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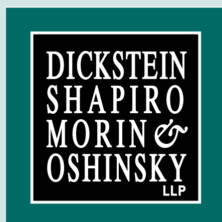

Legal Innovators

Our attorneys guide clients through the maze of regulations to maximize a company's ability to secure government contracts. If you would like more information on this issue or any other government contracts issue, please contact us.

Richard J. Conway
ConwayR@dsmo.com
(202) 828-2235

Merle M. DeLancey, Jr., ***Author***
DeLanceyM@dsmo.com
(202) 828-2282

J. Andrew Jackson, ***Author***
JacksonA@dsmo.com
(202) 828-2268

David M. Nadler
NadlerD@dsmo.com
(202) 828-2281

Jacob B. Pankowski
PankowskiJ@dsmo.com
(202) 828-2207

Charlotte R. Rosen
RosenC@dsmo.com
(202) 955-6672

Robert J. Moss, ***Author***
MossR@dsmo.com
(202) 775-4784

Enforcing Teaming Agreements

By Robert J. Moss

In recent years, the federal government has consolidated many of its contracts to reduce administrative costs. This process has resulted in the bundling of very diverse requirements under single master contracts, and has created the need for government contractors to team together to meet the government's consolidated requirements.

Although the Federal Acquisition Regulation (FAR) expressly recognizes teaming agreements in the context of government procurements, *see* FAR Subpart 9.6, the enforceability of teaming agreements between the parties is governed by state law. Historically, most state courts (and federal courts applying state law) have viewed teaming agreements as unenforceable "agreements to agree." Recently, however, the Circuit Court of Fairfax County, Virginia signaled a possible relaxation of the restrictions that Virginia has traditionally imposed on the enforceability of teaming agreements. *EG&G Inc. v. Cube Corp.*, In Chancery No. 178996 (Dec. 2002).

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Former United States Senator Tim Hutchinson Joins Dickstein Shapiro

Former U.S. Senator Tim Hutchinson (R-Arkansas) joined Dickstein Shapiro Morin & Oshinsky LLP as Senior Advisor in January 2003, bringing more than 18 years of legislative experience to the Firm. He works with the Legislative & Regulatory Affairs Group, advising Firm clients on congressional and executive branch issues and adding depth in the areas of homeland security, health care, defense, agriculture, education, and transportation. Senator Hutchinson served as U.S. Senator from 1997 through 2002, and worked on the Armed Services Committee, where he was a ranking member of the Armed Services Personnel Subcommittee; the Health, Education, Labor, and Pensions (HELP) Committee, where he was a ranking member of the HELP Aging Subcommittee; the Agriculture, Nutrition, and Forestry Committee; the Veterans' Affairs Committee; the Environment and Public Works Committee; and, the Special Committee on Aging. He also founded the Senate Biotechnology Caucus in 2001.

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The seminal case on teaming agreements in Virginia is *W. J. Schafer Assocs., Inc. v. Cordant, Inc.*, 254 Va. 514 (1997). There, the Virginia Supreme Court held that a teaming agreement on a federal procurement was an unenforceable "agreement to agree" because it left open several essential subcontract terms, including the price to be paid by the prime contractor to the subcontractor. The *Schafer* decision highlights the practical difficulty that contractors face in entering a teaming arrangement, that is, the difficulty of knowing what price or rates the government will ultimately accept.

Generally, teaming agreements are executed before the team submits its initial proposal to the government, and they contemplate that the parties will enter into a subcontract, assuming a prime contract is awarded by the government. As part of the evaluation and award process, the government often negotiates price or rate reductions (or service-level increases) before awarding the prime contract. Because of the pricing uncertainty created by that process, the parties to a teaming agreement are often unable to agree on final prices or rates at the time the teaming agreement is executed. Instead, the parties normally include a provision requiring them to negotiate prices or rates in good faith after award of the prime contract. It is that very agreement to negotiate, however, that led the court in *Schafer*, and has led most other courts, to find teaming agreements unenforceable.

The *EG&G* decision appears to be the first attempt to reconcile the conflict between federal procurement law recognizing teaming agreements and their historical unenforceability under state laws. In *EG&G*, Cube (as prime contractor) and EG&G (as subcontractor) entered into a teaming agreement. After the government awarded a prime contract to Cube, the parties entered into an interim letter agreement under which EG&G agreed to begin performance pending execution of a subcontract. During subcontract negotiations, Cube attempted to add a convenience termination provision and a G&A rate cap, neither of which was mentioned in the parties' teaming agreement. EG&G resisted. Ultimately, the parties failed to reach a final agreement on a written subcontract, and EG&G brought suit to enforce the teaming agreement.

Distinguishing *Schafer*, the Circuit Court of Fairfax County found that, although the parties failed to execute a contemplated written subcontract, their teaming agreement, combined with their subsequent conduct, provided adequate evidence of their intent to be bound by the essential terms of the subcontract. The court held that, "in the context of Teaming Agreements, the court may examine the parties' conduct, including any proposals submitted in response to a government RFP, to ascertain whether they intended that the proposed subcontractor receive a subcontract upon award to the prime." Central to the court's analysis was Cube's proposal to the government, which "touted" EG&G's experience. This, the court found, provided adequate evidence of the parties' intent that EG&G would receive a subcontract upon award of the prime contract. The court also found that, because EG&G had been performing during negotiations and Cube had been paying EG&G without dispute, the parties' conduct demonstrated that they did in fact agree on price. The court concluded that the two new terms that Cube attempted to introduce in negotiations were inconsistent with the parties' teaming agreement, and thus did not excuse Cube's refusal to execute the subcontract. Significantly, rather than award damages, the court ordered specific performance of the subcontract and enjoined Cube from terminating EG&G absent a subsequent breach.

Whether the *EG&G* decision will withstand appellate review cannot be predicted. Regardless, contractors contemplating a teaming agreement should review the *EG&G* decision. This potential shift in the law could create advantages or pitfalls depending upon whether you are a prime contractor or subcontractor. Through careful planning and negotiation, a prime contractor may obtain the benefits of a teaming agreement without losing business flexibility. By the same token, subcontractors should carefully analyze proposed teaming agreements to determine whether they will ultimately be legally enforceable.

If you would like a copy of the *EG&G* decision or advice concerning a teaming agreement, please contact one of the attorneys in Dickstein Shapiro Morin & Oshinsky LLP's Government Contracts Practice.

Federal Acquisition of Information Technology by State and Local Governments Through Federal Supply Schedules

By J. Andrew Jackson and Merle M. DeLancey, Jr.

On January 23, 2003, the General Services Administration (GSA) requested comments regarding a proposed rule that would amend the GSA Acquisition Regulation to implement Section 211 of the E-Government Act of 2002. Section 211 authorizes GSA to permit state and local governments to make purchases from Federal Supply Schedule (FSS) 70, which covers automated data processing equipment (including firmware), software, supplies, support, equipment, and services. GSA refers to the proposed rule and its effect as "cooperative purchasing."

As you may recall, GSA attempted, albeit unsuccessfully, to "open" FSS schedules to state and local governments in 1995. The 1995 initiative sought to open *all* FSS schedules to cooperative purchasing, but met significant industry opposition. GSA now has narrowed its focus by proposing to open only Schedule 70. At a February 4, 2003 public meeting regarding the proposed rule, GSA reserved the right to add or subtract the products and services it intends to "open" based upon public comments. For example, GSA does not currently intend to open the Federal Technology Service Schedules to state and local governments; however, GSA reserved the right to do so if public comments supported it.

Under the proposed rule, GSA intends to allow contractors to voluntarily opt-in to cooperative purchasing. All solicitations and contracts awarded after the effective date of an Interim or Final Rule, as well as existing contracts, will be modified to provide contractors the opportunity to opt-in. However, even if a contractor chooses to participate, it can still decline to accept any and/or all orders that are attempted to be placed by state or local governments. In other words, by opting-in, a contractor has not automatically agreed to sell to state and local government customers at FSS prices. This provision provides contractors substantial flexibility in dealing with state and local entities.

As a general notion, the proposed rule provides that state and local governments placing FSS orders are prohibited from changing or modifying the underlying FSS terms and conditions. The exceptions to this rule are the Disputes clause, Patent Indemnity clause, and Payments clause, which may be changed by mutual agreement of the contractor and the state or local government buyer. Because certain states have enacted laws that require certain specific terms and conditions, those states may not be able to participate, absent modification or elimination of the applicable statute. The standard 1% Industrial Funding Fee (IFF) will apply to any state and local government purchases (effective January 1, 2004, the IFF will be reduced to 3/4%).

While the proposed rule will open Schedule 70 contracts to new customers, it is troubling in several respects. First, it requires that a new clause, "Contractor's Billing Responsibilities" (GSAR 552.232-83), be included in Schedule 70 solicitations and schedule contracts. This new clause, which concerns a schedule contractor and its dealers, creates new reporting obligations and new liability under the Price Reductions clause (PRC):

> An agreement between a Contractor and its dealers pursuant to this procedure will not establish privity of contract between dealers and the Government. **Price reductions made by a participating dealer on sales under this contract will result in an overall price reduction being assessed against the Contractor as provided for in the Price Reduction clause.**

As you are aware, the PRC requires that a schedule contractor maintain the relative relationship between the price/dis-

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count given to the government and the price/discount given to the Basis of Award customer (previously, the "customer of comparability"). If better prices/discounts are given to the Basis of Award customer, the more favorable price/discount must be passed on to the government.

The proposed rule and new clause would trigger the PRC for the contractor when "[p]rice reductions made by a participating dealer on sales under this contract will result in an overall price reduction being assessed against the Contractor..." This clause can be read to mean that dealer sales will trigger a price reduction against a manufacturer. Presently, of course, sales to the federal government – regardless of price or discount – do not trigger a price reduction. Alternatively, the proposed clause might be read to mean that all dealer sales must be reported to the manufacturer and that any dealer commercial discount may require that the manufacturer/contractor give an across-the-board discount to all government customers (regardless of the identity of the contractor's Basis of Award customer). We believe that this new proposed liability was not an intended result when Congress passed Section 211. We also believe that the proposed clause may result in higher prices and adversely impact manufacturer/dealer relationships.

GSA intends to publish an Interim or Final Rule on April 17, 2003. There is a public meeting concerning the proposed rule scheduled for March 10, 2003. Comments on the proposed rule are due March 24, 2003. If you have any questions regarding how the proposed rule could impact your company, please contact us.

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The Government Contracts Practice of the Technology Group of Dickstein Shapiro Morin & Oshinsky LLP assists clients in obtaining and maintaining a competitive edge in government procurements.

If you would like to receive future issues of *The Advisor* via e-mail, please contact MaryBeth Mora at MoraM@dsmo.com.

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Dickstein Shapiro Morin & Oshinsky LLP
www.DicksteinShapiro.com

2101 L Street, NW
Washington, DC 20037
Tel: (202) 785-9700 Fax: (202) 887-0689

1177 Avenue of the Americas
New York, NY 10036
Tel: (212) 835-1400 Fax: (212) 997-9880