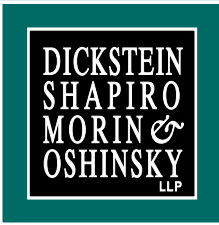




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*Legal Innovators*

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.

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## Government Contracting Under The Homeland Security Act

The Homeland Security Act of 2002 (HSA)<sup>1</sup> represents the single most extensive restructuring of the federal government in the past 50 years. Under the HSA, 22 existing federal agencies with more than 160,000 employees merged under the umbrella of the Department of Homeland Security (DHS). With an estimated annual budget in excess of \$36 billion, DHS is the third-largest federal agency behind the Department of Defense (DOD) and the Department of Veterans Affairs.

Because DHS is comprised of existing federal agencies, any contract already in place with a consolidated agency has been transferred to DHS and continues to operate without significant change. HSA § 1511. On a going-forward basis, however, DHS is authorized to employ special contracting procedures that represent a dramatic departure from standard government contracting procedures. The HSA also provides special contracting rules for other executive agencies acquiring goods or services needed to combat terrorism. This paper provides an overview of the significant changes in government contracting practices that have been implemented under the HSA in procurements conducted by DHS and other government agencies combating terrorism.

### I. DHS Acquisitions

#### A. Mission and Organizational Structure

The mission of DHS is to prevent domestic terror attacks, reduce domestic vulnerability to terror attacks, and minimize the harm caused by, and assist in the recovery following, any terror attack that may occur. HSA § 101. To accomplish its mission, DHS is divided into four Directorates: (1) Border and Transportation Security, which is charged with securing the nation's borders and transportation systems, including airports, seaports, and shipment centers; (2) Science and Technology, which conducts and coordinates counter-terror research and development efforts; (3) Information Analysis and Infrastructure Protection, which gathers, coordinates, and analyzes anti-terror intelligence and assesses security risks surrounding civilian and military infrastructure; and, (4) Emergency Preparedness and Response, which is charged with managing emergency response systems and procedures.

As an executive department of the federal government, DHS generally is subject to the procurement statutes that govern all executive agencies,<sup>2</sup> including the

*continued on next page*

Competition in Contracting Act of 1984 (CICA)<sup>3</sup> and the Truth in Negotiations Act (TINA),<sup>4</sup> as well as the Federal Acquisition Regulation (FAR),<sup>5</sup> which imposes detailed, mandatory competitive procedures on government procurements. The HSA, however, creates areas of special contracting authority applicable only to DHS.

## **B. DHS's Special Contracting Authority**

### **1. Conditions under which DHS may use its special contracting authority**

Under the HSA, DHS is granted special contracting authority when its mission would otherwise be "seriously impaired." HSA § 833. That determination must be made by the Secretary of Homeland Security or his designee (who must be a presidential appointee confirmed by the Senate), and specifically must find that normal competitive procedures would seriously impair DHS's ability to carry out its functions. To trigger its special contracting authority, DHS also must promptly inform Congress of its determination and the basis for its determination. *Id.* Once those conditions have been met, the HSA authorizes DHS to: (1) increase the micro-purchase threshold from \$2,500 to \$7,500; (2) increase the simplified acquisition threshold from \$100,000 to \$200,000 for domestic contracts and to \$300,000 for foreign contracts; and, (3) expand the use of commercial item acquisitions.

#### Increasing the micro-purchase threshold from \$2,500 to \$7,500:

Under FAR Subpart 13.2, agencies making purchases at or below the micro-purchase threshold may use extremely simplified purchasing procedures under guidelines set forth in FAR 13.202. The primary advantage of micro-purchases is that contracting officers may use

the government-wide commercial purchase card. Once DHS's special contracting authority has been triggered, DHS is permitted to use those extremely simplified procedures in acquisitions up to \$7,500.

#### Increasing the simplified acquisition threshold:

Under FAR Subpart 13.1, agencies making purchases in excess of the micro-purchase threshold, but below the simplified acquisition threshold, may employ the streamlined acquisition procedures of FAR Part 13, which significantly reduce advertising, competition, and evaluation requirements and specify far less burdensome contract clauses. Once DHS's special contracting authority is triggered, the HSA raises the simplified acquisition threshold to \$200,000 for contracts to be performed in the United States and \$300,000 for contracts performed outside the United States.

#### Expanding the use of commercial item acquisitions:

Under the FAR, agencies acquiring commercial items may use the streamlined acquisition and administration procedures in FAR Part 12, which permit reduced competition, streamlined contract clauses, and commercial data rights provisions. Under the HSA, once DHS's special authority is triggered, DHS may purchase up to \$7.5 million of *any* goods or services as if they were commercial items.

Of these three special procedures, the first two have a relatively limited impact on government contracting because they implicate relatively small dollar amounts. The third, however, is quite significant in scope and, thus, if employed with any frequency, may significantly alter standard government contracting practices. This item also is potentially controversial in its application because, as dis-

cussed below, it is not at all clear how, and to what effect, commercial item acquisition rules apply to goods and services that are deemed, but are not actually, commercial items.

### **2. Commercial item acquisitions generally**

A commercial item is defined as (1) any item of a type customarily used by commercial entities that has been (or soon will be) offered or sold to the public; or, (2) a service offered or sold competitively in the commercial marketplace based on catalog or market prices for specific tasks performed under standard commercial terms and conditions. FAR 2.101. Under FAR Part 12, an agency may acquire commercial items under significantly reduced competitive procedures designed to mimic, to the extent practicable, rules used in the commercial market. The rationale behind that policy rests in part on the notion that commercial items have been verifiably "tested" by the marketplace, providing an enhanced basis for the government to verify and evaluate contract terms and conditions without a full competition.

There are a number of significant shortcuts available to all executive agencies in the acquisition of commercial items. For example, agencies acquiring commercial items need not obtain cost or pricing data from offerors before awarding a contract, which allows a far more streamlined evaluation and award process and presents a far less imposing burden on companies wishing to do business with the government. In a commercial item acquisition, executive agencies may acquire only the technical data rights that the commercial contractor customarily provides under its commercial license, and must accept a warranty consistent with the contractor's standard commer-

cial warranty. Likewise, many of the standard clauses and subcontract flow-down provisions that are mandatory in federal procurements are either streamlined or made wholly inapplicable to commercial item acquisitions, further reducing the burden on companies wishing to do business with the government. Flexible financing options, including advance and installment payments, also are available in the acquisition of commercial items.

3. DHS's authority to acquire deemed commercial items under streamlined procedures may create large-scale non-competitive acquisitions

The streamlined acquisition procedures available in commercial acquisitions, particularly procedures relating to pricing, data rights, and warranties, function well in commercial acquisitions because commercial items have been subject to competition in the commercial marketplace, which provides a firm, verifiable basis for a streamlined evaluation of both price and product quality. It is not clear, however, how, and to what effect, commercial item acquisition procedures function when applied to goods and services that are not truly commercial items.

For example, a major conflict may arise in the evaluation of pricing with respect to goods and services for which no commercial or catalog pricing is available. Under its special contracting authority, DHS may nonetheless use streamlined price evaluation procedures, which undoubtedly result, in some instances, in the government's paying excessive prices. This is particularly true in the acquisition of deemed commercial research and development (R&D) services for which no comparable commercial service exists. Similarly, conflicts may arise in the govern-

ment's acquisition of warranty rights and product quality assurance. While true commercial items are subject to stringent market scrutiny, items that are merely deemed commercial carry none of the quality assurances of a true commercial item. It is unclear how the government effectively will employ streamlined pricing and quality evaluations in deemed commercial item acquisitions.

Complications also may arise in the acquisition of technical data rights in deemed commercial item acquisitions. In a true commercial item acquisition, the government may acquire only technical data rights that are customarily available under the offeror's standard commercial license. In a deemed commercial item acquisition in which the item in question has never been sold to the public, it is effectively impossible to determine what technical data rights are customarily available under the offeror's standard license. It is unclear how that conflict is to be resolved in practice.

### C. DHS's Dispute Resolution Procedures

#### 1. Protests

As an executive agency, DHS is subject to all statutes and FAR provisions governing dispute resolution procedures. Disappointed bidders or offerors on DHS procurements therefore may file agency-level protests directly with the Contracting Officer as permitted by FAR Part 33 or bring a protest action to the U.S. General Accounting Office or the U.S. Court of Federal Claims. It is important to note, however, that

regardless of the protest forum selected, DHS's special contracting authority and the accompanying streamlined procedures often result in a very deferential standard of review. For that reason, it is very difficult to prevail in a protest of a DHS procurement action.

#### 2. Contract claims

DHS contracts are subject to the Contract Disputes Act (CDA)<sup>6</sup> and the FAR "Disputes" clause,<sup>7</sup> under which contractors must submit contract claims to the agency contracting officer and obtain a "contracting officer's final decision" before an appeal may be brought. Under the CDA, a contractor wishing to appeal a contracting officer's final decision may file an appeal with a Board of Contract Appeals (BCA) or bring an action directly to the U.S. Court of Federal Claims. Although DHS is free to create its own BCA, it is more likely that it will designate an existing BCA to hear DHS appeals, as permitted by the CDA.

### D. DHS's Authority To Enter "Other Transactions"

In 1989, Congress authorized the DOD to enter what are known as "Other Transactions," (OT) a term that encompasses transactions other than traditional contracts, cooperative agreements, or grants. *See* 10 U.S.C. § 2371 (2003). OTs may be used in R&D projects when DOD determines that, to acquire a unique technology or research capability, it is "not feasible or appropriate" to use standard contracting or grant-making procedures. 10 U.S.C. § 2371(e). OT authority gives DOD access to

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technologies and research capabilities that would be otherwise unavailable through standard procedures. Although OTs are exempt from nearly all the procurement statutes, including the competition requirements of CICA, the cost and pricing requirements of TINA, and the government rights in data provisions of the Bayh-Dole Act,<sup>8</sup> DOD is limited in that it generally may not pay more than “the total amount provided by other parties” to a transaction. *Id.* Congress since has expanded DOD’s OT authority to include the acquisition of weapon and weapon-system prototypes.

Under the HSA, DHS may employ DOD’s OT authority to the same extent and under the same conditions that it is available to DOD. Thus, DHS is authorized to acquire unique, cutting-edge technologies and research capabilities with substantially reduced competition requirements and without requiring extensive government data rights. Just as with DOD, DHS generally is not permitted to pay more than half of the total cost of the OT project. Research entities offering unique technologies and cutting-edge capabilities should be aware of the flexibility available under OT programs.

## II. Government-Wide Emergency Contracting Procedures

The HSA also grants special contracting authority, on a one-year test basis, to all executive agencies in the acquisition of goods and services necessary to combat terrorism. This government-wide contracting authority is triggered when the head of any agency determines that the goods or services to be acquired facilitate in the defense against or recovery from a terror attack or an attack employing a weapon of mass destruction.

In such circumstances, executive

agencies are authorized to use streamlined procedures similar to the streamlined procedures available exclusively to DHS. Executive agencies acquiring anti-terrorism goods or services, therefore, may employ the increased micro-purchase threshold of \$7,500 and increased simplified acquisition threshold of \$200,000 for domestic contracts and \$300,000 for foreign contracts.

Agencies also are authorized to acquire unlimited quantities of anti-terrorism goods and services under modified commercial item procedures. Once the special acquisition procedures have been triggered, any executive agency may acquire unlimited quantities of covered goods using modified commercial item acquisition procedures. Given the potentially unlimited scope of this emergency authority, agencies could conduct large-scale procurements under significantly streamlined acquisition procedures of the HSA’s emergency procedures.

## III. The SAFETY Act

Another significant change in government contracting practices implemented under the HSA relates to third-party liability protections. The Support Anti-terrorism by Fostering Effective Technologies Act of 2002 (“SAFETY Act”)<sup>9</sup> limits third-party liability that may be imposed on contractors providing qualified anti-terrorism goods or services to the government.

### A. Factors To Be Used by DHS in Approving Anti-Terrorism Technology Designations

The SAFETY Act applies only to goods or services that the Secretary of Homeland Security (“the Secretary”) has previously approved as “qualified anti-terrorism technology.” In making that

determination, the Secretary should consider seven factors:

- 1) Whether the product has an established effectiveness or history of use;
- 2) Whether the new technology is available for deployment in existing environments;
- 3) Whether the contractor may face liability that is extraordinarily large or unquantifiable;
- 4) The risk that the contractor would not deploy the new technology in the absence of liability protections;
- 5) The public risk if the new technology is not deployed;
- 6) The nature of the evidence supporting the effectiveness of the new technology; and,
- 7) The potential effectiveness of the new technology in combating terrorism.

HSA § 862.

After considering those factors, the Secretary may approve any product or service as qualified anti-terrorism technology, and, therefore, subject to the protections of the SAFETY Act.

### B. The Protections Available Under the SAFETY Act

First, the SAFETY Act creates a federal cause of action for any claim against a seller of qualified anti-terrorism technology. That provision allows any contractor sued for damages caused by anti-terrorism technology to remove an action against it to federal court and limits the types of damages available in actions against vendors of qualified technology.

Second, the SAFETY Act creates a rebuttable presumption that covered technology is protected by the government contractor defense, which shields contractors from liability for harm to third parties caused in the performance of a

government contract. Under the government contractor defense, a contractor is not liable to a third party for harm caused when the contractor builds a product to specifications approved by the government. While rebuttable, the SAFETY Act's presumption that covered technology is shielded by the government contractor defense creates a strong protection for contractors supplying approved anti-terrorism technology.

Finally, the SAFETY Act caps a covered contractor's liability to the amount of its liability insurance, provided the contractor maintains liability coverage in an amount that is not unreasonably "distort" the contractor's prices to the government. HSA § 864(a).

#### IV. Indemnification Under Pub. Law 85-804

Under the Anti-Deficiency Act, agencies generally may not indemnify contractors against third-party liability. 31 USC § 1341. It is important to recognize that, although the SAFETY Act provides significant limits on a contractor's potential third-party liability, it does not authorize DHS, or any agency, to indemnify contractors.

DHS's indemnification authority instead is instead derived through Public Law 85-804, which allows the President to designate agencies with authority to indemnify defense contractors against harm resulting from "unusually hazardous or nuclear" risks. 50 USC §§1431, *et seq.* In February 2003, President Bush extended indemnification authority under P.L. 85-804 to DHS, but in so doing established a strong preference for use of the SAFETY Act, allowing indemnification only for acquisitions that "could not" qualify for SAFETY Act coverage. While it is not clear precisely how it is determined that a product or service "could not" qualify under the

SAFETY Act, it is reasonable to expect that DHS's indemnification authority under P.L. 85-804 to be used very sparingly.

#### V. Rated Orders and the Defense Production Act

The HSA creates numerous incentives to encourage contractors to make their products and services available to the government on a voluntary basis. It is important to note, however, that the government has the right to compel private companies, even companies without a government contract, to prioritize delivery to the government, even if the prioritization disrupts the company's business. The Defense Production Act, 50 U.S.C. app. §§ 2601, *et seq.*, permits DOD to "rate" order based on various levels of national security or defense priority when necessary to ensure national security or the national defense. Any company that receives a priority-rated order and fails to comply with the priority rating may be subject to civil and criminal penalties.

<sup>1</sup> Pub. L. No. 107-296, 116 Stat. 296 (Nov. 25, 2002).

<sup>2</sup> The Transportation Security Administration (TSA), a Department of Transportation component that was transferred to DHS, continues to use its unique, streamlined contracting procedures. The TSA, which Congress created in 2001 to oversee airport security, is authorized to use the Federal Aviation Administration's (FAA) unique contracting procedures, as modified to suit TSA's needs. The HSA does not address TSA's contracting authority, leaving Congress's original 2001 authorization in force. TSA apparently continues to use its unique, modified FAA contracting procedures, at least as long as it remains a discrete entity within DHS. After two years, DHS may absorb TSA, at which time TSA's procedures no longer will apply.

<sup>3</sup> 41 U.S.C. § 253.

<sup>4</sup> 41 U.S.C. § 254b.

<sup>5</sup> 48 C.F.R. Parts 1-53.

<sup>6</sup> 41 U.S.C. §§ 601, *et seq.*

<sup>7</sup> See, e.g., FAR 52.233-1.

<sup>8</sup> 35 U.S.C. §§ 200-212.

<sup>9</sup> HSA §§ 861-865.



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