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NEWSLETTER

Government Contracts Issue Update

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Top 5 Political Law Issues for Government Contractors in This Election Year

By D. Mark Renaud

As we head into an election year that is already flush with campaign contributions at the federal, state, and local levels, this article summarizes five key limits or restrictions on political donations and campaign finance activities that all government contractors must heed.

Pay to Play Is Here to Stay. The Supreme Court of the United States recently denied cert in a case involving one of the federal pay-to-play rules. Although these rules are not applicable to most non-financial services contractors, the fact is that courts have upheld pay-to-play laws time and time again. Such laws, then, which at the state and local level preclude government contracts when the contractor, its PAC, officers, directors, or certain employees (or even family members) make certain types of contributions, are here to stay and will only continue to multiply. The provisions vary widely by jurisdiction (such as New Jersey, Illinois, and Connecticut), but they are at the intersection of the First Amendment and

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SCA Covered or Not? Special Challenges with IDIQ Contracts

By Craig Smith and Adam R. Briscoe

Federal service contractors face additional challenges when applying the McNamara-O'Hara Service Contract Act (SCA) to indefinite-delivery/indefinite-quantity (IDIQ) contracts. Deciding whether the SCA applies to an order is not always straightforward, especially when the underlying IDIQ contract includes some labor categories subject to the SCA and others that are not. Two Civilian Board of Contract Appeals (CBCA) decisions have drawn focus to these challenges in applying the SCA—and underscore the need to be vigilant in assessing which IDIQ orders, if any, are SCA-covered.

Ordinarily, contractors and contracting agencies each have responsibilities for applying the SCA. U.S. Department of Labor (DOL) regulations and the Federal Acquisition

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government contracts. In order to develop state and local government business with confidence, your contracting firm must establish and maintain a political contribution preclearance program to intercept and avoid any impermissible contributions, and to accurately certify compliance and report as required. Nobody likes the government interfering in fundraising and the campaign finance space, but, given that a successful challenge to pay-to-play rules is less and less likely, staying ahead of the curve with a rigorous compliance program is the only option.

The Contractor Must Provide Guidance When an Executive Fundraises. At the federal level and in many states (especially those with pay-to-play laws), corporate contributions are prohibited. This includes a corporate subsidy of political fundraising organized by an executive. Nonetheless, executives often will want to be politically active and fundraise for candidates or act in a campaign's kitchen cabinet. Absent pay-to-play laws, this is usually fine, but the employing contractor must ensure that the executive follows the applicable campaign finance/ pay-to-play rules and avoids any activity that could give rise to an impermissible corporate in-kind contribution. This includes the use of company client lists, the use of administrative assistant time, charging travel costs to the company, etc. Executives should be briefed on the required rules for their voluntary political activity, and legal and compliance oversight should ensure that the guidelines are followed.

The Ban on Federal Contributions by Federal Contractors Includes Super PACs Too. Federal law prohibits corporate contributions to federal candidates and committees. Federal law also prohibits contributions by federal contractors, regardless of whether the contractors are corporate in nature or not. The symmetry between these laws was broken when the Supreme Court in *Citizens United* permitted corporations to make unlimited independent expenditures and the D.C. Circuit permitted the creation of independent-expenditure (IE) only political committees or super PACs to receive unlimited contributions for IEs. Regular corporations may contribute to super PACs, but federal contractors, given the additional statutory restrictions, may not. The Federal Election Commission over the past few years has handed out several civil penalties for violations of this restriction, so this rule is important to keep in mind. (Similar rules apply to state or local contractors in various jurisdictions.)

Political Costs Are Unallowable. It cannot be stressed enough that political costs, like lobbying costs, are unallowable and may not be charged to the government. Contractors must be meticulous in ensuring that the administrative costs of their PACs and any costs, such as travel, related to handing out PAC or corporate contribution checks are not included in an indirect overhead or G&A pool that is allocated to a government contract. For those who use time cards, employees must be properly trained to charge political and lobbying time to unallowable charge codes. For tax purposes, political costs are also nondeductible.

There Are Permissible Ways for Candidates and Office holders to Visit Your Business Site in Election Years. Most contractors welcome a visit by members of Congress to their business sites. In-state and in-district members of Congress are very happy to make such visits, especially in election years. The big problem in election years, however, is how to avoid such a visit becoming an impermissible corporate contribution. The good news is that the treatment of such a visit will depend on the timing of the event, the audience for the event (all employees, executives only, the public), and the content of the discussion. There are site visits that can definitely occur up until Election Day without any impermissible corporate contribution or, even worse, the dreaded reciprocity obligation with respect to other candidates in the race. Of course, without proper guidance, such an event can bring about federal violations and problems for a preferred candidate.

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Is a FAAP Right for You? Functional Affirmative Action Plans Provide an Explanation, Not an Excuse

By Todd A. Bromberg and Martha G. Vázquez

Doing business with the United States government requires complying with the various laws and regulations administered by the Office of Federal Contract Compliance Programs (OFCCP). One of the more challenging requirements is maintaining written Affirmative Action Programs (AAPs) required under Executive Order 11246, Section 503 of the Rehabilitation Act, and the Vietnam Era Veterans' Readjustment Assistance Act (VEVRAA). While all contractors and subcontractors with more than 50 employees and more than $50,000 per year in government contracts have to maintain AAPs, those contractors are often faced with the problem of fitting their workforce into AAPs that don't quite make sense for the way the company does business. There is, however, an underutilized and poorly understood solution to this problem: the Functional AAP (FAAP).

The traditional 'establishment' AAP. When a company is required to maintain an AAP, the default requirement is that these AAPs are maintained based on establishments. This means that each of the contractor's physical locations (e.g., an office, store, factory) is required to have its own AAP based on the employees in that location. Because of the way the American workforce now operates, a single establishment often has different categories of employees residing within each location. For example, one office may have a sales team, an operations team, service workers, a human resources department, and corporate functions. Typically, these employees will all have to be recorded in one establishment-based AAP, which can lead to the tricky problem of explaining why certain reported numbers, such as salary, have standard deviations over the acceptable levels. The raw differences may be easy to explain—different types of employees are compensated and promoted based on different metrics. For example, a salesman who earns a commission will be compensated differently than a customer service representative, but if those employees are located in one establishment, they could end up being compared to one another. Properly organized job groups can help to abate most of these problems, but ultimately a company with many different functions can still find itself having to provide "excuses" to the OFCCP if an audit turns up wage or employment figures that OFCCP finds unacceptable.

Enter the FAAP. A FAAP is an alternative to the establishment-based AAP that allows the contractor to develop a program organized around functional or business units if such a program is approved by the OFCCP. These units are not typically defined by a physical location, but rather components within a company that operate autonomously in the ordinary course of business across all physical locations. A good example would be a company that has a sales division, members of which are spread across many locations, but all of whom report to one ultimate managing official. Per OFCCP's guidelines, such a unit should also "have identifiable personnel practices or transactional activities specific to the functional or business unit (e.g., applicant flow, hires, promotions, compensation determinations, terminations) that are distinguishable from other parts of the organization's business." In this way, a FAAP allows a company to explain differences between employees, before having to provide an excuse following an audit.

FAAPs are greatly underutilized. Some of this is due to misconceptions about the program; historically, FAAPs had renewal and reporting requirements that made them as burdensome, if not more so, than simply sticking with the default establishment-based AAPs. Due to a revised directive issued in the spring of 2019, however, those burdensome requirements are no more. For example, contractors are no longer required to submit annual updates to the FAAP agreements, which are valid for five years from approval. Further, the application process has been streamlined so that a contractor gets a determination within 60 days of making the request. Another common concern among contractors is that having a FAAP is risky because, in the case of an audit, the OFCCP would have access to more information than it would otherwise. Yet, with an FAAP, the company will have already evaluated how the company works functionally and the OFCCP would have already signed off on those functional groupings.

One area in which the guidelines is not clear are how to structure a FAAP. The requirements for a FAAP are that each business unit must exist and operate independently (e.g., managing official has ultimate responsibility for the decisions made within a functional or business unit), have at least 50 employees, have its own managing official, and have the ability to track

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and maintain its own personnel activity. While many companies have clear functional or business units, for others those divisions may be less clear, or there may be more than one way to divide the company.

A FAAP case study. For example, imagine a company with three lines of business, say an animal feed company (Animal Co.). Animal Co. makes pet food, food for military working-animals, and farm feed from its plants throughout the United States and each type of food product is overseen by the chief food officer (CFO) for the respective product line. Now, Animal Co. has a contract with the federal government to supply pet food to our four-legged and flippered troops worth over $50,000 and has more than 50 employees at each plant, so they need an AAP, but would like to do a FAAP because it would be less burdensome to maintain and better reflect the equal employment goals of the company. All personnel decisions and processes are centralized, although Animal Co. makes hiring decisions for the entry-level positions directly from the plants. While the company could have establishment-based AAPs because each plant has its own managing official and makes hiring decisions, Animal Co. could also organize in a FAAP along the lines of the three types of products it makes, which may better reflect whether the company is achieving its affirmative action goals. For instance, the Washington D.C. plant mostly produces pet food, but also produces a great deal of food for military animals. The entry-level position for both types of food is an Apprentice Cuisinier; however, food for military animals is a highly specialized trade and requires extensive background checks to even come within 20 feet of the secret food formulas. Conversely, anyone who knows how to properly use a measuring cup can make pet food. Thus, the requirements for new hires and Animal Co. could thus meet the requirements for a FAAP by organizing its business units along product lines with the CFOs as the managing officials for each unit, or it could organize itself in traditional establishments. So, what is Animal Co. to do?

Bearing in mind that a FAAP is an opportunity to explain data, rather than excuse it, Animal Co. should use this as an opportunity to work backward and imagine if the company was audited. If many potential problems could easily be explained by how the client does business, then that is how the company should organize its FAAP. For example, Animal Co.'s Apprentice Cuisiniers all have the same job title, yet, the requirements for creating pet food is drastically different from the requirements for creating military working animal food. Thus, while it may appear the positions are comparable, and they would be compared if Animal Co. had establishment-based AAPs, in reality the positions are not comparable, and would likely raise concerns for the OFCCP if included in the same job group. Thus, by working backwards, Animal Co. has discovered that it should organize its FAAP along business lines, which explains any differences that might otherwise have to be excused away.

Conclusion. A FAAP may not make sense for every business, but it certainly is an option that federal contractors and subcontractors should consider, especially now that the OFCCP has eased many of the burdens that previously may have given contractors pause about the program. A FAAP can make it easier for a contractor to comply, and in many ways makes it easier for a contractor to actually accomplish the goals of the OFCCP in promoting equal opportunity because of the flexibility a contractor has for defining its functional or business units. Perhaps more importantly, considering a FAAP puts the company in a position where is must evaluate if it has properly grouped its employees both in terms of job categories and functions so that they accurately reflect what its employees are doing and why. Ultimately, it is better to be in a position of providing an explanation, rather than an excuse.

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Bad Assumptions: GAO Refines Offerors' Due Diligence Obligation to Support Naming an Employee in a Proposal Staffing Plan

By Richard B. O'Keeffe, Jr.

In today's tight job market, with qualified, skilled, and experienced candidates in extreme demand in many fields, proposal writers face a daunting task to assemble the most competitive teams of technical, engineering, scientific, and business personnel for advisory or technical services contract proposal staffing plans. Building and maintaining over the many months or even years that a Government procurement might take requires a great deal of effort, networking, know-how and, in many cases, luck. For a non-incumbent offeror competing in a follow-on procurement, successful staffing plans may require projections about the availability of the existing workforce. It is often reasonable for offerors to assert that they plan to hire some or all of the incumbent workforce if awarded the new contract. But there is a limit to such assumptions. A new U.S. Government Accountability Office (GAO) decision provides a cautionary tale for offerors: If you are going to name a specific person in your proposal, you had better talk to that person first.

In a December 2019 decision, *T3I Solutions, LLC,* B-418034 (Dec. 13, 2019), GAO sustained a protest by the incumbent contractor alleging that the awardee had misrepresented the availability of a specific incumbent employee without having first spoken to the employee. This decision is significant because, in several respects, the challenger's assumptions seem reasonable, but GAO nevertheless found an impermissible "bait-and-switch." Competitors intending to capture incumbent employees for services contracts should understand the rule established in *T3I*, and perhaps consider prudent adjustments to business development practices.

The awardee, Darton Innovative Technologies, Inc. (Darton), won a total small business set-aside procurement to provide courseware development and training services to the Air Force. As part of the Air Force's evaluation of personnel qualifications, the solicitation required offerors to submit "a manning level and personnel mix plan for all workload … to include all instructors, courseware developers and any other required positions." While offerors had to identify proposed personnel by name, there were no key personnel positions and the solicitation required neither the submission of resumes nor of letters of commitment from individuals named in personnel mix plans.

Darton and T3I Solutions, LLC (T3I) submitted proposals in response to the solicitation. Darton proposed a current incumbent instructor, and specifically advised the Air Force in its proposal that the person currently served in that role for T3I. In finding Darton's proposal to be technically acceptable, the Air Force specifically found that the named candidate met the qualifications requirements of the solicitation. T3I protested after a debriefing and demanded corrective action based on a Darton's alleged "material misrepresentation" in naming the T3I employee without a "reasonable expectation that [the] individual would be available for performance." The crux of T3I's protest ground was that Darton had not contacted the instructor before submitting his name, nor did it obtain permission to use his qualifications in Darton's proposal.

Darton insisted that its expectation of the instructor's availability was reasonable. It also noted that its proposal made no specific representation of the instructor's availability, and the solicitation did not require commitment letters for any proposed personnel. Notwithstanding these facts, in T3I's view, this indicated a lack of candor by Darton, and amounted to an improper "bait-and-switch."

GAO agreed that Darton's approach was a "bait and switch" because Darton had not contacted the individual in advance. GAO stated that, even if Darton did have a reasonable expectation of the incumbent instructor's availability, such an expectation would still amount to "speculation [which] cannot reasonably support Darton's inclusion of [the] individual in its proposal." Darton, in GAO's opinion, relied only on a "hope or belief" that it would be able to make good on its representation. It is difficult to see how GAO's apparent concession that Darton had a reasonable basis to believe the individual would be available can be reconciled with GAO's ultimate holding that faulted that reasonable basis as insupportable speculation.

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But in any case, based on this finding, GAO ruled that the Air Force relied on Darton's misrepresentation, and that reliance was essential to finding Darton's proposal to be technically acceptable. GAO determined that established all the elements of a bait-and-switch and warranted corrective action. GAO found that the bait-and-switch here was less egregious than ones involved in other cases, so it did not recommend eliminating Darton from the competition. It did recommend however that the Air Force "reevaluate Darton's proposal, taking into consideration [Darton's] misrepresentations." Not only is Darton's reputation tarnished by the decision, but its award may be in jeopardy.

The *T3I* decision appears to overlook factors that would seem to bolster the reasonableness of Darton's expectation while mitigating any speculative aspect of this element of its staffing mix plan. The contract is small ($2 million–$3.6 million) in a narrow, highly specialized niche (Air Force courseware) inhabited, so it seems, by just two small businesses. Thus, the named instructor would appear to have limited job mobility or incentive to depart the project simply because a new contractor took over from T3I. GAO obviously has a much deeper understanding of the facts, and it appears from the decision that Darton might have done a better job of explaining its conduct. But Darton's conduct might have been more charitably judged.

Nevertheless, this decision should cause contractors to exercise greater caution going forward. At a minimum, offerors should more closely analyze solicitation requirements and instructions to offerors–understanding with greater discernment and care what is required by way of submissions regarding personnel is more important than ever. This case does not concern key personnel, which has its own set of unique issues and risks based on GAO decisions in recent years. But at a minimum, so it would seem for the time being, if an offeror needs to name someone in its proposal, it had better at least talk to the person first, and document the conversation in some form. Such communications, especially when incumbent personnel are involved, are inherently risky and demand a delicate balance of considerations. But we now know that, in cases like T3I, any assumptions of availability without such contact are probably bad assumptions. At best they are improperly speculative and at worst they could be a possible basis for being called out by GAO for engaging in a bait-and-switch scheme.

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False Claims Act: State of the Union

By Roderick L. Thomas, Brandon J. Moss, and Michelle B. Bradshaw

As FY 2019 closed in September 2019, so too did a decade of aggressive False Claims Act (FCA) enforcement yielding $38 billion in total government recoveries. This article summarizes major developments from 2019, highlighting the continued need for government contractors to remain vigilant and maintain strong compliance programs if they want to reduce the risk that they will fall prey to the FCA's dual hammers of treble damages and statutory penalties.

I. Statistics

The U.S. Department of Justice (DOJ) recovered over $3 billion in settlements and judgments under the FCA during FY 2019–a top ten all-time recovery. Far and away, the health care industry remained DOJ's largest target, accounting for $2.6 billion (more than 85%) of the total recoveries. Defense-related matters came next, generating $252 million in recoveries (less than 8.5%). The relator bar continued to flex its muscles last year, with recoveries from non-intervened cases rising from $135 million to $293 million. As usual, *qui tam* actions generated more recoveries than DOJ's original actions ($2.2 billion v. $800 million), which corresponds with relators generally being responsible for filing the majority of FCA actions (more than 81% in 2019). These facts and figures leave no doubt–FCA actions, *qui tam* or otherwise, represent a continued risk for those doing business with the Government.

II. Executive Branch Developments

After issuing **a slew of FCA enforcement policies** in 2018, DOJ gave its pen a modest rest in 2019. The most notable FCA policy pronouncement in 2019 was a re-articulation of its position regarding cooperation credit. Under Justice Manual 4-4.112, DOJ made it clear that disclosure of new and additional misconduct should be "proactive," "timely," and "voluntary." The guidance identifies other forms of cooperation and guideposts for determining cooperation's value. DOJ continues to have discretion to reward cooperation credit. Maximum credit should generally be awarded after "timely self-disclosure… [identification of] all individuals substantially involved in or responsible… full cooperation… [and] tak[ing] remedial steps…." Even more vague, partial credit is appropriate when an entity has "meaningfully assisted." As for quantifying cooperation, maximum credit "may not" cause the Government to "receiv[e] less than full compensation for the losses." Discretion will "most often" be applied with a reduction in "penalties or damages multiple." While this guidance is an improvement from last year's **general cooperation credit policy**, the policy continues to lack some of the details and transparency the defense bar has sought for years.

DOJ's prohibition of using agency guidance documents to create *de facto* obligations, standards, or rights, first articulated in the 2018 **Brand Memo** and then Justice Manual § 1-20.100 were incorporated into two Executive Orders last year. That said, the Executive Orders continue to make it clear that such guidance documents are not irrelevant, as *awareness* of such guidance can still establish "scienter, notice, or knowledge of the law." Justice Manual § 1-20.201.

III. Legislative Branch Developments

In September 2019, staunch FCA champion Sen. Chuck Grassley (R-IA) wrote U.S. Attorney General (AG) Bill Barr expressing concerns about the 2018 **Granston Memo**. The Granston Memo's stated purpose is to guide DOJ decisions regarding its dismissal authority under 31 U.S.C. § 3730(c)(2)(A). While it can be argued that DOJ has used (c)(2)(a) offensively, as a key tool for dismissing cases that could create bad case law, Sen. Grassley expressed concern that the Granston Memo's direction undercut the FCA's purpose. Ignoring the Senator's two-week deadline, AG Barr evasively responded in December, explaining DOJ had used its (c)(2)(A) authority "sparingly" since issuing the Memo. While noting that DOJ "only" filed 45 motions to dismiss between January 1, 2018 and December 19, 2019, it neglected to mention the 45 dismissals in fact represented an uptick in the use of (c)(2)(A). It also did not mention how many relators voluntarily dropped their cases in response to a threatened (c)(2)(A) motion in the wake of the Granston Memo. It remains to be seen whether Sen. Grassley or another lawmaker might put forth legislation amending (c)(2)(A).

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IV. Judiciary Branch

In May 2019, the Supreme Court issued a unanimous decision reflecting an expansive interpretation of the FCA's statute of limitations in **resolving a three-way circuit split**. *See Cochise Consultancy Inc. v. United States ex rel. Hunt*, No. 18-315. It held that relators can use 31 U.S.C. § 3731(b)(2) *even if* the Government declines, and the U.S. official whose knowledge triggers the clock is *not* the relator. But the Court declined to define the operative individual within the Government whose knowledge starts the clock. This decision incentivizes relators to conceal their knowledge from the Government and underscores the importance of discovery into the Government's knowledge of the alleged fraud.

The Supreme Court declined *certiorari* in cases presenting opportunities to resolve other circuit splits: (1) whether the "first-to-file bar" under 31 U.S.C. § 3730(b)(5) is jurisdictional, *see Estate of Robert Cunningham v. McGuire*, No. 19-583; and (2) whether Rule 9(b)'s particularity standard requires a relator's personal knowledge of billing records to allege falsity, see *United States ex rel. Strubbe v. Crawford County Memorial Hospital*, No. 9-225.

Lower federal courts continued grappling with the proper standard for DOJ to dismiss pursuant to (c)(2)(A), an issue thrust to the forefront in the wake of the Granston Memo. DOJ succeeded with 10 of its 11 attempts to dismiss the FCA copycat cases "shell company" whistleblowers brought against drug manufacturers with backing from National Healthcare Analysis Group (NHCA). DOJ had argued the allegations were meritless, burdensome, and contradicted HHS OIG guidance. The district courts granting dismissal either applied the "rational relation" test under *Sequoia Orange Co. v. Baird-Neece Packing Corp.*, 151 F.3d 1139 (9th Cir. 1998) or sidestepped the (c)(2)(A) split by holding DOJ had met *Sequoia Orange* or the "unfettered right to dismiss" standard in *Swift v. United States*, 318 F.3d 250 (D.C. Cir. 2003). The sole denial held DOJ failed to adequately investigate and perform sufficient cost-benefit analysis. *See United States ex rel. CIMZNHCA v. UCB, Inc.*, No. 3:17-cv-00765 (S.D. Ill.). That court noted the statute's hearing requirement would be superfluous if judges had no power. Unsurprisingly, DOJ has appealed to the Seventh Circuit. As courts hash out the appropriate standard, it remains clear DOJ's (c)(2)(A) authority is an effective tool to resolve declined cases, and defendants' litigation avoidance efforts should be guided by DOJ's commitment to the Granston factors.

V. Conclusion

Using past as predicate, there is reason to believe the upcoming "roaring 20s" will continue to be a decade full of FCA enforcement and litigation. For instance, Deputy Associate AG Stephen Cox recently revealed at the 2020 American Conference Institute's Advanced Forum on False Claims and *Qui Tam* Enforcement that DOJ is considering seeking a disclosure of third-party litigation financing (at least to DOJ). Additionally, DOJ's enforcement priorities will continue to include health care (particularly opioids), private equity, customs, antitrust (e.g., Procurement Collusion Strike Force), and cybersecurity. While this year's election may shape the FCA's application at the margins, it is unlikely that the FCA will disappear whether there is a new party in charge, or if the status quo holds–every politician likes to tout his or her commitment to fighting fraud against the taxpayer. As such, those who do business with the Government must remain vigilant–those looking to mitigate their FCA risks would be wise to craft well-tailored compliance programs designed to detect and address fraud.

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Political Intelligence & Government Contracting: Impact of *Blaszczak* Opinion on Insider Trading Prosecutions

By Kevin B. Muhlendorf, Brian Walsh, and Madeline J. Cohen

In *United States v. Blaszczak,* the Second Circuit affirmed the ability of prosecutors to secure insider trading convictions even where they cannot prove that the tipper received a "personal benefit" in exchange for disclosing material non-public governmental information (governmental MNPI). This decision makes it easier for prosecutors to bring insider trading-related charges against current and former government insiders, and the individuals who trade upon governmental MNPI. Whether that results in a significant increase in political intelligence enforcement actions remains to be seen, but government procurement is one area in which the *Blaszczak* decision could result in a new target of insider trading enforcement. This article highlights a new risk "wake-up call" for all parties in the procurement space. Because the government can assert it has a property interest in maintaining the confidentiality of predecisional governmental MNPI, those who create it or have access to it are also at risk for criminal liability if they inappropriately share that information.

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Update on State Secrets Litigation Under the Trump Administration

By Moshe B. Broder

Disputes between contractors and the government, or solely between private actors, arise in the context of classified and sensitive government programs that touch on every aspect of the national security space. Although there are mechanisms for conducting litigation (usually where the government is a party) in a classified setting, the government's authority to assert the state secrets privilege can constrain the nature and scope of such litigation, especially in cases where disputes emerge between private parties (such as prime-subcontractor disputes) involving the government's classified information or programs.

The state secrets privilege is an extraordinary doctrine that, at its core, balances an individual's right of access to the court system with the government's interest in protecting sensitive or classified information from disclosure. The government invokes the privilege sparingly. Since the Supreme Court formally recognized the privilege in *U.S. v. Reynolds*, 345 U.S. 1 (1953), the privilege has been invoked and adjudicated in less than 100 published civil cases. The government is the defendant in most cases, though some disputes are solely between private parties. The privilege has been increasingly invoked in the last several decades, in part because of the central role played by contractors in national security programs and in the war on terror, as well as the significant number of challenges to government surveillance or other counter-terrorism programs.

While the state secrets privilege is relatively uncommon in civil litigation, it has the capability to fundamentally alter the rights and remedies available to litigants. Indeed, even the potential for invocation of the privilege may guide litigation and discovery strategy when suits touch on national security issues.

This article discusses important recent developments in state secrets litigation, including two U.S. Court of Appeals for the Ninth Circuit decisions outlining limits to the privilege's scope and application, and two decisions involving disputes with or between contractors. This article also discusses strategic considerations for state secrets privilege litigation.

Recent Ninth Circuit Decisions

In 2019, the Ninth Circuit decided two notable cases with implications for litigation involving the state secrets privilege. The first case, *Husayn v. Mitchell*, 938 F.3d 1123 (9th Cir. 2019), involved a discovery dispute arising out of a Polish criminal proceeding between a foreign national who was subject to enhanced interrogation techniques by the Central Intelligence Agency (CIA) and two independent contractor psychologists who proposed and developed the interrogation methods. After the government intervened in the case, invoked the state secrets privilege, and moved to quash the subpoena, the district court concluded that discovery could not proceed without risking disclosure of information subject to the state secrets privilege–namely, the roles and identities of Polish citizens involved with a CIA site in Poland.

On appeal, the Ninth Circuit reversed, finding that the district court's "hasty dismissal" overlooked the judiciary's "special burden" to assure that the appropriate balance is struck between protecting national security and ensuring access to the court system. The appellate court required the district court to consider the use of in camera review, protective orders, restrictions on testimony, code names and pseudonyms, and other measures to permit discovery to proceed. The Ninth Circuit, however, left open the possibility for dismissal should the district court find it impossible to disentangle privileged information from non-privileged. As particularly relevant here, the Ninth Circuit found that many of the facts relating to the CIA's detention and interrogation program have been "in the public eye for some years now" or are "basically public knowledge," citing media reports, allegations by non-governmental organizations, and statements by former Polish government officials. The court thus rejected the government's argument that the CIA withholding official confirmation of such facts is "key to preserving an 'important element of doubt about the veracity of the information.'" The court reasoned that the government would not have to take an official position in this litigation, and found that the independent contractors from whom discovery was sought were not "agents of the government," but rather "private parties [whose] disclosures

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are not equivalent to the United States confirming or denying anything." The Ninth Circuit's position on these issues appears to be at odds with prior decisions addressing similar circumstances in the U.S. Court of Appeals for the Fourth Circuit. *See, e.g., El-Masri v. United States*, 479 F.3d 296, 311 (4th Cir. 2007) and *Wever v. AECOM Nat'l Sec. Programs, Inc.*, 2017 WL 5139263, at *5 (E.D. Va. June 15, 2017).

Second, in *Fazaga v. FBI*, 916 F.3d 1202 (9th Cir. 2019), the Ninth Circuit agreed with several district courts in the Ninth Circuit that the Foreign Intelligence Surveillance Act's (FISA) procedures for challenging unlawful electronic surveillance takes priority over the state secrets privilege and the dismissal remedy that may follow from it. As the court explained, while the privilege may have a "constitutional core" or "constitutional overtones," at bottom, it is only an "evidentiary rule rooted in common law, not constitutional law." The Ninth Circuit's decision reflects one important consequence regarding whether the privilege is constitutional law, or, as one court put it, "constitutionally-inspired deference to the executive branch." *In re Nat'l Sec. Agency Telecommunications Records Litig.*, 564 F. Supp. 2d 1109, 1124 (N.D. Cal. 2008).

Recent Disputes Involving Government Contractor Defendants

Two recent or ongoing cases illustrate the range of possible circumstances in which the state secrets privilege can arise in disputes with government contractors. First, in *Al-Shimari v. CACI Premier Technology, Inc.*, No. 8-827 (E.D. Va. 2019), Iraqi citizens alleging they were detained and abused while held in Abu Ghraib filed suit against a contractor that provided interpreter and interrogation personnel to the government. The contractor filed multiple motions to compel discovery from the government, but on three separate occasions, the U.S. Department of Defense (DOD) invoked the state secrets privilege to bar certain discovery. The court found the invocations valid and denied the motions to compel. The contractor then moved to dismiss the case, arguing that the unavailability of evidence meant that it could not meaningfully defend itself against the detainees' allegations, and, in a somewhat unusual procedural posture, the government took no position on whether the excluded information necessitated dismissal. The U.S. District Court found that the case could proceed to trial with the use of appropriate protective measures. The contractor then filed an interlocutory appeal challenging the district court's ruling on this and other grounds, and following the Fourth Circuit's dismissal for lack of jurisdiction, the contractor filed a petition for certiorari in November 2019 seeking the Supreme Court's review. Although the cert petition primarily focused on the District Court's derivative sovereign immunity ruling, it asserted that state secrets "pervading this litigation will

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severely hamper the development of CACI's defense and its examination of the individuals who actually participated in Plaintiffs' interrogations," noting that their identities were all classified and state secrets.

Second, in *Wever v. AECOM Nat'l Sec. Programs, Inc.,* 2017 WL 5139263 (E.D. Va. June 15, 2017), a putative subcontractor sued a would-be prime contractor for breach of contract and fraudulent inducement, alleging that it was unfairly excluded under the terms of a teaming agreement from performing services on a classified government contract to perform aviation services. In that case, the government intervened and moved to dismiss the suit, and the court agreed with the government's position, finding that the litigation could not proceed because all three of the circumstances warranting dismissal were appropriate.

Tips for Contractors Thinking Strategically About the State Secrets Privilege

- Although the state secrets privilege is relatively rarely invoked, contractors must remain mindful of the risk that disputes arising out of classified contracts or programs will be found nonjusticiable. Conversely, contractors should not assume that the state secrets privilege will be invoked and a case dismissed simply because the invocation of the privilege may make certain evidence unavailable. Indeed, the Ninth Circuit in *Husayn* charted a discovery path weaving through privileged information, in part relying on the fact that statements made by contractor personnel would not amount to official government acknowledgments, as well as the fact that certain privileged information was already the subject of public reporting and debate.
- The state secrets privilege is sometimes used strategically. Plaintiffs may attempt to engage in "graymail" whereby the threat of disclosure of classified or privileged information is used as settlement leverage. Conversely, potential defendants may consider the potential for nonjusticiability as a license to use sharp elbows in dealings with others. Ultimately, both plaintiffs and defendants operating in classified environments assume a certain degree of risk that disputes arising out of such programs will be nonjusticiable in the court system because of the state secrets privilege. Parties may mitigate these risks through contract terms and pricing accounting for the risk of nonjusticiability, as well as by dealing with known entities and repeat players in the classified space, who may desire to maintain a positive reputation within industry. Additionally, parties that engage in fraud or sharp dealing with other private parties may risk agency investigation or face suspension of security clearances.
- It is critical to engage with DOJ and the relevant agencies as soon as practicable if there is a possibility that a dispute may implicate privileged information. It may take months for the government to complete its thorough review process. In the interim, it may be advisable to seek a stay, but given that there is no guarantee one will be granted, additional litigation expense will be incurred and litigation positions may worsen while DOJ decides what position it will take.
- Cleared counsel, whether in-house or outside, may be best positioned to assist in determining the risk of nonjusticiability or likelihood of dismissal under the state secrets privilege. While potentially privileged information may be dispersed throughout a record, little of it may be necessary for potential claims or defenses, and much of it may be segregable from the non-privileged evidence. Cleared counsel can conduct an investigation and provide guidance as to the legal relevance and necessity of the potentially privileged information.

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Undefinitized Contract Actions: What Contractors Should Be Aware of Before Agreeing to Perform With Key Terms Undefined

By J. Ryan Frazee

Undefinitized contract actions (UCAs) provide agencies with necessary agility to meet urgent needs, and contractors with an opportunity to lean forward and build customer confidence. But by their nature, UCAs are also prime candidates for later frustration. This article explores the potential pitfalls of UCA risks that could lead to future contract disputes. Each UCA arises in different circumstances, and so a smart risk in one case may be a bad bet in another. But no matter the circumstance, there are some issues every contractor should consider before entering into a UCA.

What are UCAs and why are they risky? UCAs are contracts where the contractor agrees to perform but the parties leave certain key terms undefined for future negotiations. UCAs are generally only awarded in pressing circumstances, where time simply does not permit parties to fully negotiate terms. Because they are merely an agreement to agree, UCAs expose contractors to significant risk if a final agreement proves unattainable. The high-pressure environment that made the UCA necessary in the first place may also cause the parties to move forward with sharply different ideas of how negotiations will or should proceed. And during those negotiations, the government maintains substantial negotiating leverage because it can unilaterally definitize the terms in the absence of an agreement.

What terms make sense for you to leave undefinitized? Agencies have significant discretion regarding what terms to leave for further negotiation, and leaving any term undefinitized presents its own risks. The most common term left open is price, but it is by no means the only one that can be. Other examples include minimum order quantities, schedule requirements, performance metrics, and cost/risk allocation, such as insurance or security requirements. But most commonly, UCAs arise where parties can agree on just about everything other than price/fee, with the government needing more time to determine that the contractor's price is fair and reasonable. And no matter the term, before committing to work the details out later, there are a few key questions that will help determine if it is a smart bet.

First, consider how far apart you are. This will be an obvious indicator on whether future negotiations can be productive enough that a UCA makes sense. Contracting officers should be able to provide a ballpark idea of where they are, or how much they think you should move. A failure to do so, or vague requests for more information without articulating precise concerns, are signs that you may be farther apart than you think and increases the potential for a unilateral definitization.

Second, make sure you can perform under a realistic, "worst case" unilateral definitization. While it may seem inconceivable that the government would want to definitize at less-than-cost, or leave you with a commercially untenable requirement, consider whether you are so far apart in your conception of what the performance entails that the contracting officer may deem many of your rationales behind your proposal (and, thus, the costs you incur) to be irrelevant for definitization purposes.

A third and related question is whether there should be a provisional term. For example, with an undefinitized price, agreeing to provisional rates can help with cashflow, and for better or worse, may "anchor" later negotiations. But contractors also are at risk of a government claim if the later-definitized rate is lower than the provisional one. Depending on which side of the provisional rates definitization seems likely to land, it may be wise to maintain adequate reserves to ensure sufficient working capital should the government attempt to collect an alleged overpayment—but doing so also means diverting money away from investing in your business on this or other contracts.

Is there a common understanding for the *basis* of the negotiation? UCAs are typically vague on what the negotiations will be based on, which can lead each party to assume different criteria will control and is a sure way for negotiations to break down.

The most common area for disagreement is whether a contract "price" will be negotiated based on the

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contractor's subsequent actual costs–a common government tactic that may betray the parties' up front pricing negotiations. Agencies can have "profit anxiety," or the belief that a high profit margin means they got a bad deal. So it is not uncommon, even in a commercial item environment, for the government to revert to a cost-plus mindset when negotiating price. And if the contracting office is one that has historically analyzed contracts through a FAR Part 31 lens, the risk is even higher that the parties will be talking past each other. It is counterintuitive, but government negotiators may be so reticent to pay a price that yields a high profit margin that an agency would rather pay an overall higher price with lower margins, than a lower price with higher margins earned through contractor ingenuity and efficiencies.

The best way to head this off is to reach an understanding up front and in writing on what factors the parties should consider during the negotiations, which can go a long way to avoiding an impasse down the road. Although it is rare to see, there is no reason why the UCA, or contemporaneous letter or email, cannot identify the criteria and relative weight that will guide negotiations. Identifying what costs, if any, will be considered, how they will be allocated and evaluated (and under what standards and by whom), and the importance of a price analysis of comparable services can help set guiderails that focus the negotiations and make them more productive.

Is there a common understanding for the *schedule* for negotiations? The UCA regulations contemplate generally bringing the definitization to conclusion fairly quickly, and each UCA must also include a definitization schedule. But agency heads have authority to waive the schedule if the services are necessary to for certain urgent operations, and in practice, it is not at all unheard of for a definitization schedule to push to the right. Before signing up for a UCA, contractors should consider whether they will be comfortable performing under the interim terms for longer than the definitization schedule would suggest. Contractors should also be ready for quick-turn agency requests, if agencies delay in providing feedback on contractor proposals, but nonetheless try to stick with the original schedule.

Contractors should also be mindful of the substantive impact an extended schedule can have on the definitization. As performance continues, initial risk to the contractor materializes into the actual cost of performance, and contracting officers are required to consider any such reduced risk when determining a reasonable profit. In practice, there is an undeniable temptation to effectively convert a fixed-price effort into a cost-plus one, where the risk to contractors is smaller but so is the reward.

One potential avenue to protect against that risk is to submit a qualifying proposal at the earliest date possible. A recent amendment to the UCA regulations requires agencies to consider the cost risk from the date that the proposal goes in, if definitization goes beyond the 180-day window, to avoid a "bait and switch" in contract type. But this is a relatively new requirement, and it is not clear how it will play out in practice. Agencies have not historically shown comfort in pricing risk, so it is unclear whether or how they will be able to do so after the fact when that risk has materialized (or not), at least in part, as actual cost.

Are you comfortable with the risk of unilateral definitization? No one agrees to a UCA with the expectation that negotiations will fail. But due to funding constraints, insurmountable differences of opinion, or other reasons, it happens–and contractors should be cognizant of the risks they are undertaking when agreeing to a UCA.

A unilateral definitization is not the final word, but it is the last word before things become costly and complicated. To challenge a unilateral definitization, contractors typically must proceed through the disputes process, ultimately raising the issue to federal court or a board of contracts appeals, both of which are lengthy, costly avenues. In the meantime, the contractor has a duty to continue performing at a unilaterally definitized price. Moreover, if the government is claiming an overpayment based on its definitization (not uncommon), agencies can claw back the putative overpayment by offsetting it against payments under the UCA, or even separate contracts. This means that even if you ultimately prevail on an appeal of the unilateral definitization, there may be significant

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The Year of the Supplemental Protest

By Gary S. Ward

Several years ago, as debates over the bid protest process were heating up, we started to take a deeper, data-driven dive into the GAO bid protest caseload. Although GAO's annual reports are useful tools for tracking how GAO's caseload has fluctuated over the years or how stable its "effectiveness rate" has remained, they do not provide, in and of themselves, much material for deeper analysis. To more fully analyze protest-related statistics, we started to collect data that GAO publishes daily on its docket. After collecting a full year's worth of data in 2016, we shared several of our notable findings in ***A Data-Driven Look at the GAO Protest System.*** The finding that most grabbed our attention related to the power of a supplemental protest: Of all the cases that GAO decided on the merits in FY16 (in a decision either sustaining or denying the protest), protesters who identified no supplemental protest grounds succeeded in only 12% of the cases, while protesters who filed at least one supplemental protest succeeded in at least 22% of the cases.

We believe this connection is more correlation (protests more likely to succeed tend to be ones where new issues are discovered and pursued) than causation (simply filing a supplemental protest increases a protester's success rate). For example, in many cases, agencies provide offerors with debriefings that give only the slightest peek into their evaluation process and findings. And even when agencies provide robust debriefings, they still cannot disclose their full evaluation record, especially as it relates to the other competitors. As a result, most initial protests rely on limited information about how the agency evaluated the offerors' proposals (and how the agency erred). After all, the documents that most offerors rely on for their initial protests–the debriefing notes and slides–are irrelevant to GAO's ultimate decision, which depends on the contemporaneous evaluation record. Thus, in preparing initial protests, companies do so in significant part so that they can obtain more information and then, with the advice of their outside counsel under the protective order, make a more informed decision about whether to continue to pursue the original protest grounds and any new supplemental protest grounds. By contrast, when protesters prepare supplemental protests, their counsel does so with the benefit of the contemporaneous evaluation record. Thus it is no surprise that protesters tend to be more successful when they raise challenges based on what they discover in the contemporaneous evaluation record (generally supplemental protests) than when they raise challenges to an evaluation record that they

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financial strain during the years spent litigating, over and above attorney fees and other legal costs.

The best way to mitigate the risks of litigating a unilateral definitization is to avoid them in the first place. That means contractors should give careful consideration of the history of the players, including the agency, the contracting office, and the relevant personnel, as well as a sober assessment of the gap between the parties going into the negotiations and any external dynamics that may alter the analysis, before determining that the UCA is worth the risk of a unilateral definitization.

Conclusion. UCAs are both a vital tool for the agencies, and an opportunity for contractors to build trust and confidence in their government partners. But the very factors that make UCAs necessary also make them uniquely susceptible to disputes. Thinking critically and concretely in advance about the risks you are undertaking, and why, can go a long way toward heading off some very common post-execution bumps in the road before your options for dealing with those issues become increasingly limited.

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hope to gain access to during the protest process (initial protests).

In the three years since we wrote our last article on this topic, the differences in odds have fluctuated, but they consistently remain in favor of the protesters who dig into the record and identify supplemental protest grounds. In fact, the data from the most recent fiscal year (FY19), shows this gap is bigger than it has been in any of the last four years. In its latest annual report, GAO reported its third straight drop in sustain rate, most recently from 15% (for cases closed in FY18) to 13% (for cases closed in FY19). But digging deeper–isolating standalone protests from supplemented protests–shows that protesters who filed supplemental protests in FY19 were more likely to succeed than they were in FY18. The drop in GAO's reported sustain rate has thus been at the expense of those protesters who did not identify any supplemental protests. Looking at protests against all agencies as outlined in the figure below, protesters who filed one supplemental protest experienced at 17% sustain rate (orange line), while those who identified no supplemental protests, experienced a 7% sustain rate (blue line).

This rate, however, can vary by agency. For example, comparing all U.S. Department of Defense (DOD) agencies with all other agencies in FY19 shows that a supplemental protest against a DOD agency will not quite double the protester's odds, while a supplemental protest against a non-DOD agency could multiply the protester's odds by five times.

Of course, not all supplemental protests are equally effective, and probabilities can't make up for a nuanced understanding of each individual case. The lesson here is not that protesters should submit more pleadings, but that they should understand that there is almost always more to learn after the initial protest is filed.

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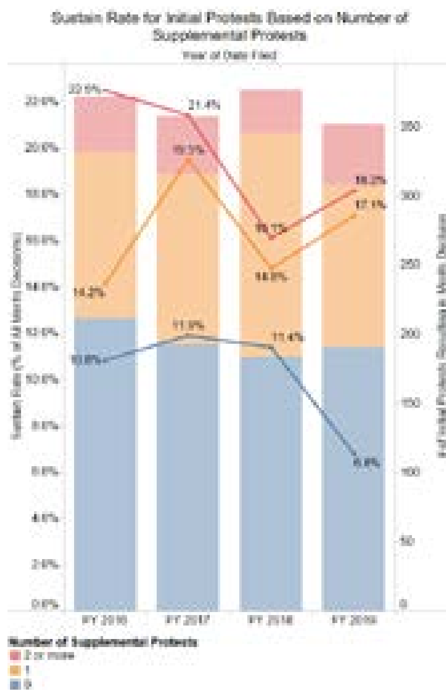

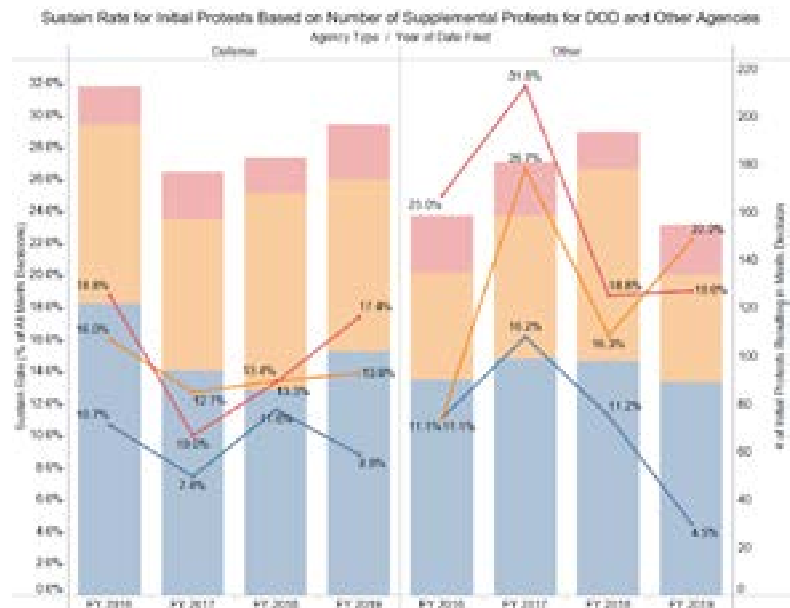

Regulation (FAR) require contracting agencies to determine whether a service contract is covered by the SCA. The contracting agency must refer any questions or uncertainty about SCA application to the agency labor advisor and, if necessary, to the DOL. From there, responsibility shifts to the contractor to identify the appropriate DOL-defined labor categories for their SCA-covered personnel (service employees) and pay at least the corresponding wage rates and prevailing fringe benefits. The CBCA recognized these ground rules in *Sotera Defense Solutions, Inc. v. Department of Agriculture,* CBCA 6029, 6030 (Aug. 29, 2019), a decision we analyzed in a prior newsletter **article**.

These ground rules can be straightforward for many IDIQ contracts. Most notably, the SCA does not apply to contracts "exclusively" or "essentially" performed by bona fide professional, administrative, and executive employees exempt from the Fair Labor Standards Act (FLSA). So some IDIQ contracts, and their resulting orders, will involve only FLSA-exempt or non-exempt personnel—making it clear whether the SCA should apply to individual orders. But other IDIQs might include a mix of FLSA-exempt and non-exempt positions. For orders under these IDIQs, who bears the responsibility to evaluate the labor mix and decide whether the SCA applies to the order? And who bears the risk of cost increases if DOL finds an order was incorrectly treated as not covered?

The CBCA's recent decisions show that the answer may come from the IDIQ contract itself. In *Sotera Defense Solutions*, the contract had a special provision requiring the contracting officer to specify line items for any SCA-covered labor in each task order. See CBCA 6029, 6030 (Aug. 29, 2019). When the contracting officer did not do so for an order, the agency was ultimately responsible for cost increases when DOL ordered the SCA applied to the order.

More recently, a contract H-clause in *Harris IT Services Corporation* required the contractor to notify the agency when task orders would include SCA-covered labor. See CBCA No. 5814, 5815, 5816 (Nov. 1, 2019). Harris did not notify the agency of any SCA-covered personnel for three task orders it had been awarded, but a subcontractor ultimately performed services with SCA-covered personnel on one of the orders. After a DOL investigation, the contracting agency retroactively incorporated wage determinations into the relevant task orders. Harris sought but was denied compensation for these cost increases. Harris argued that the IDIQ contract's H-clause had improperly placed the obligation on the contractor to determine whether the SCA applied to the task orders. The CBCA disagreed, finding that the IDIQ contract had clearly incorporated the SCA obligations, and the H-clause requiring contractor notice of SCA-covered labor "provided an efficient procedure for incorporating wage determinations into the task order in the event the contractor decided to use SCA employees to perform some of the work."

Sotera Defense Solutions and *Harris IT Services* provide timely reminders about how contractors can minimize the risk of noncompliance and unreimbursed costs, as well as claim and litigation costs through proactive contract management:

- **Read the IDIQ and Order Together:** An IDIQ contract's structure adds a layer to contract administration by having two overlapping sets of contract documents imposing obligations on the services being performed. For larger IDIQ contracts, such as GSA Schedule contracts, the contractor team managing the underlying contract may be functionally separate from the team responsible for performing an individual order. But no matter the contract size and team structure, contractors should have a process for reviewing the SCA and labor provisions in the IDIQ and order together. For example, an order awarded without incorporating any SCA clauses could still be SCA-covered if the IDIQ contract incorporates SCA clauses—coverage that may not be apparent from the face of the order documents, alone.
- **Check for SCA Provisions in Unfamiliar Places:** Contractors experienced with SCA-covered contracts will be familiar with the FAR 52.222-41 clause and SCA wage determinations. But *Sotera Defense Solutions* and *Harris IT Services* both involved contract-specific provisions found in Section H of the contract, which is not an area of the contract that traditionally includes standard SCA terms and conditions. Both cases serve as yet another reminder that contractors need to be vigilant of all terms and conditions throughout the contract, including Section H, when assessing

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potential SCA obligations. (Notably, SCA coverage is not the only area in which recent litigation has highlighted nuanced Section H obligations that depart from standard FAR or DFARS clauses incorporated into the contract. For example, other recent cases have highlighted a similar trend involving H-clauses governing rights in technical data and computer software.)

- **Monitor the Order Labor Mix:** Many task orders afford contractors flexibility in selecting the labor mix to perform the required services. When this flexibility allows for performing with SCA-covered or non-covered personnel, contractors must track the mix closely to assess whether the SCA should apply to the order. *Harris IT Services* provides a cautionary example: The SCA-covered personnel worked for a subcontractor, and the record indicates the prime contractor was unaware that covered personnel were performing. Monitoring the labor mix is important in other scenarios as well, such as when contractors green their staffs to help manage labor costs over a multi-year task order—which may involve adding new SCA-covered employees to the project.
- **Be Proactive with the Contracting Agency:** When questions arise as to the applicability of the SCA and wage determinations in either the base contract or task orders, don't try to read the tea leaves. Instead, approach the contracting agency to clarify SCA-related obligations as early as possible. And if the agency's response differs from your analysis of SCA application, notify the agency in writing. Taking these steps can help avoid the costs and administrative efforts to apply the SCA mid-performance and potentially retroactively.

While *Harris IT Services Corporation* and *Sotera Defense* provide examples of who must decide whether the SCA applies to particular orders, contractors avoid having to make these arguments at all by ensuring the contract and performance mix are evaluated comprehensively up front.

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