ 2102(b)] appears to apply only to current or former officials of the United States or persons who are acting or have acted on such an individual's behalf.”
  - The limitation “derives support from the legislative history of the statute, which refers to the provision in question as applying to “present or former federal employees.”

# Case Study: Suspension of MCR Federal LLC

- *Jacobs Technology Inc. v. United States*, 100 Fed.Cl. 198 (2011) further limits the scope of § 2012(b) to affirmative acts:
  - “[A] possible PIA violation requires the offeror to have knowingly obtained information that the agency intended to use in evaluating proposals on the new procurement. Thus, a PIA violation essentially requires an affirmative act by the offeror to obtain source selection information; simply having knowledge is not enough to support a possible PIA violation. A PIA violation also appears to be founded on improper or unlawful conduct.”



# Case Study: Suspension of MCR Federal LLC

- Bid Protest Forums:
  - Reads-in a narrowing provision to find that § 2102(b) only applies to current and former government employees
  - Finds that only “affirmative acts” and “unlawful conduct” can lead to a PIA violation
- Suspension and Debarment Officials:
  - Applies PIA prohibition against contractor employees who are not former government officials or work with former officials
  - Reads-in expansive, implicit prohibition on “use” of source selection information even when not “knowingly obtained”

# Other Areas of Expansion

- Individuals being suspended for “having reason to know” that other employees were engaging in improper conduct, but not reporting that conduct
- SDOs have stated intent to use S/D process in response to “dodgy litigation tactics” in contract disputes with the Government
- SDOs looking reviewing contractors when contracts get terminated for default due to poor performance

# Best Practices – Minimizing S/D Risk

- Robust compliance program
  - Scaled to size of business
    - internal reporting mechanism
    - ethics officer independence
    - tone from the top
    - gov't contract/grant policy
    - training
- Identify agency with responsibility
  - Lead agency - dominant financial interest?
- Early engagement with SDO

# Best Practices – Minimizing S/D Risk

- Bad things happen – respond appropriately
- S/D mitigating factors are a guide
  - Effective standards of conduct and internal control systems
  - Timely disclosed
  - Fully investigated
  - Full cooperation
  - Paid fines, full restitution

# Best Practices – Minimizing S/D Risk

- Mitigating factors (continued)
  - Appropriate disciplinary actions
  - Remedial measures
  - Revised review & control procedures and ethics training programs
  - Adequate time to eliminate circumstances that led to exclusion
  - Management understands seriousness of misconduct; implemented programs to prevent recurrence

# Best Practices – Preparing for S/D

- Businesses dependent on government contracting/grants should be ready
  - Delay may be fatal
- Emergency toolkit
  - Gather compliance materials
  - Identify company official to make present responsibility presentation
  - Identify counsel

# Best Practices – Responding to SDOs

- Know the process
  - Varies by agency
- Don't litigate
  - Identify common ground
  - Compliant, ethical procurement system
- Don't argue the facts unless clear error
- Use mitigating factors to frame response
- Know SDO's expectation for administrative agreements
- [“Only the penitent man will pass”](#)

# Mandatory Disclosure

- Know agency process/practice (DoD vs. GSA)
  - DoD – immediately informs SDO
  - GSA – informs SDO after investigation
- Proactive engagement of SDO?
- Lead Agency
- Drafting Disclosure



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# False Claims Act Developments

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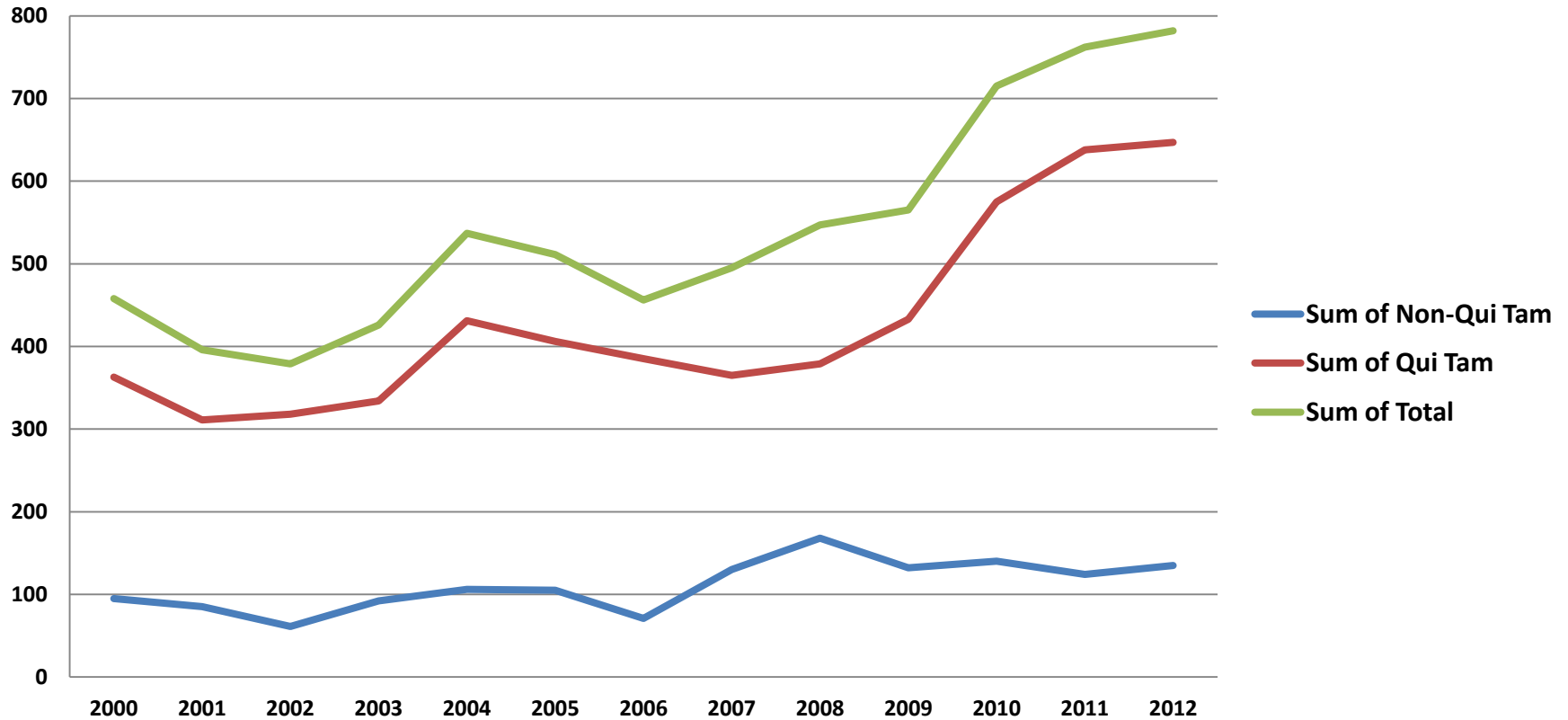
# Agenda

- Recent FCA and *Qui Tam* Enforcement Statistics
- Recent FCA-Related Regulatory/Legislative Developments
- Recent FCA Enforcement Trends
- Recent Cases and Settlements and Their Impact on Compliance and Enforcement

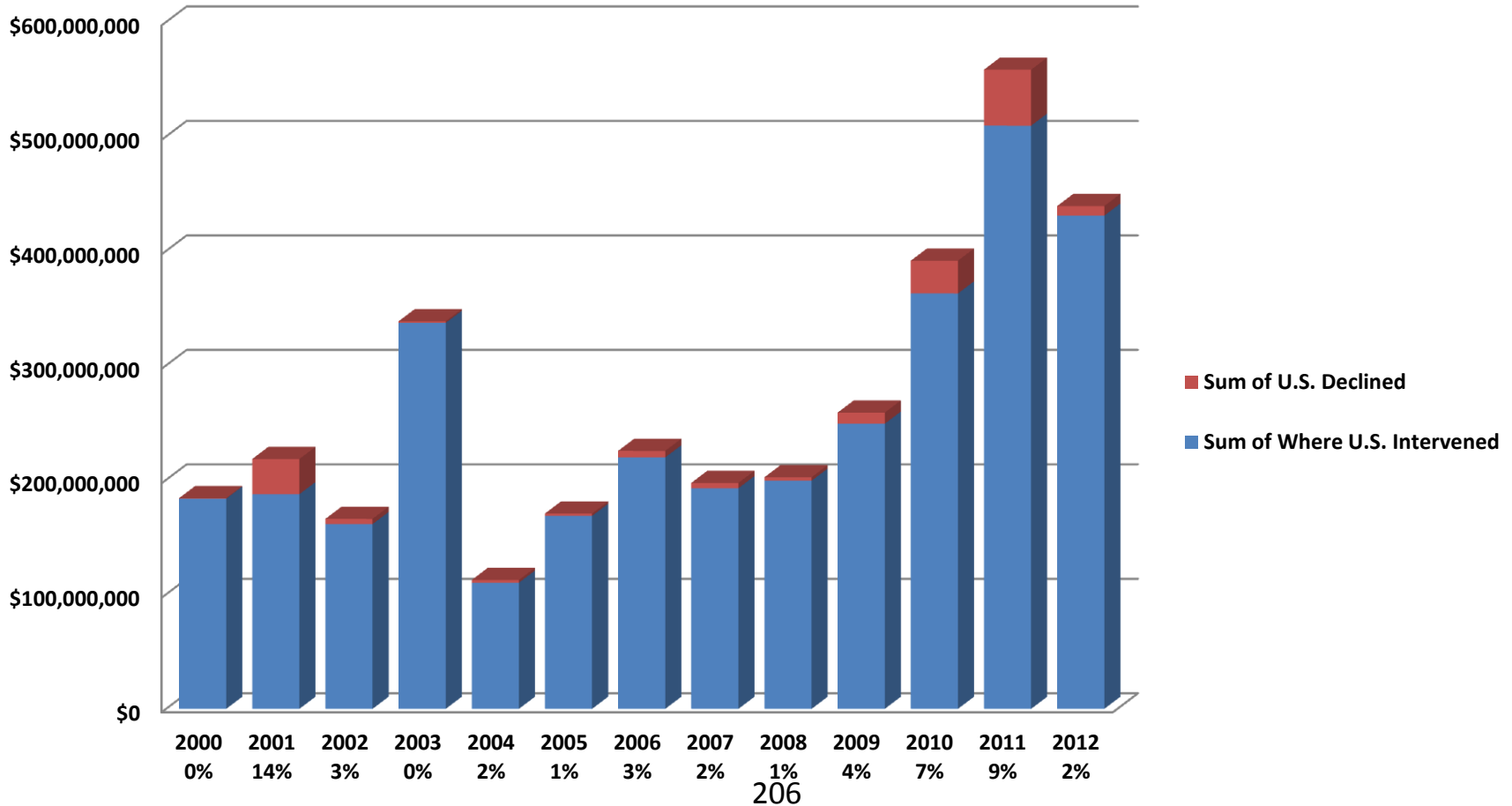
# FCA Statistics: FY 2012

	FY 2012	Total since 1986
New matters	782	12,913
<i>Qui tam</i>	647	8,489
Recoveries	\$4,959,333,598	\$35,192,303,318
Relators' share	\$439,220,244	\$3,887,909,070

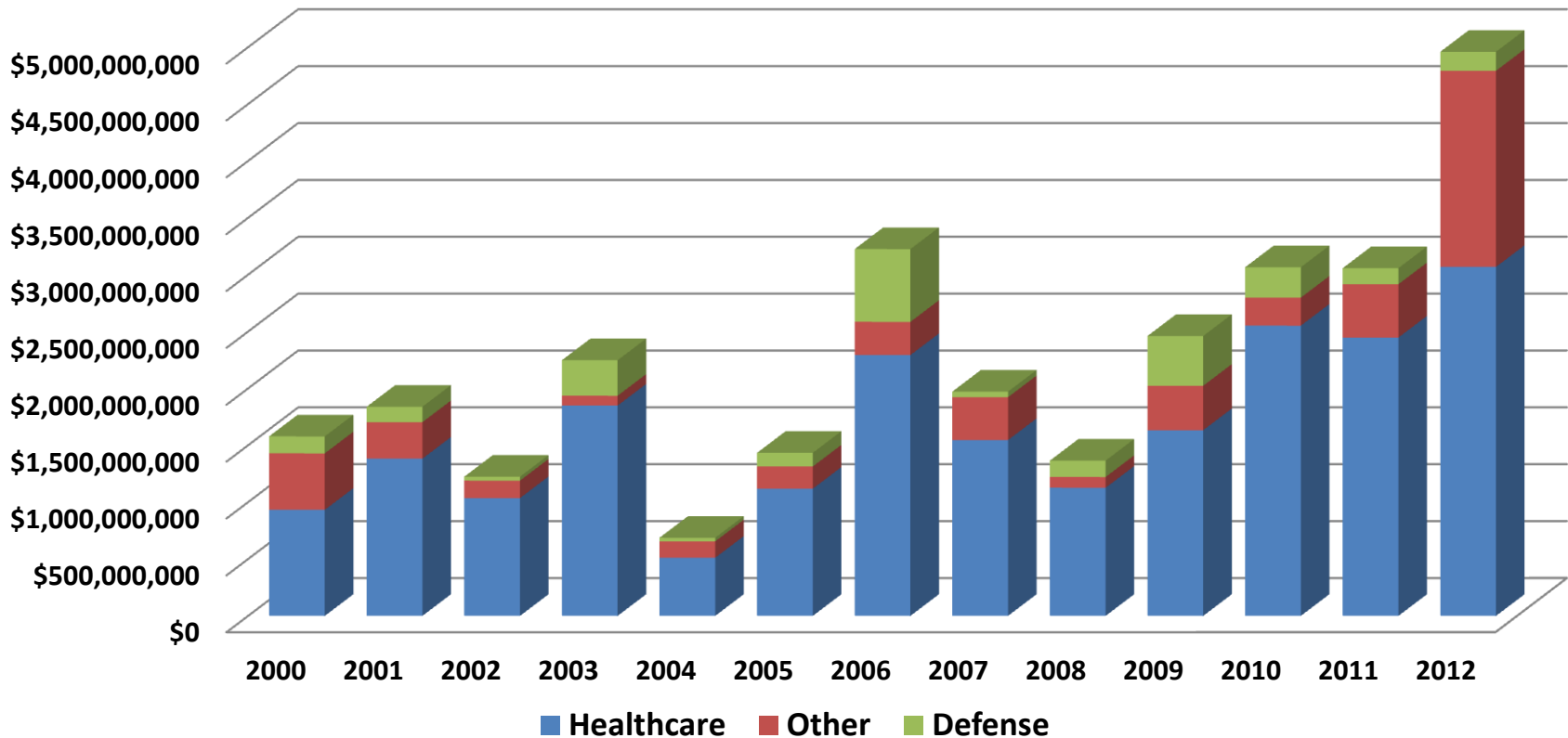
# New Matter Filings 2000-2012



# Relators' Share of Awards 2000-2012



# Total Awards by Industry 2000-2012



# Recent FCA Regulatory/Legislative Developments



# U.S. Supreme Court Upholds ACA

## *2010 Healthcare Act amendments to FCA remain law*

- Relaxation of public disclosure bar
- 60-day deadline from discovery for returning Medicare/Medicaid overpayments
- Violations of Medicare/Medicaid Anti-Kickback statutes constitute false claims for FCA purposes



# FCA-Related Legislation: Expired in Congress

- Fighting Fraud to Protect Taxpayers Act of 2011 (S. 890)
  - Senators Leahy and Grassley
  - Overview of FCA-related aspect of bill – would have amended FCA to:
    - provide that the cost of prosecutions under the FCA be credited to the appropriations accounts of the executive agency from which the funds used for the costs were paid
    - require Attorney General to submit to House and Senate Judiciary committees report of all FCA settlements
  - Expired at the end of the 112<sup>th</sup> Congress

## Updates to State FCA Laws

- Background: 2005 Federal Deficit Reduction Act (DRA)
  - incentivizes states to enact statutes as stringent as federal FCA
  - Qualified states may collect additional 10% of any recovery through state action
- HHS OIG issued 2-year grace period for states to conform to federal FCA amendments (FERA, PPACA, Dodd-Frank)
- March 2013: new OIG guidelines for evaluating state statutes

# Updates to State FCA Laws (cont'd)

- 29 States and District of Columbia have FCA laws
- Amendments to Strengthen State FCA (last year):
  - CA passed bill that conforms its FCA to the federal FCA
  - Hawaii, Massachusetts, Georgia, and Tennessee...
- Pending Legislation:
  - Alabama, Arizona, Michigan ...(among others)
- City FCA Laws: New York, Chicago and Philadelphia!
  - NYC FCA made permanent and amended to resemble NY state FCA

# States More Aggressive in Enforcing FCA

- NY State brings groundbreaking tax fraud FCA lawsuit against Sprint for over \$300 million
  - Allegations of failure to collect and pay sales tax
- NY State Attorney General plans to bring more and bigger FCA suits against corporate defendants for tax evasion



# ACA's Changes to the FCA

- Violation of the Anti-Kickback Statute (“AKS”) can be the basis for FCA liability
- Changes the intent/knowledge requirements under the AKS. Now, a “actual knowledge or specific intent to commit a violation of this section” not required.
- Affects the *Hanlester* defense, which interpreted the AKS to require proof the defendant (1) had specific knowledge of the law, and (2) had specific intent to disobey the law.
  - *Hanlester Network v. Shalala* (9<sup>th</sup> Cir. 1995)

# ACA's Changes to the FCA

- Creates *Per Se* FCA Violation for Failure to Report and Return Overpayments:
  - Any overpayment retained by a person after the deadline for reporting and returning the overpayment under paragraph (2) is an obligation (as defined in section 3729(b)(3) of title 31, United States Code) for purposes of section 3729 of such title.
- Does not add a new liability provision to the FCA, but stipulates with only limited detail the procedural steps and time period to report and return an identified overpayment obligation in order to avoid potential FCA liability.

# ACA's Changes to the FCA

- ACA provides a 60-day deadline for **reporting and returning** overpayments.
- The deadline is the later of:
  - (A) the date which is 60 days after the date on which the overpayment was identified;  
or
  - (B) the date any corresponding cost report is due, if applicable.
- Effective for overpayments “identified” as of the March 23, 2010 PPACA enactment date



# Proposed CMS Rule on Reporting and Refunding Overpayments

- Proposed rule contains 60-day report and return requirement with a 10-year “lookback”
- Strong industry opposition to proposed rule, including:
  - Lack of clarity as to what triggers 60-day period
  - 10-year lookback longer than the 6-year HIPAA record retention provision
- Comment period closed April 16, 2012; issuance of final rule is pending

# Recent FCA Enforcement Trends

# Enforcement Trends

- Expanded theories of liability and targeting of new industries
  - *E.g.*, Lance Armstrong case, mortgage cases, etc.
- Increase in “reckless disregard” cases
  - *E.g.*, *ATK Launch Systems (D. Utah)*
  - *E.g.*, *U.S. ex rel. Becker (N.D. Tex.)*
- Increase in non-employee relators
  - *E.g.*, competitors, government employees

# Recent Cases and Settlements and Their Impact on Compliance and Enforcement

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# FCA's Statute of Limitations Tolled Indefinitely?

- *U.S. ex rel. Carter v. Halliburton* (4<sup>th</sup> Cir. 2013) and *U.S. v. BNP Paribas SA* (S.D. Tex. 2012)
  - Fourth Circuit and S.D. Tex. are the latest courts to hold that the Wartime Suspension of Limitations Act tolls the civil FCA's statute of limitations when the United States is at war or Congress has enacted a specific authorization for the use of the Armed Forces (even if the contract at issue is not war-related).

# Ambiguous Requirements

- *U.S. ex rel. Williams v. Renal Care Group* (6<sup>th</sup> Cir. 2012)
  - Government intervenes in case against healthcare provider for interpreting ambiguous federal regulation in a way that maximizes its own profit.
  - Sixth Circuit rejects government's reckless disregard argument – defendant disclosed facts to government

## False Cost Estimates & Underbidding are Actionable

- *U.S. ex rel Hooper v. Lockheed Martin Corporation* (9<sup>th</sup> Cir. 2012)
  - 9<sup>th</sup> Circuit Relied on Logic of 1<sup>st</sup> and 4<sup>th</sup> Circuits
  - HELD: “[F]alse estimates, defined to include fraudulent underbidding in which the bid is not what the defendant actually intends to charge, can be a source of liability under the FCA, assuming that the other elements of an FCA claim are met.”

# False Cost Estimates & Underbidding are Actionable

## *U.S. ex rel Hooper v. Lockheed Martin Corporation (cont'd)*

- Issue - whether proposals on cost-reimbursement contract included cost estimates which Lockheed Martin knew were lower than the costs it expected to incur
  - District Court: no evidence of Lockheed Martin's state of mind in estimate choices and no suggestion of intent to submit unsupportable bids or other nefarious purpose
  - Summary judgment reversal based on testimony that one Lockheed Martin employee "was simply tasked [by management] to change the cost" estimate even though the change was not based on engineering judgment
  - Employee called the inputs to the bids "bad, bad guesses"
  - 9<sup>th</sup> Circuit did not consider why or how cost was changed
- No standard for determining how estimates will be evaluated
  - decision suggests that a cost estimate may be fraudulent if it is lower than what a contractor intends to charge



# Qui Tam Relators – Limitations and Expansions

- *U.S. ex rel. Little v. Shell Exploration & Prod. Co.* (5th Cir. 2012)
  - Federal auditors may have standing as qui tam relators
- *U.S. ex rel. Carter v. Halliburton* (4<sup>th</sup> Cir. 2013)
  - Interpreting first-to-file bar as requiring dismissal without prejudice to permit relator to bring new action if earlier related case is dismissed
- *U.S. ex rel. Beauchamp v. Academi* (E.D. Va. 2013)
  - Dismissing FCA claims under amended public disclosure bar and first-to-file bar
  - staying retaliation claims based on relators' agreements to arbitrate

# Damages – A Mixed Bag

- *U.S. ex rel. Feldman v. Von Gorp* (2d Cir. 2012)
  - government sought full contract value as damages in non-conforming goods/services case involving research training grant
  - Court rejects benefit-of-the-bargain calculation and awards full damages as matter of law on grounds that contract did not produce a tangible benefit to the government
- *U.S. v. Anchor Mortgage Corp.* (7<sup>th</sup> Cir. 2013)
  - Government’s “gross trebling” approach compared with “net trebling” calculus urged by defendant in FHA mortgage loan case where government sold the secured properties
  - Rejects DOJ’s interpretation of *U.S. v. Bornstein* and holds that net trebling approach is proper measure of government’s loss

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# Small Business: Enforcement Shakedown and Legislative Shakeup

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Bob Wagman  
Alexina Guiomar Jackson

# Agenda

- Significant expansion of mentor-protégé program
- New formulas for limitations on subcontracting
- Sources of oversight and enforcement
- Preview of proposed rules for small business size and status protests
- Questions?

# Mentor-Protégé: 8(a) Program

## Background (1)

- Mentor-Protégé (M-P) Program - Key Benefits:
- SBA's M-P Program as affiliation exception for JVs; large business can have shared responsibilities as prime contractor
- JV qualifies as small and 8(a) on set-asides and for subcontracts (can be used to meet subcontracting goals)
- Ability to form multiple JVs to exceed regulatory limit of 3 awards in 2-year period
- Mentor can have up to 40% equity interest in Protégé
- Assistance provided under M-P agreement is exempt from affiliation
- Eligibility requirements for Mentor and Protégé; currently Protégés limited to 8(a) contractors
- Mentors generally limited to 1 Protégé; prohibited from more than 3; multiple Protégés cannot be competitors
- Protégé benefits from true mentorship, increase awards due to JV combined capabilities

# Mentor-Protégé: 8(a) Program

## Background (2)

- SBA v. Other M-P Programs:
- Only SBA program provides exemption from affiliation for M-P joint venture
- Other agency-specific M-P programs with varying benefits; only exempt from affiliation for assistance provided between Mentor and Protégé if M-P program authorized by statute or SBA
- Differing approval process, benefits, eligibility, and reporting under other programs
- Most designed to operate when Protégé is acting as subcontractor to Mentor (DoD)
- Other types of benefits: subcontracting credit; reimbursement for costs of assistance; evaluation credit; awards and recognition

# Mentor-Protégé Program Expansion

- Section 1641 of FY13 NDAA authorizes expansion of SBA 8(a) M-P program to all SBs
- Expanded program similar to 8(a) program but may modify to extent necessary given types of SB protégés
- Agency M-P plans (except for DoD) no longer permitted unless minimum requirements satisfied
- Requires SBA approval of agency plans, based on
  - Finding that the plan assists protégé to compete for federal prime and subcontracts
  - Complies with regulations to be issued, including assurance that protégé is protected against mentors that may:
    - Adversely affect protégé size status; or
    - Provide disproportionate benefits to mentor over protégé



# Mentor-Protégé Program Expansion

- SBA must issue proposed regulations for M-P program within 270 days (subject to notice and comment)
- Agencies with M-P programs must submit conforming plans within 6 months of promulgation of new SBA rules
- Approved M-P agreements not impacted and may continue for duration of term of agreement

# Mentor-Protégé Program Expansion - Questions

- Limitations on number of protégés?
- What if protégé is certified in more than one category?
- Why does the new definition of a mentor eliminate non-profits?
- Will there be overall limits on numbers of agreements?
- How will this impact competitions on set-aside procurements?
- When should companies start researching for potential pairings?

# Agenda

- Significant expansion of mentor-protégé program
- New formulas for limitations on subcontracting
- Sources of oversight and enforcement
- Preview of proposed rules for small business size and status protests
- Questions?

# Limitations on Subcontracting: “Current” Limitations (1)

- Prime must perform certain percentage of cost of contract (does not include profit/fee charged at prime level):
  - Services (Non-Construction).  $\geq 50\%$  of the cost of the contract incurred for personnel with its own employees – includes any overhead which has only direct labor as its base and SB’s G&A rates multiplied by the labor cost.
  - Supplies or Products (Other Than Procurement from a “Non-Manufacturer”).  $\geq 50\%$  of the cost of manufacturing the supplies or products (not including the cost of materials). This includes the costs incurred by the SB in the production of the end item being acquired. It does not include costs of the materials purchased, shipping and handling, off-the-shelf items, or special tooling and test equipment.
  - General Construction. At least 15% of the cost of the contract with its own employees (not including the cost of materials).
  - Specialty Trade Construction. At least 25% of the cost of the contract with its own employees (not including cost of materials).
- Directed subcontracts do not count and subcontracts with affiliates of SB do not count as part of prime’s percentage

# Limitations on Subcontracting: “Current” Limitations (2)

- If Sub, understand how the limitations on subcontracting are calculated
- Focus on what does NOT count:
  - Services: 49% of the cost of the contract incurred for personnel; materials; supplies; overhead that does not have only direct labor as its base
  - Supplies: 49% of the cost of manufacturing the supplies; costs not incurred in production of the end item; materials, off-the-shelf items; required special tooling or test equipment
  - Construction: 84% of the cost of the contract, materials
  - Specialty Trade Construction: 74% of the cost of the contract, materials
- Also consider non-manufacturer rule, if applicable
- Must still consider other affiliation factors – “totality of the circumstances”

# Limitations on Subcontracting: “Changing” Limitations

- New rule for services: SB prime may not spend on subs more than 50% of the amount paid to the SB under the contract
- New rule for supplies: (other than from a regular dealer), SB may not spend on subs more than 50% of the amount paid under the contract, less cost of materials
  - Supplies from regular dealer: must supply the product of a domestic small business manufacturer or processor, unless waived by SBA under certain circumstances
- Added test: Also determine whether supplies or services represent the greatest percentage of the contract, and SB prime may not spend more than 50% of that amount on subs
- Similarly situated entities are not “subs”
- SBA may establish rules for categories of contracts not covered here; must establish similar rules for construction projects

# Limitations on Subcontracting: Potential Impact

- Major questions raised by these changing limitations include:
  - When will implementing regulations be issued? For SBA regulations and FAR? What about in the interim?
  - How is a “subcontractor” to be defined?
  - Will this result in more or less work performed by the SB prime?
  - If it requires greater self-performance, will it decrease competition?
  - Why was the calculation on construction not addressed?
  - Any requirements or obligations for determining that a subcontractor is a “similarly situated entity”? Is small business status determined based on NAICS code for the prime contract or most appropriate code for the subcontract?

# Agenda

- Significant expansion of mentor-protégé program
- New formulas for limitations on subcontracting
- Sources of oversight and enforcement
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- Questions?



# Oversight and Enforcement: Overarching Policies

- Ensure that small businesses are the true beneficiaries of set-aside dollars
- Encourage small business skill development in government contracting
- Assure use of small businesses as contemplated by contract awards
- Avoid fraud in contracting

# Oversight and Enforcement: 2013 NDAA Provisions

- Penalties associated with new limitations on subcontracting
  - Greater of \$500K or amount in excess of the limitations on subcontracting spent on subs
- Provisions for reporting the fraud of a prime
  - SBA to establish a reporting mechanism to allow a sub or potential sub to report fraudulent activity or bad faith by a prime with regard to a subcontracting plan
- Requirement for Suspension and Debarment
  - SBA directed to implement regulations for a suspension and debarment program to ensure that “fraudulent” businesses are suspended or debarred

# Oversight and Enforcement: Mentor-Protégé

- “Enforcement” under the Mentor-Protégé Program: SBA regulations identify consequences for a Mentor that fails to provide the assistance it committed to provide in its Mentor/Protégé agreement:
  - SBA may recommend that the procuring agency issue a stop work order for each Federal contract for which the Mentor and Protégé are performing as a small business joint venture; protégé may be permitted as substitute for mentor/protégé joint venture
  - Authorizes SBA to terminate a mentor/protégé agreement when the mentor has failed to provide the agreed upon developmental assistance, and render the mentor firm ineligible to again act as a mentor for a period of two years from termination of agreement
  - Failure to comply with terms and conditions of mentor/protégé agreement may be grounds for suspension/debarment

# SB Penalties for Misrepresentation

- Size protests can lead to determinations that entity is not small or not eligible for particular SBA status
- Other penalties could follow an adverse size/status determination
- The Small Business Act provides for severe criminal penalties for knowingly misrepresenting small business size status:
  - Fine of not more than \$500,000 or by imprisonment for not more than 10 years, or both
  - Subject to administrative penalties for fraud
  - Subject to suspension and debarment
  - Ineligible to participate in any program or activity conducted by the SBA for up to 3 years
- May also be subject to:
  - Investigations
  - Civil or criminal False Claims Act penalties

# Oversight and Enforcement: “Subcontract Integrity”

- Relates to “covered contracts” for which SB subcontracting plan is required (construction over \$1.5M; others over \$650K)
- Allows funding agency to monitor prime’s small business subcontracting and to encourage it to meet subcontracting plan
  - Prime must represent that it will make good faith efforts to award subcontracts to small businesses at same percentage as indicated in plan
  - Provide written justification and explanation to CO for failure to meet percentage
  - Notify CO if pay reduced price to subcontractor
  - Allow funding agency to establish goals at individual level for multi-agency, FSS, MAS, and IDIQ contracts

# Oversight and Enforcement: Example (1)

- Caddell Construction Co. Non-Prosecution Agreement (NPA) with DOJ to resolve criminal fraud allegations on two contracts
  - Related to overstatement of development assistance provided to SDB under DoD program
  - Related to participation in mentor-protégé program and participation in DoD Native-American business rebate program
    - False statements of Native-American business' size and income
    - Also regarding technical capabilities and business infrastructure
    - And requests for rebate against services largely completed by Caddell, not Native-American business
  - Caddell voluntarily disclosed issues
  - \$2 million penalty and NPA

# Oversight and Enforcement: Example (2)

- Virginia Security Contractors Pled Guilty to Illegally Obtaining \$31 million in Contracts Intended for SDBs
  - Formed one company with African-American woman as CEO in 2001 to participate in 8(a) program; she left in 2003 and company lost status
  - Formed second company in 2003, listing another minority woman as “figurehead owner,” but who would not actually manage the company
    - Misled SBA through 2012, including falsely certifying status under size protest
    - Also agreed to pay a bribe to US contracting official to secure contracts
  - Investigated by numerous IGs (NASA, SBA, GSA, DHS) and DCIS
  - Principal conspirator faces 10 years and multi-million fine for fraud; 5 years for conspiracy to commit bribery; forfeiture of \$6.3 million
  - Four other co-conspirators also pled guilty and will be sentenced this summer

# Agenda

- Significant expansion of mentor-protégé program
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# SB Size & Status Protests Background (1)

- Size/status protests differ from bid protests – file with the SBA under even tighter timelines
- Contractor may have to pursue size protest with SBA at same time as bid protest
- Low threshold to file; difficult/burdensome to respond; document production obligations and certifications for protested entity (SBA Form 355)
- Proposed rule issued 3/7/13 to amend FAR provisions related to small business size and status protests; 60 day comment period
- Most revisions are long overdue and consistent with 1/2/11 and 1/12/12 revisions to SBA regulations, which are already being applied by SBA in considering protests

# SB Size & Status Protests Background (2)

- Current FAR Size & Status Protest Procedures:
- Eligible offerors (does not include large businesses unless only 1 offer submitted), CO, and SBA may challenge size status
- File protest with CO within 5 business days; SBA Gov't Contracting Area Office decides; appeals to OHA
- Awardee has 3 business days to respond; may request extension
- Size protest must relate to a particular procurement and be specific to be considered
- SBA to issue a size determination w/in 10 business days, "if possible"
- Burden of persuasion is with the concern whose size is challenged
- Appeals are available for size and certain status determinations
- Status protests have slightly different procedures for each category
- NAICS code appeals also have own procedures

# SB Size & Status Protests Effect of Determination

- If a concern is found to be other than a small business
  - A CO shall not award a contract to the concern for the procurement in question
  - If the determination is received after award, the CO shall terminate the award if no appeal filed
  - If an appeal is filed, the CO must determine if performance can be suspended until an appellate decision is rendered
    - If the CO allows performance to proceed and the concern is found to be other than small on appeal, the CO shall either terminate the contract or not exercise the next option
- Once a concern is determined to be other than small
  - It cannot reduce its size to become eligible
  - Is ineligible for future procurements authorized for entities of that size or smaller unless SBA recertifies or OHA reverses
  - Recertification is not required if ineligibility was based only on affiliation due to joint venture (e.g., ostensible subcontractor)

# Proposed Rules: New Size Protest Procedures

- Increases time that SBA has to make a size determination of a protested concern to 15 business days and allow the CO to extend that time, if needed
- No award made until SBA makes size determination or 15 days since SBA receipt of protest (whichever first); CO may award if determine in writing necessary to protect the public interest
- If no SBA determination in 15 days (or granted extension), CO may award contract if determine in writing immediate need to award
- Clarifies that SBA may reopen a formal size determination to correct an error if still within appeal period and no appeal has been filed
- Clarifies that it is within the discretion of OHA to accept an appeal
- SBA decision if received before award, applies to the pending acquisition
- Provides for a CO to determine whether to suspend an award to a party whose size determination has been timely appealed
- Provides that a contract to a concern found ineligible by OHA, and award had already been made, must be terminated unless not in best interests of Gov't; no options or orders to be exercised

# Recent Size Appeal Cases

- *Professional Project Servs., Inc.*, SBA No. SIZ-5411 (2012) (NAICS Code omitted from GSA Schedule task order competition)
- *Metters Indus., Inc. v. United States*, 109 Fed. Cl. 444 (2013) (government enjoined from making award prior to OHA decision)
- *Miles Constr., LLC v. United States*, 108 Fed. Cl. 792 (2013) (reinstating protester to SDVOSB program)

# New Rule: Woman-Owned Small Businesses

- Previously, agencies could only set-aside contracts valued at \$4 million (\$6.5 million for manufacturing) for WOSBs or EDWOSBs
- NDAA for FY 2013 removed dollar value restrictions
- SBA issued Interim Final Rule effective immediately
- Contracting Officers now may set-aside any dollar value contract for WOSBs or EDWOSBs
  - in industries where WOSBs or EDWOSBs are underrepresented,
  - a reasonable expectation two or more entities will submit offers, and
  - the government can award a contract at fair and reasonable prices

# Proposed Rules: Misc. Other Revisions

- Clarifies requirements for “nonmanufacturers”
  - SB must be primarily in the retail or wholesale trade
  - Must sell the item in its normal course of business
  - Must take ownership or possession of item, consistent with industry practice
  - Must supply an end item made in the US (or outlying areas)
- States that CO must update the status of an ineligible concern in the Federal Procurement Data System (FPDS) once a final size determination is made
- Provides additional guidance to COs regarding NAICS determinations
  - Instructs that CO shall select NAICS code that best describes “principal purpose” of product or service
  - Including changes to the appeal process

# Agenda

- Significant expansion of mentor-protégé program
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# Questions?

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**The Pendulum Continues to Swing the  
Wrong Way for Contractors:  
*The Government's Continued Assault on  
Contractor Intellectual Property***

John E. McCarthy Jr.

Jonathan M. Baker

Jacinta Alves

# FY 2012 NDAA Data Rights Changes

John E. McCarthy Jr.

# 2012 NDAA Data Rights Changes

- Enacted
- Applicable to DoD only
- Scope of change unclear pending implementing regulations

# 2012 NDAA Data Rights Changes

- “segregation” “reintegration” data
  - “necessary for the segregation of an item or process from, or”
  - “the reintegration of that item or process (or a physically or functionally equivalent item or process) with, other items or processes”

10 U.S.C. § 2320(a)(2)(D)(i)(II)

# 2012 NDAA Data Rights Changes

- New exception to non-disclosure of limited rights technical data
  - “such release, disclosure, or use . . . is”
    - “necessary for the segregation of an item or process from, or”
    - “the reintegration of that item or process (or a physically or functionally equivalent item or process) with, other items or processes”

10 U.S.C. § 2320(a)(2)(D)(i)(II)

# 2012 NDAA Data Rights Changes

- Super deferred ordering provision
  - Notwithstanding any contract delivery requirements, USG can require delivery of technical data
    - If generated or used in the performance of a contract
    - Needed for “reprocurement, sustainment, modification, or upgrade (including through competitive means) of a major system or subsystem thereof, a weapon system or subsystem thereof, or any noncommercial item or process,” AND
      - Pertains to an item or process developed in whole or in part with Federal funds; OR
      - “segregation” “reintegration” data
    - Compensation = copying costs
- 10 U.S.C. § 2320(b)(9) (emphasis added).
- No Time Limitation

# 2012 NDAA Data Rights Changes

- Extends the right for the Government to challenge use or release restriction from three years to six years from the latter of
  - Date of final payment of contract in which data is required to be delivered
  - Date of delivery
- No date restriction in the case of fraudulently asserted use or release restriction

10 USC 2321(a)(2)



# Policy Changes Impacting Contractor Intellectual Property

Jonathan M. Baker

# DoD's Better Buying Power 2.0

- Preliminary version issued November 13, 2012
- “Do more without more”
- 7 Focus Areas
  - Achieve Affordable Programs
  - Cost Controls Throughout the Product Lifecycle
  - Incentivize Productivity & Innovation in Industry & Government
  - Eliminate Unproductive Processes & Bureaucracy
  - *Promote Effective Competition*
  - Improve Tradecraft in Acquisition of Services
  - Improve the Professionalism of the Total Acquisition Workforce

# BBP 2.0: Implementation Directive

- Implementation Directive issued April 24, 2013
- Effective immediately
- BBP 2.0 is subject to professional judgment; it is not “rigid dogma”

# BBP 2.0: Promote Effective Competition

- Emphasizing Competition Strategies
  - Competition from cradle-to-grave
  - Strategies:
    - Leader-follower arrangements
    - Open systems architecture (OSA)
    - Acquisition of technical data packages
    - Competition at subsystem level

# BBP 2.0: Promote Effective Competition

- Enforce OSAs & effectively manage technical data rights
  - Emphasis on OSAs supportable through multiple competitive alternatives
  - Focus on IP strategy that is implemented over product's lifecycle
  - DoD components must describe how OSA is considered during milestone reviews
  - Sole-source J&A waivers must discuss OSA

# BBP 2.0: Promote Effective Competition

- Specific Actions
  - Re-publish OSA Contract Guidebook for Program Managers (PMs), version 1.1 by June 1, 2013
  - Re-publish DoD Data Rights Brochure to update changes to DFARS by Oct. 1, 2013
  - Publish replacement procedure for acquisition & management of technical data by Jan. 1, 2014

# OSA Contract Guidebook for PMs

- Draft issued in December, 2011
- USG cannot condition award or responsiveness on relinquishing rights, but can evaluate data rights
- Includes model solicitation language for SOW, sections H, L, M

# Update on Recent Case Law

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# *Coastal Seal Services, LLC*

- B-406219, March 12, 2012, 2012 CPD ¶ 111
- GAO protest of Navy's proposed sole-source contract for stern tube seal repair kits for ships
- Sole-source J&A largely based upon Navy's lack of rights in, and access to, relevant technical data relating to the seals construction and manufacture

## *Coastal Seal Services, LLC (cont'd)*

- Navy argued lack of technical data made it impossible to determine whether protester's proffered design was an adequate substitute
- GAO concluded that this was a proper basis for a sole-source award

## *Appeal Of Alenia N. Am., Inc.*

- ASBCA No. 57935, 2013 WL 1871512 (Mar. 26, 2013)
- Contract did not contain any FAR or DFARS data rights clauses
- Contractor delivered publications with restrictive markings

# *Appeal Of Alenia N. Am., Inc. (cont'd)*

- Air Force sent Alenia letter 18 months after delivery of first publication challenging Alenia's assertions
- Alenia disagreed
- CO issued a final decision stating it had unlimited rights to the publications, arguing
  - DFARS 252.227-7037, Validation of Restrictive Marking, was incorporated by operation of law pursuant to the Christian Doctrine
  - Alenia never identified any restrictive data in its proposal
  - Inconsistent with Distribution Statement C, required by the contract

## *Appeal Of Alenia N. Am., Inc. (cont'd)*

- Contractor appealed final decision to ASBCA
- Contractor then argued ASBCA lacked jurisdiction, because there was no claim
- ASBCA found that there was a government claim

# *Colt Defense, LLC*

- B-406696.2, Nov. 16, 2012, 2012 CPD ¶ 319
- GAO protest alleging terms of the solicitation are inconsistent with the terms of Colt's license agreement with the Army
  - Protester relied on FAR 27.202-2(b)(1) “[w]hen the Government is obligated to pay ... a royalty,” agencies must “[e]valuate an offeror's price by adding an amount equal to the royalty.”

## *Colt Defense, LLC (cont'd)*

- GAO dismissed protest:
  - GAO will not resolve a dispute involving interpretation of a license agreement
  - FAR 27.202–2
    - Not applicable to royalties on the use of technical data
    - Does not preclude the evaluation of a royalty where the amount of the royalty has yet to be determined

## *D'Andrea Bros. LLC v. U.S.*

- 109 Fed. Cl. 243 (2013) (Judge Firestone) recon. denied, 08-286C, 2013 WL 1316534 (Fed. Cl. Mar. 28, 2013)
- Licensee claimed \$1.95 million in reliance damages for alleged breach of implied covenant of good faith and fair dealing in connection with a CRADA
- Government counterclaimed for \$60,000 in unpaid royalties



# *D'Andrea Bros. LLC v. U.S. (cont'd)*

- Exclusive five-year license to trademarks for HooAH! nutritional energy bars in exchange for payment of royalties to Army
- Army agreed to help licensee test and improve HooAH! bars for commercial market
- Alleged Army breached the CRADA by:
  - Unreasonably failing to communicate with Claimant for 9 months
  - Changing name of its military energy bar from “HooAH!” to “First Strike”
  - “Bad mouthing” and electing to compete with plaintiff by developing its own bar within the military community

# *D'Andrea Bros. LLC v. U.S. (cont'd)*

- Holdings:
  - Government breached implied covenant of good faith and fair dealing
  - Government's breach was a prior material breach excusing licensee's failure to pay royalties
  - Licensee was not entitled to reliance damages

# *ITT Electronic Services*

- B-406405 *et al.*, May 21, 2012, 2012 CPD ¶ 174
- GAO protest alleging unequal treatment in evaluating the data rights that each offered to the government
- One of the five technical evaluation subfactors provide for, among other things, the evaluation of data rights granted to the government

## *ITT Electronic Services (cont'd)*

- All 3 offerors offered a mix of limited and unlimited data rights
- Agency assessed a marginal rating due, in part, to ITT's proposed data rights
- GAO found that ITT's offer included different restrictions not found in the other offers
- Evaluation reflected “reasonable distinction” between proposals

# *IHS Global, Inc. v. U.S.*

- 106 Fed. Cl. 734 (2012) (Judge Wheeler)
- Procurement for, *inter alia*, access to a database of information regarding obsolete parts
- Protest challenged a sole-source award to BAE
- Air Force justified sole-source contract on basis that the BAE parts database was needed to perform the contract
- Protester alleged:
  - BAE's specifically negotiated license agreements relating to the parts data either did not cover the relevant data or were invalid
  - Two years earlier, BAE failed to include a particularly relevant data field on a list of data to which it asserted ownership rights

# *IHS Global, Inc. v. U.S. (cont'd)*

- COFC found that IHS lacked standing, because the database proposed by IHS admittedly could not meet the contract requirements, and therefore did not reach the merits of the issues
- In *dicta*, COFC:
  - Expressed skepticism of any claims of entitlement to data developed in performance of contracts paid for by the government
  - Agreed with Air Force approach to avoid the data rights issue

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# Costs

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# DCAA's Continuing Troubles

- DCAA criticized for audit quality issues
  - March 7, 2013 DoD IG Report found audit quality issues through FY 2010
  - E.g., of the sample surveyed, 0 met government auditing communication standards, 8% met quality standards, 22% met evidence standards, 26% met professional judgment standards
- Significant delays in incurred cost audits
  - DCAA's 2012 report to Congress revealed that it completed 349 incurred cost audits in 2011 and had an audit backlog of almost 25,000 incurred cost proposals (do the math – 714 year backlog)
  - While DCAA has implemented steps to address the backlog – dedicated audit teams, multiple-year audits, and low risk sampling – it is too big to be resolved quickly
  - Backlog results in document retention issues and potential Statute of Limitations problems for the government

# Statute of Limitations for Incurred Cost Claims

- The Contract Disputes Act, 41 U.S.C. §§ 7101-7109, sets forth certain prerequisites for the exercise of jurisdiction over claims, including 6-year SOL
- Claims submitted more than six years after accrual are not valid and cognizable under the CDA
- CDA does not define the term “accrual.” The Board (and the Court) rely on the Federal Acquisition Regulation 33.201 definition:
  - ... the date when all events, which fix the alleged liability of either the Government or the contractor and permit the assertion of the claim, were known or should have been known ...
- “Contracting parties cannot establish a statute of limitations longer than that set forth in the Contract Disputes Act, where the Government is a party ... [th]us, parties may set a shorter limitations period, but not a longer one.” - Judge Robert Hodges, *Raytheon Co. v. United States*, No. 09-306C (April 2, 2012)
- Key takeaway: once a contracting party is aware of the basis for its claim, it is “on the clock” and should not rely on discussions or agreements with the other party to resolve a dispute or toll the statute of limitations, at the expense of preserving its claim.

# Statute of Limitations

- *Sikorsky Aircraft Corp. v. United States*, COFC Nos. 09-844C, 10-741C (July 2012)
  - Court of Federal Claims found there to be triable issues of fact with regard to contractor's SOL defense as to when the government's claim accrued, i.e., when the government "knew or should have known" of alleged CAS 418 noncompliance.
  - This case raises very interesting issue of who in the government needs to have notice of a claim for it to accrue -- a contracting officer or "other responsible actors" such as DCAA auditors?
  - FN 12: "The parties strenuously dispute who in the government must have notice of a claim for it to accrue. The government contends that, for a CAS noncompliance claim to accrue, the contracting officer must have notice. Sikorsky contends that accrual may occur when other responsible actors, purportedly including DCAA auditors, know of the claim. At this early juncture it is unnecessary to decide the question."
  - Subsequent dispute about assertion of deliberative process privilege.

# Statute of Limitations

- *Appeal of Raytheon Co.*, ASBCA Nos. 57576, 57679 (December 17, 2012)
  - Raytheon appealed Government's claims to recover increased costs paid under government contracts, plus penalties and interest, for CAS and FAR violations relating to incentive compensation plans.
  - Good decision for contractors, though somewhat unclear.
  - DCAA audited incentive compensation plans in prior years and accepted the costs. DCAA subsequently changed its mind about what was allowable, and Raytheon argued that the final decision disallowing costs in ALL subsequent years was time-barred because the final decision was more than 6 years after initial audit report.
  - Board found that the Government's failure to bring a claim within 6 years of the audit -- in the year where there was an actual audit -- was time-barred.
  - Board did not find that all Government claims are barred if not brought within 6 years of the incurred cost submission, only that in the circumstances of the case, where the plans at issue had been audited and accepted in a prior year, the CDA "should have known" standard began to run as to the costs of those plans when the claims including those plans were submitted.

# Statute of Limitations

- *Appeal of Raytheon Co.*, ASBCA No. 58011 (January 28, 2013)
  - Raytheon appealed COFD asserting \$17 million claim arising from alleged CAS violation.
  - Here, ASBCA held that the statute began to run in 1999, when a DCMA price analyst had all the information the government needed to recognize that it had a claim for an alleged CAS violation, even though the responsible CO may not have been aware of the claim until an audit report was issued in 2006.
  - In the absence of any evidence of trickery or concealment, the government "should have known" that it had a claim based on the contractor's 1999 cost proposal that appeared to be inconsistent with its disclosed accounting practice, and that the government could not unilaterally extend the statute of limitations by failing to perform an audit that put the CO on actual notice that there might be a claim.
  - Government's claim found to be untimely, and therefore barred by the SOL. Significant case in the evolving interpretation of the CDA statute of limitations.

# Implications of SOL Decisions for Incurred Cost Claims

- What happens when an Government decision disallowing costs is time-barred?
- Are all costs included in the contractor claim allowable, regardless how clearly unallowable they may be (alcohol, charitable contributions, lobbying, etc.)?
- If a CAS noncompliance is not caught in year one, how long is the Government barred from disallowing the increased costs resulting from the noncompliance in subsequent years?

# Access to Internal Audit Reports

- December 2011 -- GAO report recommended that DCAA establish a procedure for obtaining internal audit reports from contractors to improve the efficiency of audit planning and execution.
- August 2012 – DCAA issued guidance requiring audit offices at major contractor locations to establish a process for obtaining and monitoring DCAA's access to and use of internal audit reports and work papers, when needed.
- January 2013 – Congress directed DCAA to revise its guidance on access to contractor internal audit reports.
  - DCAA must document its rationale for requesting internal audit reports
  - DCAA must document contractor's rationale if access is denied
  - DCAA cannot use internal audits as sole basis to disapprove a contractor's business system

# Business Systems Reviews

- No decisions, so far.
- Anecdotal evidence suggests that there have been a number of inadequacy findings as to accounting systems, at least, but apparently in circumstances where the contractor decided that disputing the findings was imprudent.
- In at least one case, DCMA forced the contractor to make changes based on a threat to find the system inadequate, very arguably where such a finding was unjustified.



# Developments in Cost Law: Executive Compensation Reviews

- *Appeal of Metron, Inc.*, ASBCA Nos. 56624 et al. (2012)
  - Company's comp for its executives set based on survey data
  - DCAA questioned executive compensation included in indirect rate proposals for two years
  - Government's expert agreed with Metron's that DCAA's methodology contained numerous flaws
  - Board found that Metron's comp plan set reasonable compensation levels based on achievement of pre-established management goals and metrics and that Metron had followed its plan
  - DCAA's extrapolations and adjustments of the compensation survey data were unmerited; DCAA improperly classified a number of the executives as non-executives; DCAA used unreliable surveys

# Developments in Cost Law:

## Legal Fees and REA Preparation Costs

- *Tip Top Construction, Inc. v. Donahue*, CAFC No. 2011-1509 (Sept. 19, 2012)
  - Federal Circuit reversed PSBCA, and held that attorney (and consultant) costs arising out of negotiations over the price of changed work were recoverable under the Changes clause.
  - PSBCA had held that work “solely directed at ... maximizing [Tip Top’s] recovery” did not constitute recoverable contract administration costs.
  - Federal Circuit rejected this view:
    - Simply because the negotiations related to the price of the change does not serve to remove the associated costs from the realm of negotiation and genuine contract administration costs. Consideration of price is a legitimate part of the change order process.
  - Bottom line: price adjustment held to be a part of the change order process.
  - Almost all litigation about these issues arises in construction cases, where contractors often classify costs that would be indirect in other industries as direct project costs.

# Developments in Cost Law: Legal Fees and REA Preparation Costs

- *Appeal of F. Versar, Inc.*, ASBCA No. 56857 (April 23, 2012)
  - Appeal arising out of a task order for HVAC and other work at a DoD elementary school in Fort Jackson, South Carolina.
  - Board held, probably wrongly, that costs incurred preparing REA were not allowable because the REA was prepared by the contractor’s employees rather than by a professional / consultant (note that REA preparation was a very small part of the contractor claim and may not have been the subject of extensive briefing).
  - “REA preparation costs, costs of professional and consultant services incurred for the genuine purpose of materially furthering a negotiation process, and rendered by persons who are not officers or employees of the contractor, are normally contract administration costs allowable under FAR 31.205-33 ... However, here, appellant's project manager ... submitted the REA, the preparation costs were primarily effort by him and appellant's off-site QA/QC manager, and there is no evidence that appellant paid for any consultant or professional services in connection with the REA's preparation ... Thus, the claimed ... REA preparation costs [are]not allowable.”
  - Board also disallowed costs incurred preparing an REA that was never filed (but “evolved” into a certified claim) on the grounds that it considered the work part of the contractor’s prosecution of a CDA claim.

# Developments in Cost Law:

## Cost Reasonableness

- *KBR v. U.S.*, 103 Fed. Cl. 714 (2012)
  - Using DCAA Form 1, government suspended \$41.1 million associated with a cost reimbursement contract to build a dining facility in Iraq.
  - Government alleged that KBR caused higher-than-necessary subcontract costs because it did not conduct reasonable negotiations with its subcontractor.
    - E.g., the KBR negotiator had not followed standard KBR negotiation policies and procedures, had unreasonable negotiation objectives, included errors and deficiencies in the price negotiation memorandum.
  - Based on evidence of reasonableness presented at trial, Court concluded that KBR demonstrated the reasonableness of approximately  $\frac{1}{4}$  of the suspended costs, and thus was entitled to reimbursement of \$11.5 million.

# Developments in Cost Law:

## Cost Reasonableness

- *KBR v. U.S.*, 107 Fed. Cl. 16 (2012)
  - Using DCAA Form 1, government disallowed \$12.5 million associated with a cost reimbursement contract to build a dining facility in Iraq.
  - KBR argued for an alternative standard for reasonableness; Government argued – and the Court agreed – that FAR 31.201-3 alone provides the standard for determining reasonableness of costs.
  - The Court found that KBR failed to demonstrate that another dining facility subcontractor's costs were reasonable because KBR's subcontract administrator failed to adequately negotiate the price, his price negotiation memorandum was flawed, and KBR failed to provide a price basis for comparison.
  - KBR entitled to \$4.2 million of the disputed \$12.5 million, reflecting, in part, KBR's ability to demonstrate that reasonableness using an after-the-fact price reasonableness analysis conducted by an expert.

# Developments in Cost Law:

## Cost Reasonableness

- *Appeal of Kellogg Brown & Root, ASBCA No. 56358 (2012)*
  - KBR appealed the denial of its claim for \$19.6 million for private security services for one of its dining facility subcontractors.
  - While the ASBCA found that there was no prohibition under the prime contract against the use of armed private security companies without express permission of the theater commander, the Board found genuine issues of material fact about whether, at the time of subcontract award, a component of the fixed prices for the security companies was reasonable as to both the need for and amount of that component.
  - The Board rejected KBR's argument that the Government has no contractual right to disallow a particular component of a subcontract fixed price, but can consider only the allowability of the total subcontract price.

# Developments in Cost Law: CAS Compliance

- *Sikorsky Aircraft Corp. v. United States*, COFC Nos. 09-844C & 10-741C (March 2013)
  - Sikorsky failed to demonstrate that the Government had actual or constructive knowledge of a potential claim under CAS 418 (court had declined to grant summary judgment on this issue in July 2012).
  - But, Government unable to demonstrate Sikorsky's noncompliance with the CAS 418.
  - Court of Federal Claims denied the Government's \$80 million claim for alleged CAS 418 violation.

# DOE Contractor Legal Costs

- DOE has just issued a final rule addressing its handling and reimbursement of contractor legal costs (78 Fed. Reg. 25795, May 3, 2013)
  - Applicable to management and operating (“M&O”) contractors; cost reimbursement contractors with contracts over \$100 million; other contractors with contracts over \$100 million that include cost reimbursable elements of over \$10 million.
  - DOE can direct the contractor to initiate litigation against third parties, despite possible ethical problems for the contractor’s counsel and the fact that the resulting legal costs will be found allowable.
  - Requires DOE approval of legal settlements involving contractor payments of \$25,000 or more.
    - DOE approval also required for subcontractor and third party insurance settlement payments.
  - Limits reimbursement of costs for retaining legal counsel.
  - Compliance with the rule does not guarantee that costs will be allowable; allowability rules in FAR and DEARS will still apply.



# “Obamacare” Cost Issues

- FAR 31.205-41 provides that all excise taxes on employee benefits that are listed in Subchapter D, Chapter 43, of the Internal Revenue Code are expressly unallowable on Government contracts
- All of the excise taxes imposed by the Affordable Care Act are included in that subchapter, including
  - Excise tax for failing to offer insurance to some employees and
  - Excise tax on offering “rich” plans to employees
  - (See Sections 4980H and 4980I of the Code)

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