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COMBATING TERRORISM: CONTRACTING APPROACHES & LESSONS LEARNED

By Marcia G. Madsen, David F. Dowd, and Michael J. Farley

In the wake of the September 11, 2001 terrorist attacks, federal agencies are under pressure to expedite the purchase of products and services needed in the fight against terrorism. Since these attacks, there has been much discussion of whether the procurement system is adequate to obtain the products and services that may be needed to combat all forms of terrorism in the United States or overseas. Are new contracting approaches really needed? What can agencies learn from prior experiences with serious national security needs?

After discussing procurement-related responses to the terrorist attacks, including Department of Defense memoranda instructing Government contracting personnel on the use of nontraditional contracting techniques and recent legislative changes and proposals that bear on the war against terrorism, this BRIEFING PAPER examines procurement practices being advocated or previously undertaken in emergency or urgent situations. The PAPER attempts to identify potential pitfalls for the Government and contractors if, during contract performance, these practices are not properly managed.

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Procurement-Related Responses

■ DOD Memoranda

On September 14, 2001, President George W. Bush declared a national emergency due to the attacks of September 11.¹ On October 9, 2001, the Under Secretary of Defense determined that Operation “Enduring Freedom” meets the statutory definition of “contingency operation,”² which permits the use of all “contingency operations” contracting procedures in the Federal Acquisition Regulation and the Defense FAR Supplement for procurements in support of Operation “Enduring Freedom.”³

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In an October 5, 2001 memorandum regarding "Transition to a Wartime Posture," the Principal Deputy Assistant Secretary (Acquisition and Management) for the Department of the Air Force, Darleen A. Druyun, called upon "acquisition warriors" to rapidly obligate funds appropriated to combat terrorism, stating, "To meet this end, I will support you in the liberal use of Undefined Contract Actions, urgent and compelling Justification and Authorizations, options for increased quantities, accelerated delivery options, etc."⁴

In another memorandum issued October 5, 2001, (Enduring Freedom Memo EF-01-01), Brigadier General Darryl A. Scott, the Deputy Assistant Secretary (Contracting) at the Department of the Air Force, called on Air Force Contracting Officers to be "innovative, even daring risk takers" and to "lean way forward" in meeting customer needs to support the war against terrorism.⁵ General Scott further stated:⁶

During the past couple of weeks I've heard lots of folks say that the FAR and statutes such as the Competition in Contracting Act (CICA) hinder us from responding quickly to warriors' requirements. This is nonsense. In nearly all cases, we have all the authority we need to do the right thing, we just need to *get on with it*....Bottom line...when the circumstances warrant, we've got the tools to speed up the acquisition process to support warriors' requirements.

This memorandum identifies "Techniques for Rapid, Agile Contracting Support," which include the statutory exceptions to the Competition in Contracting Act's "full and open competition" requirement, "Letter Contracts/Oral

Solicitation/Oral Awards," "Oral Change Orders/Verbal Authorization," and "Undefined Contractual Actions," as well as adding options for "Additional Delivery" and "Accelerated Delivery." After a discussion of legislative responses to the September 11 attacks, these contracting techniques are discussed below.

■ FY 2002 Authorization & Appropriations Acts

The National Defense Authorization Act for Fiscal Year 2002 increased the thresholds for micropurchases and simplified acquisitions for procurements to facilitate the defense against terrorism or biological or chemical attack against the United States.⁷ This increase applies to DOD procurements for which funds are obligated during FYs 2002 and 2003.⁸ The micropurchase threshold was increased from \$2,500 to \$15,000.⁹ The simplified acquisition threshold was increased from \$100,000 to (a) \$250,000 for contracts awarded and performed in the United States in support of contingency operations, and (b) \$500,000 for contracts awarded and performed outside the United States in support of such operations.¹⁰ This Authorization Act also included a special provision for the procurement of biotechnology:¹¹

For any procurement of biotechnology property or biotechnology services for use (as determined by the Secretary of Defense) to facilitate the defense against terrorism or biological attack against the United States, the procurement shall be treated as being a procurement of commercial items.

This provision allows biotechnology to be treated as a commercial item even if it does not meet the statutory and regulatory definitions of a "commercial item."¹² In addition, the Defense



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Appropriations Act for 2002 included \$881 million for counterterrorism and homeland defense.¹³

■ **Bioterrorism Act**

On June 12, 2002, President Bush signed into law the Public Health Security and Bioterrorism Preparedness and Response Act of 2002.¹⁴ The Bioterrorism Act charges the U.S. Department of Health and Human Services with developing a National Preparedness Plan to prepare for and respond to bioterrorism and establishes the National Disaster Medical System, a coordinated effort with other agencies to provide health-related services for victims of a public health emergency.¹⁵

The Act requires HHS to maintain a stockpile or stockpiles of drugs, vaccines, and other biological products, medical devices, and other supplies to provide for the emergency health security of the United States in the event of a bioterrorist attack or other public health emergency. It appropriates \$640 million for this effort and \$509 million to ensure the stockpile includes sufficient amounts of the smallpox vaccine.¹⁶ It also requires that the President make potassium iodide tablets available to state and local governments for stockpiling and distribution to public facilities in sufficient quantities to adequately protect populations within 20 miles of a nuclear power plant.¹⁷

The Bioterrorism Act permits the HHS Secretary to designate a priority countermeasure as a fast-track product or as a device granted review priority and includes provisions on accelerated countermeasure research and development and on the evaluation of new and emerging technologies regarding bioterrorist attacks.¹⁸ The Act also enhances controls on dangerous biological agents and toxins, including requiring (1) a list of each biological agent and toxin that has the potential to pose a severe threat to public health and safety and (2) registration to possess, transfer, or use listed agents or toxins.¹⁹ In addition, the Act includes provisions for protecting the food, water, and drug supplies.²⁰

■ **Border Security Act**

Congress also recently enacted Public Law 107-173, the Enhanced Border Security and Visa Entry Reform Act of 2002. Among other things, this Act appropriates \$150 million to the Immigration and Naturalization Service to make improvements in technology for improving border security and authorizes funds to hire and train additional INS personnel and to expand INS and Department of State facilities. The Act includes provisions for interagency sharing of law enforcement and other information and requires that the INS fully integrate its databases and data systems containing information on aliens. It further requires the development of an interoperable electronic data system to provide immediate access to law enforcement and intelligence community databases for information relevant to determine whether to issue a visa or to determine the admissibility or deportability of an alien. The Act also requires that, by October, 2004, the Attorney General and the Secretary of State will issue to aliens only machine-readable, tamper-resistant visas and travel documents and will install equipment and software at all U.S. ports of entry to allow biometric comparison and authentication of all U.S. visas and other entry documents issued to aliens.

■ **Additional Procurement Authorities?**

Are additional procurement authorities necessary for the Government to meet its needs for combating terrorism? On February 27, 2002, the Administrator of the Office of Federal Procurement Policy stated that she was unaware of “substantive evidence” that “points to the need for broad-sweeping legislative changes.”²¹ Nevertheless, legislation has been or may be introduced to assist procurement officials in obtaining products and services to support the war against terrorism. For example, a pending bill seeks to further streamline the procurement process by, among other things, expanding the definition of “commercial item.”²²

■ **Department Of Homeland Security**

On June 6, 2002, President Bush proposed the formation of a new Cabinet Department,

the Department of Homeland Security. Under this proposal, a number of agencies involved in homeland security would be realigned into a single Department, including the Customs Service, Immigration and Naturalization Service, the Coast Guard, the Federal Emergency Management Agency, and the recently created Transportation Security Administration.²³ As outlined by the President, the new Department's mission will require procurement of new technology and services. One question is whether the new Department will be granted procurement authority that is special or different from that which the agencies and entities enjoy in their current Departments. If new authority is granted, the new Department may rely on a mixture of FAR-based procurement practices for existing contracts and contract vehicles (such as multiple award schedule contracts) as well as new authorities.

For example, when created as part of the Department of Transportation in late 2001, the TSA was granted the same exemption from procurement laws and regulations that the Federal Aviation Administration enjoys, at least with respect to products.²⁴ Under its exemption, the FAA has created an Acquisition Management System.²⁵ The legislation that established the TSA mandated that this System "shall apply to acquisition of equipment, supplies, and materials" by the agency, but also permitted the head of the agency to make modifications to the System.²⁶ This exemption, however, does not apply to the acquisition of services.²⁷ As such, the TSA's acquisitions of services are subject to review at the U.S. General Accounting Office, while its acquisitions of equipment and supplies are subject to review under the FAA's Acquisition Management System procedures.²⁸ The same (potentially confusing) duality applies to the substantive law to be applied by the TSA in acquiring products and services—i.e., the FAR applies to acquisitions of services while the Acquisition Management System (as modified by the TSA) applies to acquisitions of products.

It is unclear whether this mixed authority will be retained by the TSA if and when it becomes part of the Department of Homeland

Security or if this mixed authority will be extended to other parts of the new Department. The procurement legislation for the new Department also will need to address whether it will be granted additional procurement flexibility. For example, under the draft legislation prepared by the Bush Administration,²⁹ the new Department would have authority to enter into so-called "other transactions" (OTs)—transactions other than contracts, grants, or cooperative agreements for research or prototype projects—which are discussed below.³⁰

Acquisition Vehicles & Techniques

Regardless of whether additional legislation is enacted to augment procurement authorities, there likely will be renewed interest in, or an increased use of, existing contract vehicles and techniques to support the war against terrorism. A number of these are discussed below. Lessons learned from prior uses of these vehicles and techniques may enable the contracting parties to avoid prior mistakes.

■ **Undefinitized Contract Actions**

An undefinitized contract action (UCA) is any contract action for which the contract terms, specifications, or price are not agreed upon before performance has begun. Examples include letter contracts, orders under basic ordering agreements, and provisioned item orders.³¹ UCAs should be used only when (a) the negotiation of a definitive contract is not possible in time to meet the Government's requirements, and (b) the Government's interest demands that the contractor be given a binding commitment so that performance can begin immediately.³²

UCAs include a not-to-exceed price. The Government may not obligate more than 50% of the not-to-exceed price before definitization (unless a qualified proposal is submitted before reaching this 50% mark, in which case, the limitation on obligation before definitization is 75%).³³ The head of an agency may waive these limitations, however, if the agency head determines that the waiver is necessary to support a "contingency operation" or a "humanitarian or peacekeeping operation."³⁴

The UCA must contain a schedule for definitization by the earlier of (1) 180 days after issuance of the action (unless extended to 180 days after the contractor submits a qualifying proposal), or (2) when the amount of funds obligated under the contract action is equal to more than 50% of the not-to-exceed price.³⁵ Submission of a qualifying proposal in accordance with this schedule is a material term of the contract. If the contractor does not timely submit a qualifying proposal, the CO may suspend or reduce progress payments or take other appropriate action.³⁶

Because they involve relatively little work before performance begins, UCAs increasingly may be used to combat terrorism. Agency heads may be willing to waive the limitations on obligations and price ceilings, either on a contract-by-contract basis or more broadly. For example, the Air Force has issued a broad waiver of these limitations. As noted above, the Air Force is encouraging “liberal use of Undefined Contract Actions.”³⁷

Moreover, on November 28, 2001, General Scott issued another “Enduring Freedom” Memo.³⁸ This memorandum provides that Operation “Noble Eagle” (U.S. military operations in homeland defense and civil support to federal, state, and local agencies in the United States) meets the statutory definition of a “contingency operation,” based on the same rationale used in declaring Operation “Enduring Freedom” (the name for the operation against terrorism outside the United States) a contingency operation.³⁹ For the Air Force, General Scott waived regulatory provisions regarding the definitization schedule and the limitations on obligations for UCAs that support Operations “Enduring Freedom” and “Noble Eagle.” Under this waiver, the Air Force may obligate up to 75% (rather than 50%) of the not-to-exceed price before definitization, unless a qualified proposal is submitted before reaching this 75% mark, in which case, the limitation on obligation before definitization is 90% (rather than 75%) and may obligate up to 100% “under exceptional circumstances.”⁴⁰ The memorandum cautions that UCAs are not the “normal means of conduct-

ing business” and should be used only “when the negotiation of a definitive contract action is not feasible to meet our requirements.”⁴¹

While UCAs may be an effective tool, their use raises some questions. For example, it may be unclear what terms and conditions apply if the parties are unable to reach agreement or if a dispute arises before the contract is definitized. As a practical matter, moreover, the circumstances that warrant use of the UCA also contribute to slips in reaching the 180-day target for definitization. Furthermore, the contractor bears the risk that an authorized Government official does not order in haste to get the order fulfilled. Under such circumstances, could the definitization constitute ratification? The Anti-Deficiency Act prohibits Government officials from incurring obligations in excess of the funds available or in advance of appropriations.⁴² Improperly managed UCAs run the risk of violating this statutory prohibition. Finally, the “Limitation of Cost” and “Limitation of Funds” contract clauses⁴³ also must be considered. Particularly under these circumstances, contract needs that give rise to UCAs might be more likely to expand or change in unforeseen ways.

A number of cases that have addressed issues related to UCAs provide some useful lessons. For example, in one case, the contractor had entered into an “Advanced Acquisition Contract” with the Navy, requiring it to deliver two F404 demonstrator and ten pilot engines. This contract gave the Navy the option to purchase 90 production engines, which the Navy exercised. The contractor claimed that the Navy breached the contract by (a) refusing to definitize the contract price in accordance with an investment incentive clause in the contract, (b) repeatedly attempting to “ratchet” its engine prices down by ignoring established overhead rates, pressuring contractor to be competitive with prevailing General Electric Company (which had been the Government’s sole-source) engine prices, and threatening to end the program, and (c) unnecessarily prolonging negotiations in definitizing the contract. The Armed Services Board of Contract Appeals found that the facts sup-

porting the contractor's claim for breach in connection with definitizing the contract predated and were known to the contractor when the parties' senior officers negotiated a settlement. The contractor accepted the negotiated price and an accelerated tooling recoupment schedule and subsequently signed a definitized contract without any reservation of claims. The ASBCA held that, under the circumstances, the contractor had waived its breach claims arising out of the definitization of the contract. It also faulted the contractor for not reserving its claim. Because the contractor failed to reserve its claims based on events occurring before definitizing the contract that superseded the Advance Acquisition Contract, i.e., UCA, the contractor's breach claim, arising out of the definitization process, was barred by waiver. The board also held that contractor's breach claim in connection with the definitization of the contract was discharged by accord and satisfaction.⁴⁴

Another case involved a UCA to produce and deliver desert boots during Operation Desert Storm. Before definitization, the contractor had been advised to decelerate deliveries after Operation Desert Storm had ended and there was no longer an urgent need for the boots. In denying the appeal, the ASBCA faulted the contractor for not reserving its claim. The ASBCA found that the contractor failed to reserve its claim for the delay that allegedly affected its production under the UCA in negotiating and agreeing to prices in the definitive contract. Since the definitized contract had the effect of superseding the UCA, it was necessary for the parties to recognize the existence of claims based on events occurring while the UCA was in effect with an express reservation in the definitive contract or an acknowledgment that, notwithstanding definitization, the claims would be a matter for resolution by separate agreement.⁴⁵

In a case involving a cost-reimbursable letter contract for urgent development and production of a "bomblet" for use in Vietnam, the Government intended to eventually negotiate a cost-plus-incentive-fee contract, but the contract was never definitized due to doubts about the performance of the bomblet. There was a

"Limitation of Government Liability" provision in the letter contract, but the Government had the right to, and did, require performance after the cost limitation was exceeded, subject to eventual definitization of a contract or determination of a reasonable price under regulations pertaining to a termination for convenience. The ASBCA found that, during performance, the Procuring CO had no intention of relying on the limitation after the initial amount was exceeded. Citing cases involving the well-established principles of waiver of cost limitations in "Limitation of Cost" clauses of cost-reimbursable contracts where the Government continues to order despite knowledge that the limitation has been reached, the ASBCA held that the Government thus had waived the cost limitation of the "Limitation of Government Liability" clause.⁴⁶

■ Other Than Full & Open Competition

The Competition in Contracting Act requires agencies to obtain full and open competition in conducting a procurement for property or services.⁴⁷ CICA provides a number of exceptions to its full and open competition requirement.⁴⁸ Each is discussed in turn.

(1) *Only one responsible source and no other supplies or services will satisfy agency requirements.*⁴⁹ Full and open competition need not be conducted when the required supplies or services are available from only one responsible source (or, for the DOD, the National Aeronautics and Space Administration, and the Coast Guard, from only one or a limited number of responsible sources), and no other type of supplies or services will satisfy agency requirements.⁵⁰ Supplies or services may be considered to be available from only one source if the source has submitted an unsolicited research proposal that (a) demonstrates a unique and innovative concept or demonstrates a unique capability of the source to provide the particular research services proposed, (b) offers a concept or services not otherwise available to the Government, and (c) does not resemble the substance of a pending competitive acquisition.⁵¹ In addition, supplies may be deemed to be available only from the original source in the case of a follow-on contract for the

continued development or production of a major system or highly specialized equipment when it is likely that award to any other source would result in (1) substantial duplication of cost to the Government that is not expected to be recovered through competition, or (2) unacceptable delays in fulfilling the agency's requirements.⁵² In the case of the DOD, NASA, and the Coast Guard, services may be deemed to be available only from the original source in the case of follow-on contracts for the continued provision of highly specialized services when it is likely that award to any other source would result in (a) substantial duplication of cost to the Government that is not expected to be recovered through competition, or (b) unacceptable delays in fulfilling the agency's requirements.⁵³ Contracts awarded using this authority must be supported by the written justifications and approvals (J&As) described in FAR 6.303 and 6.304.⁵⁴ For contracts awarded using this authority, the notices required by FAR 5.201 (synopses of proposed contract actions) must be published and any bids and proposals must be considered.⁵⁵

(2) *Unusual and compelling urgency.*⁵⁶ Full and open competition is not required when an agency's need for the supplies or services is of such an unusual and compelling urgency that the Government would be seriously injured unless the agency is permitted to limit the number of sources from which it solicits bids or proposals.⁵⁷ This authority applies in those situations where an unusual and compelling urgency precludes full and open competition and delay in award of a contract would result in serious injury, financial or other, to the Government.⁵⁸ Use of this authority must be supported by a J&A, but it may be made and approved after contract award if doing so before award would unreasonably delay the acquisition.⁵⁹ Agencies must request offers from as many potential sources as is practicable under the circumstances.⁶⁰

(3) *Industrial mobilization; engineering, developmental, or research capability; or expert services.*⁶¹ Full and open competition need not be conducted when it is necessary to award the contract to a particular source or sources, among

other things, to maintain a facility, producer, manufacturer, or other supplier available for furnishing supplies or services in case of a national emergency or to achieve industrial mobilization.⁶² Use of this authority may be appropriate when, among other things, it is necessary to (a) keep vital facilities or suppliers in business or make them available in the event of a national emergency, (b) train a selected supplier in the furnishing of critical supplies or services or prevent the loss of a supplier's ability and employees' skills, (c) maintain properly balanced sources of supply for meeting the requirements of acquisition programs in the interest of industrial mobilization, (d) limit competition for supplies or services approved for production planning under the DOD Industrial Preparedness Program to planned producers with whom industrial preparedness agreements for those items exist or who agree to enter into industrial preparedness agreements, (e) create or maintain the required domestic capability for production of critical supplies by limiting competition to items manufactured in the United States or the United States and Canada, (f) continue in production contractors that are manufacturing critical items when there would otherwise be a break in production, or (g) divide current production requirements among two or more contractors to provide for an adequate industrial mobilization base.⁶³ Contracts awarded using this authority must be supported by a written J&A.⁶⁴

(4) *International agreement.*⁶⁵ Full and open competition is not required when precluded by the terms of an international agreement or a treaty between the United States and a foreign government or international organization or the written directions of a foreign government reimbursing the agency for the cost of the acquisition of the supplies or services for such government.⁶⁶ Except for the DOD, NASA, and the Coast Guard, a contract awarded using this authority must be supported by a written J&A.⁶⁷

(5) *Authorized or required by statute.*⁶⁸ Full and open competition is not required when a statute expressly authorizes or requires that the ac-

quisition be made through another agency or from a specified source, or when the agency's need is for a brand name commercial item for authorized resale.⁶⁹

(6) *National security.*⁷⁰ Full and open competition need not be conducted when the disclosure of the agency's needs would compromise the national security unless the agency is permitted to limit the number of sources from which it solicits proposals.⁷¹ This authority may be used when disclosure of the Government's needs would compromise the national security, but it may not be used merely because the acquisition is classified or access to classified matter will be necessary to submit a proposal or to perform the contract.⁷² Contracts awarded using this authority must be supported by written J&As.⁷³ Agencies must request offers from as many potential sources as is practicable under the circumstances.⁷⁴

(7) *Public interest.*⁷⁵ Full and open competition is not required when the agency head determines that it is not in the public interest for the particular acquisition.⁷⁶ This authority may be used when none of the other authorities discussed above applies.⁷⁷ A written determination to use this authority must be made in accordance with FAR Subpart 1.7 ("Determinations and Findings"), by the Secretary of Defense, Army, Navy, Air Force, and Transportation for the Coast Guard, or by the Administrator of the NASA or the head of any other executive agency. This authority may not be delegated.⁷⁸ The agency must notify Congress in writing not less than 30 days before award of the contract.⁷⁹ The Determination and Finding (D&F) must not be made on a class basis.⁸⁰

While these seven exceptions are available, agencies may be susceptible to successful *protests* challenging their applicability to particular procurements. The GAO closely scrutinizes sole-source procurements. Some recent examples of protests challenging sole-source or limited competition procurements are summarized below:

(a) A protest of an agency's justification for a noncompetitive, sole-source procurement

on the basis of unusual and compelling urgency was sustained where the agency sought to buy enough engine electrical start systems to replace an earlier, vehicle control unit system that could no longer be used due to safety considerations; the agency did not know, and made no reasonable effort to discover, what quantity was required to meet the agency's immediate needs; and the use of the non-competitive procedure was due to a lack of advanced procurement planning.⁸¹

(b) An agency's proposed award of a sole-source contract for engineering and overhaul services for helicopter engines on the basis that only one firm was capable of meeting the agency's needs was not reasonable where the agency's documentation, including the J&A, the agency's submissions prepared in response to the protest, and agency testimony at the hearing were inconsistent and inaccurate.⁸²

(c) A protest challenging the agency's basis for a sole-source procurement—that only one firm could meet its requirements—was sustained where the record showed that another potential vendor was given an incorrect understanding of the agency's requirement and the agency thus misled the protester about its actual requirements. Agencies must provide potential sources an opportunity to demonstrate their ability to meet the agency's requirements based on an accurate portrayal of the agency's needs.⁸³

■ Other Transactions

OTs—transactions other than contracts, grants, or cooperative agreements for research or prototype projects—are an innovative procurement technique that may be used in the war against terrorism, including by the proposed Department of Homeland Security. Historically, only the DOD has had authority to use OTs.⁸⁴ Although OTs were intended to induce companies that have not done business with the Government to enter into contracts, most OTs have been entered with traditional defense contractors, although under more flexible terms than procurement contracts.

The Defense Advanced Research Projects Agency (DARPA) and the Army recently competed the Concept Technology Demonstration phase of the Future Combat System (FCS) program as a “prototype project” OT, a type of OT which is authorized by § 845 of the FY 1999 National Defense Authorization Act.⁸⁵ OTs are not subject to the statutes and regulations that apply to “procurement contracts,” such as the Contract Disputes Act.⁸⁶ Like other OTs, the FCS solicitation includes an “Alternative Dispute Resolution” clause that calls for the parties to attempt to resolve disputes informally. It requires that any disputes be submitted to a panel of three persons that consists of the DARPA Director (or designee), a senior DARPA Contracts manager, and a senior executive appointed by the contractor. DOD guidance, however, notes that an OT dispute “can be the subject of a claim in the Court of Federal Claims.”⁸⁷ No Court of Federal Claims decisions address disputes regarding OTs.

In some respects, FCS is an expanded use of OT authority. The contractor will serve as a “lead system integrator” for DARPA/the Army. The lead system integrator assesses and integrates technology to network a “system of systems.” The contractor thus is not producing a single prototype or technology, but rather is assisting DARPA/the Army in integrating a series of systems and subsystems, such as armored vehicles, tanks, and unmanned aerial vehicles.

Although Congress has not yet authorized such use, the DOD has for some time been seeking to extend its OT authority to production. Particularly if the war against terrorism continues and requires the application of new technologies, the emphasis on OTs likely will increase. In many respects, OTs offer the Government a means to encourage participation by companies that traditionally have not done business with the Government and to do so more readily and on more flexible terms.

Potential expanded use of OTs raises a question whether a board of contract appeals would entertain a dispute involving an alleged OT. If a contractor brought a claim involving an OT before a board of contract appeals, the

Government likely would contend that jurisdiction is lacking. The contractor, in turn, might argue that the contract is not properly classified as an OT and, as such, must be a procurement contract to which the Contract Disputes Act applies. Although CICA does not apply to OTs, the GAO has reviewed certain types of OTs for the limited purpose of ascertaining whether OT authority properly has been invoked.⁸⁸ A board of contract appeals thus may find itself faced with a novel jurisdictional dispute that may require it to ascertain whether the Government properly invoked OT authority for the agreement at issue. Alternatively, an OT contractor or the Government might request a board to render an advisory opinion to assist in the resolution of a dispute involving an OT.

■ Oral Solicitations & Oral Contracts

Oral solicitations and oral awards are techniques identified by General Scott in Memo EF-01-01. The FAR provides that oral requests for proposals are authorized “when processing a written solicitation would delay the acquisition of supplies and services to the detriment of the Government.”⁸⁹ The use of oral solicitations and awards raise several questions. For example, what are the contract terms and conditions and the statement of work? If there is a dispute, how will or can the parties prove the terms of the contract? What about ambiguities? How is the rule of *contra proferentem* applied? Does the *Christian* doctrine⁹⁰ apply? What is a change? What is the measure of performance? What is the effect of form terms and conditions (such as a “shrink-wrap” license) delivered with a product in response to an oral order?

According to the General Services Administration Board of Contract Appeals, “Complex procurements conducted under oral solicitations are fraught with peril.” When oral solicitations are used, “[t]he potential for miscommunication, misunderstanding, and inequitable treatment of vendors is great, and the likelihood of a resultant improper award is correspondingly large.”⁹¹ In this case, the GSBCA stated:⁹²

Although we are sensitive to the urgency of some procurements conducted under oral solicitations, we reject the application of th[e] proposition [that misunderstandings in oral solicitations must be tolerated unless an offeror was intentionally misled by Government contracting personnel] to the procurement in question here. Procurements made pursuant to oral solicitations must be conducted under the requirements for elemental fairness which statute and regulation impose on all procurements.

Boards and courts have held that, while oral modifications to written contracts are clearly disfavored, there are and might be circumstances that allow a departure from the general requirement for a writing.⁹³ The ASBCA has held that the Government may be bound by an oral contract if the official purporting to enter into that contract has the requisite contract authority.⁹⁴ In one case, the contractor alleged that implied-in-fact contracts resulted from oral agreements made with Government officials. While noting that it was not precluded from enforcing oral contracts, the board decided that it lacked jurisdiction to decide the case because the Government official involved in the oral agreements did not have contracting authority.⁹⁵

■ Contract Modifications

Another technique identified in Memo EF-01-01 is modifying existing contracts. Contract modifications are advantageous because an agency may avoid the need to undertake competitive procedures, but there are significant constraints on an agency's ability to modify contracts.

While CICA requires agencies to obtain full and open competition when procuring property or services, it does not require a new competition for every change to a contract. Only modifications that exceed the scope of the original contract (commonly known as "out of scope" modifications) fall under the statutory competition requirement.⁹⁶ Such modifications either must be competed or meet one of the statutory exemptions to competition discussed above. The "integrity of the competitive procurement system requires the contracting parties not make changes to contracts

which have the effect of circumventing the competitive procurement statutes."⁹⁷ This principle is violated when a modification so substantially changes the purpose or nature of a contract that the contract for which the competition was held and the contract to be performed are essentially different.⁹⁸

CICA does not set forth a standard for determining when a contract modification exceeds the general scope of a contract and thus requires a new competition. In developing a standard, the U.S. Court of Appeals for the Federal Circuit has analogized to the "cardinal change" doctrine.⁹⁹ Under this doctrine, a contractor is not bound by an agency's unilateral contract modification where it "effects an alteration in the work so drastic that it effectively requires the contractor to perform duties materially different from those originally bargained for" by the parties.¹⁰⁰ Just as the cardinal change doctrine prohibits an agency from compelling a contractor to perform contract terms that are not within the scope of the original bargain, CICA prevents an agency from modifying a contract to such an extent that it is "materially different" from the contract for which a competition was held.¹⁰¹

In assessing whether a modification is "out of scope," courts examine whether the contract as modified materially departs from the scope of the original procurement.¹⁰² This inquiry is "primarily an objective one viewed from the perspective of potential bidders for the first procurement."¹⁰³ The relevant factors include the extent of any changes in the type of work, performance period, and costs, as well as whether the solicitation for the original contract adequately advised offerors of the potential for the type of changes that have occurred and whether the modification is of a nature that potential offerors would reasonably have anticipated under the contract's "Changes" clause.¹⁰⁴ This fact-specific analysis is not limited to major cost increases or time extensions.

For example, one court found that a modification was "out of scope" even though it did not involve a substantial increase in obligated funds and did not materially change either

the performance period or the nature of the work.¹⁰⁵ In this case, a modification to a computer maintenance services contract increased the number of performance sites from 6 to 16 and increased the number of “client” entities from a single agency within the Air Force to several agencies within the DOD across all service boundaries. The court pointed out:¹⁰⁶

The “type” of work...and whether other bidders could have anticipated a change in that type, goes beyond merely the physical task itself. In the context of this case, “type” requires an examination of where the work was to be performed, and for whom, and...the degree of flexibility built into the procurement.

Even what may appear to be a minor change may be “out of scope” if the field of competition clearly would be affected by the modification. For example, the GAO sustained a protest where the change was only to the type of paper used in a printing contract. The GAO concluded that the field of competition under a changed specification would have been materially different in view of clear evidence that a number of paper mills could have supplied paper under the changed specification.¹⁰⁷

A change to the form of the contract may constitute a significant change. For example, a change in the form of a contract for disk drives from purchase to a 5-year lease-to-ownership plan, with stringent performance requirements over the lease term, created a new ongoing agreement to support the equipment and was a significant change that should have been competed. The modification exceeded the scope of the contract, the GAO concluded, because the change from the simple purchase of machines to the acquisition of guaranteed service was a significant change in the nature of the thing procured.¹⁰⁸

Even where cost increases and schedule extensions are minimal, a modification may be “out of scope” where it permits a performance approach that was prohibited by the solicitation.¹⁰⁹ In one case, the protester challenged a Navy procurement for, among other things, the design and construction of aircraft generator system test stands, which consisted of different assemblies. The conventional method of opera-

tion was to use two shafts in this assembly but the RFP indicated that this approach was unacceptable. As a result, firms like the protester were compelled to offer high-priced units to meet this operation approach. After award, the Navy modified the contract to permit two output shafts running to the aircraft generator rather than one. The implementation of such changes would result only in a modest cost increase and would have little effect on the overall schedule. The GAO found, however, that the record strongly suggested that proposals submitted on the basis of the modified performance specifications would be significantly lower in price and different in design and delivery schedule from those submitted under the original purchase description and sustained the protest.¹¹⁰

Even where the types of services to be provided under the original and modified contract are nearly identical, a modification may be “out of scope” where the services extend beyond the purpose for which the contract was awarded. For example, the GAO sustained a protest that a task order to provide accounting support services for an agency’s portfolio reengineering demonstration program was outside the scope of the original contract, which was to provide a broad range of accounting support services for the agency’s asset sales program. (The demonstration program was not authorized by Congress at the time the original contract was awarded.) The GAO found that, although the types of accounting support services required under the contract and the task order were quite similar, potential offerors could reasonably anticipate that the ordered services would be limited to the purpose for which the contract was awarded.¹¹¹

Another mechanism to expedite acquisitions without conducting competitions is to modify *expiring* contracts. Such sole-source extensions raise the “out-of-scope” issues discussed above. They also raise additional issues, such as whether the “Changes” clause permits the Government to extend a contract (well) beyond the specified term at existing rates. If the contractor resists a “change” on the basis that it exceeds the scope of the contract, does the “Disputes” clause require the contractor to proceed with

the work anyway pending resolution of the dispute? At a minimum, the Government may demand completion under the terms of a contract of an order properly placed within the term of an indefinite delivery/indefinite quantity (ID/IQ) contract even if performance under the order will not be completed until after the contract term.¹¹²

■ Exercising Options & Adding Options

Contract options are another means to acquire needed supplies or services. A CO may exercise an option only after determining that (1) funds are available, (2) the requirement covered by the option fulfills an existing Government need, (3) the exercise of the option is the most advantageous method of fulfilling the Government's need, price and other factors considered, and (5) the option was synopsized (unless otherwise exempted).¹¹³

After considering "price and other factors," the CO must make the determination based on one of several concerns. First, the CO may exercise an option if a new solicitation fails to produce a better price or a more advantageous offer than the option.¹¹⁴ If it is anticipated that the best price available is the option price or that this is the more advantageous offer, the CO should not use this method of testing the market.¹¹⁵ Second, the CO may exercise an option if an informal analysis of prices or an examination of the market indicates that the option price is better than prices available in the market or that the option is the more advantageous offer.¹¹⁶ Finally, the CO may exercise an option if the time between the award and the exercise of the option is so short that it indicates the option price is the lowest price obtainable or the more advantageous offer, when considering factors such as market stability and the usual duration of contracts for such supplies or services.¹¹⁷ The "other factors" to be considered in determining whether to exercise an option include the Government's need for continuity of operations and the potential costs of disrupting operations.¹¹⁸

The Government is not required to inform the contractor when it does not intend to ex-

ercise an option.¹¹⁹ In one case involving a contract for aerial surveys, the contractor claimed costs incurred in acquiring and modifying an aircraft that had not been amortized by the time the Government declined to exercise an option. The contractor maintained that the agency had a duty to disclose the fact that it was attempting to acquire another aircraft. The contractor argued that knowledge of this fact would have affected its decision to submit an offer. The board denied the claim, stating as follows:¹²⁰

[U]nder settled principles governing option contracts, the contractor that amortizes fixed costs over a period that includes option years assumes the risk that these costs will not be recovered if the Government, for some reason, does not exercise the options. Regardless of whether the likelihood of obtaining a substitute aircraft for option periods was remote or reasonably certain, the Government was not obligated to disclose to [the contractor] that it might not exercise the options. This is obvious on the face of the solicitation and the risk that options might not be exercised is inherent in the terms of the contract. This risk is unequivocally assigned to the contractor and is akin to the risk, under an indefinite delivery indefinite quantity (IDIQ) contract, that quantities above the guaranteed minimum might not be ordered.

The interaction of options and the "Disputes" clause raises interesting questions regarding the Government's ability to obtain supplies and services. In one case, the contractor maintained that (a) the Army failed to timely exercise an option and (b) even if the exercise was timely, the option was improper because it required a delivery rate not included in the option clause. The contractor filed suit at the Court of Federal Claims, which ruled that the option was timely exercised and that, while it included the wrong delivery rate, the option was validly exercised. On appeal, the Federal Circuit ruled that, while the option was timely exercised, the determination of the delivery rate was "an impermissible construction of the contract" and the agency thus did not validly exercise the option. The court held, however, that the contractor had a duty to perform the option under the "Disputes" clause "until and unless it obtained a court order excusing it from its performance obligation."¹²¹ The court ruled that the contractor was obli-

gated to perform at the rate established by the lower court “absent reversal or interim relief” from the court.¹²²

As noted earlier, in Memo EF-01-01, the Air Force has identified adding options, including for “accelerated delivery,” as techniques to be employed in the war against terrorism. Adding options raises a number of issues for the contracting parties to consider, some of which are similar to those related to modifications of expiring contracts. For example, may an added option act as an accord and satisfaction waiver of all contractor claims for increased costs related to the extension? What if the option is not priced, *i.e.*, undefinitized? In the case of accelerated delivery, could there be “unabsorbed overhead” if the schedule slows down? If the schedule accelerates, could there be significant costs that might not be recovered if the contract ends earlier than planned? May the Government terminate the contract for default if the contractor does not meet a unilaterally established schedule?¹²³

■ Multiple Award Task & Delivery Order Contracts

The Federal Acquisition Streamlining Act of 1994 authorized the use of multiple award task and delivery order contract vehicles.¹²⁴ Under this method, agencies award two or more contracts under a single solicitation, effectively prequalifying a group of contractors. The agency then awards task orders (for services) or delivery orders (for products) after giving the various contractors a “fair opportunity” to be considered.¹²⁵ Orders may not be protested, except on the basis that they increase the scope, period, or maximum value of the contract.¹²⁶ For example, the GAO found that a task order for management support services exceeded the scope of a multiple award ID/IQ contract for noncomplex integration services where the work required by the task order was materially different from the scope of work set forth or reasonably contemplated under the contract.¹²⁷

These contract vehicles are attractive to acquisition officials because they permit continu-

ing competition among the existing contractors for specific orders and allow the agency to rapidly acquire needed goods or services from a small field of qualified contractors. Concerns have been raised, however, as to whether agencies are properly using these vehicles. The DOD Inspector General recently noted that contracting organizations often direct orders to selected sources without providing all contractors a fair opportunity to be considered.¹²⁸ The IG found that 304 of the 423 task orders examined (72%) were awarded on a sole-source basis or directed-source basis, and 264 of those 304 task orders were improperly supported.¹²⁹ The IG noted that, as a result, the DOD was not obtaining the benefits of sustained competition and the reduced costs envisioned when Congress provided the authority for multiple award contracts.¹³⁰ Only 119 of 423 task orders were competed and only 82 (69%) of these orders received multiple bids.¹³¹

■ GSA Schedules

Another vehicle likely to be more frequently used as a result of the war against terrorism is the Federal Supply Schedule program. The FSS program, which is directed and managed by the General Services Administration, provides federal agencies with a simplified process for obtaining commonly used commercial supplies and services at prices associated with volume buying.¹³²

Schedule contractors provide over four million commercial off-the-shelf products and services. The GSA Schedules offers an array of brand name products from information technology (computer) hardware to laboratory equipment, as well as an extensive range of professional services, including management, financial, engineering, and accounting services.

Schedule purchases are deemed to have been conducted under “full and open” competition if participation in the FSS program was open to all responsible sources and orders under the program result in the lowest overall cost alternative to meet the Government’s needs.¹³³ When placing orders under Schedules, ordering offices are not required to seek further com-

petition, synopsise the requirement, or make separate determinations of fair and reasonable pricing.¹³⁴

Increased use of the GSA Schedules will raise a number of issues. For example, increased use of Schedule buys may lead to more protests and possibly restrictions or limitations on how agencies acquire products and services off the Schedules. Although agencies are not required to conduct a competition before ordering supplies or services off the Schedules, they may do so. Such competitions must be reasonable and consistent with the solicitation terms.¹³⁵ Agencies must act reasonably and treat vendors fairly when purchasing products or services off the Schedules.¹³⁶ For example, in one competition under the FSS program in which the solicitation stated that award would be made on a best value basis and that technical factors were more important than price, the GAO found that the agency improperly selected a vendor based on its technically acceptable, lowest-priced quote.¹³⁷ Where the FSS contains services priced at hourly rates, merely comparing competing vendors' hourly rates, without regard to the hours or the mix of labor categories to be used by the different vendors, is an inadequate indicator of which solution offers the lowest price.¹³⁸

Increased use of the GSA Schedules also may result in more disputes. Disputes under Schedule contracts have presented unique issues.¹³⁹ Although the ordering agency administers and pays invoices, a contractor may have to pursue a claim with the GSA. Under recent rule changes, for disputes pertaining to the performance of orders under a Schedule contract, the ordering office CO may issue a final decision or refer the dispute to the Schedule CO, while only a Schedule CO can issue a final decision on a dispute pertaining to the terms and conditions of a Schedule contract.¹⁴⁰ It may be difficult to determine whether a dispute arises from the performance of the order or whether it pertains to the terms and conditions of the Schedule contract. Thus, the result may still be a "pit of bureaucratic quicksand."¹⁴¹ In the past, contractors often submitted claims to the wrong agency, requiring boards to dismiss subsequent appeals for lack of jurisdiction.¹⁴² Even

under the new rules, appeals from decisions issued by Schedule COs must still be brought to the GSBCA rather than the board for the agency that placed the order, which may be different. The GSA—rather than the ordering agency—is the respondent in such an appeal, which may lead to difficulties (and increased expense) in pursuing the litigation, such as obtaining discovery.¹⁴³

Disputes also may arise over the Industrial Funding Fee, which is paid by customer agencies to fund the GSA's operation of the FSS program. The fee (1% of the total sales) is incorporated into the price charged to agencies and remitted by contractors to the GSA on a quarterly basis.¹⁴⁴

■ Defense Production Act

The Defense Production Act of 1950 enables the Government to shape defense preparedness programs and to take appropriate steps to maintain and enhance the defense industrial and technological base.¹⁴⁵ It authorizes the President (1) to require that performance under contracts or orders (other than contracts of employment) that he deems necessary or appropriate to promote the national defense take priority over performance under any other contract or order, and, for the purpose of assuring such priority, to require acceptance and performance of such contracts or orders (so-called "rated orders") in preference to other contracts or orders by any person he finds to be capable of their performance, and (2) to allocate materials, services, and facilities in such manner, upon such conditions, and to such extent as he deems necessary or appropriate to promote the national defense.¹⁴⁶ The Act immunizes a contractor from liability to third parties arising out of compliance with orders.¹⁴⁷

The President's authority under the Defense Production Act is broad. A contractor has few remedies for displaced work. For example, if the Government requires a manufacturer to expedite delivery of a machine and that order frustrates the sale by the manufacturer of that machine to another party, the Government's order under Act will not constitute a Fifth Amendment taking of the ordered ma-

chine or the contract with the third party, but rather only a frustration of expectations for which damages may not be recovered.¹⁴⁸

■ Economy Act Interagency Acquisitions

If one agency has a contract to provide a product or service that another agency requires, the latter (the “requesting agency”) may obtain the product or service from the former (the “servicing agency”) by way of an interagency acquisition under the Economy Act.¹⁴⁹ Agencies also may place orders between major organizational units within an agency.¹⁵⁰ The FAR prescribes policies and procedures for interagency acquisitions.¹⁵¹ Such acquisitions must be supported by a D&F stating that the use of an interagency acquisition is in the best interest of the Government and that the supplies or services cannot be obtained as conveniently or economically by contracting directly with a private source.¹⁵²

■ Unsolicited Proposals

Companies with innovative approaches or ideas that may be of use in the war against terrorism may make their ideas available to the Government through unsolicited proposals.¹⁵³ Unsolicited proposals allow unique and innovative ideas or approaches that have been developed outside the Government to be made available to Government agencies for use in accomplishing their missions.¹⁵⁴ They are offered with the intent that the Government will enter into a contract with the offeror for research and development or other efforts supporting the Government mission.¹⁵⁵ Offers of commercial items do not constitute unsolicited proposals.¹⁵⁶ Unsolicited proposals must (a) be innovative and unique, (b) be independently originated and developed by the offeror, (c) be prepared without Government supervision, endorsement, direction, or direct Government involvement, (d) include sufficient detail to permit a determination that Government support could be worthwhile and the proposed work could benefit the agency’s research and development or other mission responsibilities, and (e) not be an advance proposal for a known agency requirement that can be acquired by competitive methods.¹⁵⁷

The Government may not use any data, concept, idea, or other part of an unsolicited proposal as the basis for a solicitation or in negotiations with another firm unless the offeror of the unsolicited proposal agrees to such use.¹⁵⁸ This prohibition does not preclude using any data, concept, or idea in the proposal that also is available from another source without restriction.¹⁵⁹ The Government also may not disclose restrictively marked information included in an unsolicited proposal.¹⁶⁰ Contractors thus should properly mark any data submitted in unsolicited proposals.¹⁶¹

■ GWACs

Another potential source for rapidly obtaining products is through Government-wide agency contracts (GWACs). GWACs are a type of ID/IQ contract in which one agency (a “host”) awards the contract but makes it available for use by other agencies (at least to some degree). These vehicles are commonly used for IT products and services.¹⁶² Agencies with major GWAC programs include NASA, the Department of Transportation, the Defense Information Systems Agency, and the National Institutes of Health. An issue for GWACs (especially for recently established GWAC programs) is whether they are subject to the requirements and limitations of the Economy Act, discussed above.

■ Broad Agency Announcements

Another vehicle is the use of a broad agency announcement (BAA), which is one of the competitive procedures available for use in fulfilling the requirement for full and open competition. The competitive selection of basic and applied research and that part of development not related to the development of a specific system or hardware procurement is a competitive procedure if award results from (1) a BAA that is general in nature identifying areas of research interest, including criteria for selecting proposals, and soliciting the participation of all offerors capable of satisfying the Government’s needs and (2) a peer or scientific review.¹⁶³ BAAs often call for short initial responses, followed by full proposals if the responses show merit.¹⁶⁴

BAAs help identify viable candidates for solutions to combat terrorism while avoiding the time and significant opportunity costs involved in standard competitive acquisitions. For example, in October 2001, the Under Secretary of Defense for Acquisition, Technology and Logistics and Combating Terrorism Technology Support Office Technical Support Working Group issued a BAA for capabilities in combating terrorism, location and defeat of hard and difficult targets, protracted operations in remote areas, and countermeasures to weapons of mass destruction. The BAA sought to identify technologies and approaches that provide near-term solutions (12–18 months). More than 12,000 responses were submitted to the BAA.¹⁶⁵ Only a fraction of these are expected to result in contracts.

Indemnification

When presented with considerable potential liability to third parties, contractors may seek indemnification from the Government to cover claims and losses for defined risks. Issues related to the availability of indemnification from the Government to contractors providing products and services to support the war against terrorism are discussed below.

■ Problems Absent Special Authority

The Government generally may not incur obligations in advance of appropriations to cover them.¹⁶⁶ The Government also may not enter contracts for which adequate funds have not been appropriated.¹⁶⁷ Because an indemnification agreement would require expenditure of appropriated funds if the covered contingency were to occur and the Government's liability is indefinite, indeterminate, and (potentially) unlimited, an indemnification agreement constitutes the obligation of funds that have not yet been appropriated.¹⁶⁸ To avoid this concern, the Government may limit any liability assumed under an indemnification agreement to available appropriations.¹⁶⁹ This might be achieved by defining the maximum liability in the agreement (coupled with an appropriation) or agreeing that indemnification will be

subject to available funds with no obligation to appropriate additional funds to cover the contractor's losses.¹⁷⁰ The former approach requires a contractor to agree in advance to limit its coverage for risks that inherently are difficult to define and estimate. The latter approach leaves a contractor unsure what, if any, coverage it ultimately will have. These approaches, therefore, have limited utility—particularly with regard to indefinite risks.

■ Public Law 85-804

Reliance on appropriated funds to cover indemnification thus is not always feasible. As a practical matter, therefore, an agency must have special authority to agree to indemnify a contractor for claims or losses by third parties that arise out of contract performance. The Government has statutory authority to enter indemnification agreements with contractors to cover matters such as nuclear-related work (Price-Anderson Act),¹⁷¹ certain research and development work,¹⁷² and work to “facilitate the national defense.”¹⁷³ The last of these methods is known as “85-804” relief after the Public Law that gave agencies such authority.

The President has designated certain agencies that may exercise 85-804 indemnification authority.¹⁷⁴ The designated agencies include the Departments of Defense, Treasury, Interior, Agriculture, Commerce, and Transportation as well as the GSA, NASA, and FEMA. Following the anthrax attacks in late 2001, the President added HHS to the list.¹⁷⁵

Designated agencies may indemnify contractors for any claim or loss, whether resulting from a contractor's negligence, wrongful act or omission, or otherwise, that arose out of or results from risks defined by a contract as “unusually hazardous or nuclear in nature.”¹⁷⁶ Covered claims include those of third parties (including contractor employees) for death, personal injury, or property losses as well as loss of or damage to contractor or Government property.¹⁷⁷ Claims or losses caused by the willful misconduct or lack of good faith of contractor's directors, officers, or other principal officials are not covered.¹⁷⁸ The agreement to indemnify is reflected by a standard

FAR clause—“Indemnification Under Public Law 85-804”¹⁷⁹—that is tailored to define the covered “unusually hazardous or nuclear risks.”

To support inclusion of the FAR clause¹⁸⁰ in a contract, the contractor must provide certain information to the CO. Among other information, this includes (a) the contract for which the clause is sought, (b) identification and definition of the “unusually hazardous or nuclear risks” for which indemnification is requested, with a statement indicating how the contractor would be exposed to such risks, (c) a statement of all insurance coverage applicable to risks to be defined in the contract as “unusually hazardous or nuclear risks,” including occurrence limits and deductibles, and (d) “controlling or limiting factors” for determining the amount of financial protection the contractor is to provide and maintain, including information regarding availability, cost, and terms.¹⁸¹

If the CO denies the request, the CO promptly must notify the contractor of the denial and the basis.¹⁸² If the CO recommends approval of the request, the CO must forward the request to the head of the agency, along with certain supporting information, including the definition of the unusually hazardous or nuclear risks to which the parties have agreed.¹⁸³ The CO must state whether the indemnification should be extended to subcontractors.¹⁸⁴

In considering whether to approve indemnification and the type of financial protection the indemnified contractor is to maintain, the head of the agency must consider such factors as “self-insurance, other proof of financial responsibility, workers’ compensation insurance, and the availability, cost, and terms of private insurance.”¹⁸⁵

One major challenge in obtaining indemnification under Public Law 85-804 is defining what constitutes an “unusually hazardous” activity. This may be particularly problematic for the war against terrorism. The diverse nature of the threat and the broad range of products that may be used to combat it may strain the notion of an “unusually hazardous” activity. Could the deployment of even commercial products, when used to prevent or mitigate a catastrophic

terrorist attack, be an “unusually hazardous” activity? Particularly in light of the diverse nature of the threats faced, what are the parameters of the unusually hazardous risks? How well can these risks be defined?

If a contractor or the Government believes that certain products to be sold to the Government do not fit within the parameters of 85-804 indemnification either due to the type of product or the agency to which it is sold, another option is to pursue additional statutory authority. Although this approach may be time-consuming, the unique challenges faced by the Government after September 11, 2001 may require new approaches to indemnification.

Government Contractor Defense

If a contractor is unable to obtain 85-804 or other statutory indemnification, it may rely on the “Government contractor defense” when faced with product liability claims that arise out of products supplied to the Government. Contractors that have produced certain products for the Government in accordance with specific Government specifications have been able to take advantage of this special affirmative defense. The potential availability of the Government contractor defense to contractors providing products and services to support the war against terrorism is considered below.

■ Overview

In the landmark *Boyle* case, the U.S. Supreme Court extended the immunity afforded to discretionary governmental functions under the Federal Tort Claims Act to Government contractors, thus protecting them against claims “based upon the exercise or performance or the failure to exercise or perform a discretionary function or duty on the part of a federal agency or an employee of the Government.”¹⁸⁶ A contractor will not be held liable for design defects if (1) the Government approved reasonably precise specifications, (2) the equipment conformed to those specifications, and (3) the supplier warned the Government about dangers in the use of equipment known to the supplier but not to the Government.¹⁸⁷ Although the Supreme Court

initially applied the Government contractor defense to military products, some courts have extended it to nonmilitary products, claims for manufacturing defects, and failure-to-warn claims.¹⁸⁸ The courts are split in these cases, rendering the law somewhat uncertain.¹⁸⁹

For nonmilitary products, in particular, contractors have had difficulty persuading courts to accept the defense. Some courts have held that the defense simply does not apply to such products.¹⁹⁰ Other courts have held that the defense may apply.¹⁹¹ In any event, contractors selling commercial products are unlikely to be able to establish the defense because the Government's role in directing specifications likely will be lacking. On the other hand, the expansion of homeland security—and what constitutes a truly nonmilitary product—may be in a state of flux since September 11, 2001.

While *Boyle* was a design defect case, courts subsequently have recognized that the Government contractor defense may apply to failure-to-warn claims. In some cases involving manuals and alleged failures to warn by the contractor, the contractor was held to be protected by the defense.¹⁹² The nature of the specified warning, however, may make the defense problematic. For example, where the Navy specified the use of asbestos-based cement and was aware of the risks involved, but did not require the provision of warnings to the workers, the U.S. Court of Appeals for the Second Circuit held that the defense did not apply absent greater Government control over the nature and content of the warnings.¹⁹³ It found that that nothing “indicate[d] that the Government controlled or limited the ability of contractors...to warn those who would come into contact with its product.”¹⁹⁴

■ New Limits On the Defense?

In a recent case involving a Blackhawk helicopter crash that resulted in injuries to Army personnel, the Second Circuit imposed what may be a substantial limitation on the Government contractor defense. It held that the defense does not apply to failure-to-warn claims when the warning is to run to the Government (as, in effect, a learned intermediary) rather than the end-users.¹⁹⁵ The court thus limited the defense to the subset of cases in which the warnings are to be transmitted directly to the product end-user.

This decision is problematic for Government contractors. Plaintiffs increasingly have emphasized failure-to-warn theories in product liability claims. Apart from purchases of ordinary consumer products, the duty to warn almost always will run to the Government as a learned intermediary. As a practical matter, therefore, this decision may abolish the Government contractor defense in failure-to-warn cases.

Limitations on the Government contractor defense may have a significant effect on contracts for items to support the war against terrorism, which has military and homeland security components. To the extent plaintiffs can negate the defense, plaintiffs awards or settlements may be larger. Insurance costs may increase in anticipation of the risk. Contractors and the Government will bear the costs of protective efforts that contractors will be forced to undertake to protect themselves from product liability claims. In this regard, contractors should assess their products for all reasonably foreseeable events that could potentially cause harm and document such possibilities to the Government.

GUIDELINES

These *Guidelines*, intended for Government and contractor officials and their counsel, review the contracting techniques discussed in the PAPER under which the Government can obtain supplies and services required to combat terrorism. They recognize the need for expediting the procurement process but

recommend actions based on lessons learned to avoid pitfalls that could arise (either in the form of a protest or a dispute) if such techniques are not properly implemented or managed. They are not, however, a substitute for professional representation in any specific situation.

1. *UCAs*. If feasible, efforts should be made to *avoid* UCAs by reaching agreement on the material terms and conditions in advance, or at least to reach agreement on as many material terms as possible, and to reduce any such definitization to writing. If UCAs are used, the parties should make every reasonable effort to *definitize* the terms and conditions as soon as possible and, in any event, *not later than 180 days*. While the conditions that gave rise to the UCA may very well delay the submission of a qualifying proposal, the parties should endeavor to reach agreement as quickly as possible to eliminate the uncertainty of an undefinitized contract and avoid disputes that may arise as a result.

2. When the Government issues a UCA, contractor officials should confirm that any oral instructions or directions received from, or confirmed by, the Government are from officials with *contracting authority*. Both contractor and Government officials should confirm oral communications *in writing* to ensure common understandings between the parties.

3. Government officials must monitor funding under UCAs to ensure compliance with the *Anti-Deficiency Act*. Contractor officials should monitor and communicate with Government officials well in advance of reaching the UCA's *price ceiling*. Contractors should keep the CO informed of their costs as they approach the ceiling. If the Government orders continued performance knowing the "Limitation of Cost" clause has been exceeded, the Government may be held to have *waived* the "Limitation of Government Liability" clause.

4. If a contractor has a *potential claim* based on events occurring *before* definitization, the contractor should expressly *reserve* its right to pursue such claim at the time of definitization to avoid a waiver.

5. *Other Than Full and Open Competition*. As a successful challenge to a contract award will only further delay the Government's efforts to acquire needed goods or services, when utilizing other than full and open competition procedures agency officials should seek legal guidance during procurement planning to

ensure the exception is properly invoked. Because lack of *adequate documentation* is frequently cited as one of the reasons for sustaining a protest regarding use of such authorities, agency officials also should carefully document their *justification* for using other than full and open procedures.

6. *Oral Solicitations*. To avoid misunderstandings about material elements of an oral solicitation, contractors should, to the extent feasible, reduce to *writing* any key elements of the oral solicitation and request that the agency confirm the parties' understanding.

7. *Oral Presentations*. When properly used, oral presentations can streamline the procurement process. They are particularly effective when awarding *delivery orders* or *task orders* under *multiple award ID/IQ contracts* in fostering an understanding of how an offeror would perform under a *sample* task order or in assessing an offeror's *experience*. Government contracting officials should follow any agency-specific guidance in deciding whether to conduct or in conducting oral presentations. At a minimum, agencies should prescribe a *specific format* and identify the types of information they are seeking. If the agency intends to make *award without discussions*, officials should be careful that oral presentations do *not* result in "discussions" by allowing offerors to change their proposals.

8. *Oral Contracts*. Given the potential for uncertainty as to the statement of work and the terms and conditions, oral contracts should be *avoided*. At a minimum, the parties should communicate (and confirm in writing if possible) the terms and conditions, the statement of work, and how performance is measured. When the Government seeks to enter into an oral contract, contractors must ensure that the Government official with whom they are dealing has the requisite *authority* to enter into the contract.

9. *Contract Modifications*. Guidance from agency legal counsel can assist in avoiding successful challenges to "*out of scope*" modifications. Agency counsel need to familiarize themselves with the body of case law interpreting whether

a contract modification is within scope, including sensitivity to the type of contract, nature of the work, and the specific language of the original solicitation.

10. *Exercising Options and Adding Options.* To the extent Government contracting officials seek to modify existing contracts to add options for *additional* or *accelerated deliveries*, the Government should address the *cost impact* with the contractor before such modifications. In the case of accelerated delivery, the parties should address the cost/price impact for *schedule accelerations* as well as *decelerations*.

11. *Multiple Award Task and Delivery Order Contracts.* Generally, it is in the Government's best interests to obtain *as much competition as possible* among multiple award ID/IQ contractors. This should include *notice to all contractors* of the intent to issue a task or delivery order, an *explanation of the products or services* sought, and an *opportunity to be considered for the order*. As with contract modifications, COs should assess whether a particular order is *within the scope* of the contracts and, if in doubt, seek legal guidance regarding the scope of the order.

12. *GSA Schedules.* While GSA Schedule contracts have numerous benefits, contractors need to consider the obligations imposed by such contracts, many of which may be unfamiliar to companies without prior experience with Federal Government contracting. This includes Government rights and contractor obligations under the "*Price Reduction*" clause and with respect to *audits*. Intellectual property rights need to be negotiated in advance, documented, and incorporated into the contract, and proprietary information delivered must contain sufficient *proprietary markings*. *Disputes* involving Schedule contracts often can be far more difficult in terms of procedure than those pertaining to noncommercial products or services.

13. A simple way for an agency to reduce the likelihood of a successful protest of a Schedule buy is to adhere strictly to the ordering provisions in the *FAR*. Agencies are *not* required to conduct a competition before ordering

supplies or services off the Schedule. If a *competition* is necessary, an agency should reconsider whether the Schedule is the best vehicle for the agency's procurement needs. If the agency decides to conduct a competition among Schedule contractors, such competition could be comparable to those conducted under multiple award ID/IQ contracts. If it conducts a competition, the agency must adhere to the terms of the *solicitation* and should *document the evaluation* to support the reasonableness of the evaluation.

14. *Defense Production Act.* The Government should make judicious use of the broad authority granted by the Defense Production Act. Contractors and subcontractors need to work with the Government to perform *rated orders*. Particularly in light of their *lack of remedies for displaced work*, contractors and subcontractors are advised to consult with non-Government customers regarding displaced work and work-arounds. Priority always must be given to rated orders: *failure to perform* such an order may subject the contractor or subcontractor to *criminal prosecution*.

15. *Unsolicited Proposals.* Contractors with *innovative* or *unique products* that wish to submit an unsolicited proposal to the Government should (a) consider *which agency* is the best to approach, (b) review *FAR Subpart 15.6* and *agency-specific regulations*, and (c) appropriately *mark* any product or data that is *proprietary*.

16. *Indemnification.* In ascertaining whether indemnification would be appropriate, promptly identify any "*unusually hazardous*" risks associated with the product or service and the environment in which it may be deployed. A critical part of this effort will involve identifying relevant *insurance coverage* and the nature and scope of coverage *exclusions*.

17. *Government Contractor Defense.* Contractors (and the Government) should *not* assume that the Government contractor defense will be available with regard to items deployed in the war against terrorism, particularly in regard to *failure-to-warn claims*. Depending on the product, the parties may wish to consider an *indemnification agreement*.

★ REFERENCES ★

- 1/ Proclamation No. 7463, 66 Fed. Reg. 48,199 (Sept. 14, 2001). See 43 GC ¶ 366(c).
- 2/ 10 U.S.C. § 101(a)(13).
- 3/ See 43 GC ¶ 389.
- 4/ See 43 GC ¶ 402.
- 5/ Deputy Assistant Secretary (Contracting), U.S. Department of the Air Force, Enduring Freedom Memo EF-01-01, "Rapid, Agile Contracting Support During Operation Enduring Freedom" (Oct. 5, 2001).
- 6/ *Id.*
- 7/ National Defense Authorization Act for Fiscal Year 2002, Pub. L. No. 107-107, § 836(a), 115 Stat. 1012, 1192-93 (2001).
- 8/ *Id.*
- 9/ *Id.* § 836(a)(1).
- 10/ *Id.*
- 11/ *Id.* § 836(a)(2).
- 12/ See 41 U.S.C. § 403(12); FAR 2.101.
- 13/ Department of Defense and Emergency Supplemental Appropriations for Recovery from and Response to Terrorist Attacks on the United States Act of 2002, Pub. L. No. 107-117, 115 Stat. 2230.
- 14/ Pub. L. No. 107-188, 116 Stat. 594.
- 15/ *Id.* §§ 101, 102.
- 16/ *Id.* § 121.
- 17/ *Id.* § 127.
- 18/ *Id.* §§ 122, 125, 126.
- 19/ *Id.* §§ 201-231.
- 20/ *Id.* §§ 301-315, 321-322, 331-336, 401-403.
- 21/ Hearing Before the Readiness and Management Support Subcomm. of the Senate Comm. on Armed Services, 107th Cong. 11 (2002) (Statement of Hon. Angela B. Styles).
- 22/ Services Acquisition Reform Act of 2002, H.R. 3832, 107th Cong (2002).
- 23/ White House June 2002 Proposal for the Department of Homeland Security, available at <http://whitehouse.gov/homeland> (accessed June 7, 2002). See generally 44 GC ¶¶ 235, 264.
- 24/ See Aviation and Transportation Security Act, 49 U.S.C. § 114.
- 25/ See 49 U.S.C. § 40110(d).
- 26/ *Id.* § 114(o).
- 27/ Resource Consultants, Inc., Comp. Gen. Dec. B-290163 et al., 2002 CPD ¶ 94, 44 GC ¶ 237.
- 28/ *Id.*
- 29/ Homeland Security Act of 2002, available at <http://whitehouse.gov/homeland> (accessed June 23, 2002).
- 30/ See 10 U.S.C. § 2371 & note; Carl L. Vacketta, Richard N. Kuyath & Holly Emrick Svetz, "Other Transactions," Briefing Papers No. 98-4 (Mar. 1998).
- 31/ DFARS 217.7401(d).
- 32/ DFARS 217.7403(a)(1)-(2).
- 33/ DFARS 217.7404-4.
- 34/ DFARS 217.7404-5(b)(1)-(2); see 10 U.S.C. §§ 101(a)(13) ("contingency operation"), § 2302(7) ("humanitarian or peacekeeping operation").
- 35/ DFARS 217.7404-3(a).
- 36/ DFARS 217.7404-3(b).
- 37/ See 43 GC ¶ 402.
- 38/ Deputy Assistant Secretary (Contracting), U.S. Department of the Air Force, Enduring Freedom Memo EF-01-03, "Unfinitized Contract Actions and Contingency Operations in Support of Operations Enduring Freedom and Noble Eagle" (Nov. 28, 2001).
- 39/ *Id.*
- 40/ *Id.*
- 41/ *Id.*
- 42/ 31 U.S.C. § 1341.
- 43/ FAR 52.232-20, -22.
- 44/ United Techs. Corp. Pratt & Whitney Group, Gov't Engines & Space Propulsion, ASBCA 46880 et al., 97-1 BCA ¶ 28,818, 39 GC ¶ 327.
- 45/ Belleville Shoe Mfg. Co., ASBCA 46036, 95-2 BCA ¶ 27,680 (citing Lear Siegler, Inc. (Instrument Div.), ASBCA 15250, 71-2 BCA ¶ 9059; Sylvania Elec. Prods., Inc., ASBCA 11206, 66-1 BCA ¶ 5536).
- 46/ American Elec., Inc., ASBCA 16635, 76-2 BCA ¶ 12,151, modified on recons., 77-2 BCA ¶ 12,792.
- 47/ 10 U.S.C. § 2304; 41 U.S.C. § 253.
- 48/ See FAR 6.302.

- 49/ 10 U.S.C. § 2304(c)(1); 41 U.S.C. § 253(c)(1).
- 50/ 10 U.S.C. § 2304(c)(1); 41 U.S.C. § 253(c)(1); FAR 6.302-1(a)(2).
- 51/ 10 U.S.C. § 2304(d)(1)(A); 41 U.S.C. § 253(d)(1)(A); FAR 6.302-1(a)(2)(i).
- 52/ 10 U.S.C. § 2304(d)(1)(B); 41 U.S.C. § 253(d)(1)(B); FAR 6.302-1(a)(2)(ii).
- 53/ 10 U.S.C. § 2304(d)(1)(B); FAR 6.302-1(a)(2)(iii).
- 54/ FAR 6.302-1(d)(1).
- 55/ FAR 6.302-1(d)(2).
- 56/ 10 U.S.C. § 2304(c)(2); 41 U.S.C. § 253(c)(2).
- 57/ 10 U.S.C. § 2304(c)(2); 41 U.S.C. § 253(c)(2); FAR 6.302-2(a)(2).
- 58/ FAR 6.302-2(b).
- 59/ FAR 6.302-2(c)(1).
- 60/ FAR 6.302-2(c)(2).
- 61/ 10 U.S.C. § 2304(c)(3); 41 U.S.C. § 253(c)(3).
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- 64/ FAR 6.302-3(c).
- 65/ 10 U.S.C. § 2304(c)(4); 41 U.S.C. § 253(c)(4).
- 66/ 10 U.S.C. § 2304(c)(4); 41 U.S.C. § 253(c)(4); FAR 6.302-4(a)(2).
- 67/ FAR 6.302-4(c).
- 68/ 10 U.S.C. § 2304(c)(5); 41 U.S.C. § 253(c)(5).
- 69/ 10 U.S.C. § 2304(c)(5); 41 U.S.C. § 253(c)(5); FAR 6.302-5(a)(2).
- 70/ 10 U.S.C. § 2304(c)(6); 41 U.S.C. § 253(c)(6).
- 71/ 10 U.S.C. § 2304(c)(6); 41 U.S.C. § 253(c)(6); FAR 6.302-6(a)(2).
- 72/ FAR 6.302-6(b).
- 73/ FAR 6.302-6(c)(1).
- 74/ FAR 6.302-6(c)(3).
- 75/ 10 U.S.C. § 2304(c)(7); 41 U.S.C. § 253(c)(7).
- 76/ 10 U.S.C. § 2304(c)(7); 41 U.S.C. § 253(c)(7); FAR 6.302-7(a)(2).
- 77/ FAR 6.302-7(b).
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- 80/ FAR 6.302-7(c)(4).
- 81/ Signals & Sys., Inc., Comp. Gen. Dec. B-288107, 2001 CPD ¶ 168.
- 82/ Sabreliner Corp., Comp. Gen. Dec. B-288030 et al., 2001 CPD ¶ 170.
- 83/ Lockheed Martin Sys. Integration—Owego, Comp. Gen. Dec. B-287190.2 et al., 2001 CPD ¶ 110.
- 84/ See 10 U.S.C. § 2371 & note; Vacketta, Kuyath & Svetz, *supra* note 30.
- 85/ See 10 U.S.C. § 2371 note.
- 86/ 41 U.S.C. § 601 et seq.
- 87/ DOD, "Other Transaction" Authority (OTA) for Prototype Projects ¶ C.2.20.1 (May 9, 2001).
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- 91/ ViON Corp., GSBICA 10107-P, 89-3 BCA ¶ 22,106, at 111,178.
- 92/ *Id.* at 111,182.
- 93/ Staff, Inc., AGBCA 96-112-1 et al., 97-2 BCA ¶ 29,285 (citing Daly Constr., Inc. v. Garrett, 5 F.3d 520 (Fed. Cir. 1993), 35 GC ¶ 709), 40 GC ¶ 38; Texas Instruments, Inc. v. United States, 922 F.2d 810, 814 (Fed. Cir. 1990), 33 GC ¶ 23; Lance Dickinson & Co., ASBCA 36804, 89-3 BCA ¶ 22,198, 34 GC ¶ 338, *aff'd* on recons., 90-1 BCA ¶ 22,511 (1989); DBA Sys., Inc., ASBCA 34664, 89-1 BCA ¶ 21,465 (1988).
- 94/ Lance Dickinson, 89-3 BCA ¶ 22,198.
- 95/ *Id.*
- 96/ AT&T Communications, Inc. v. Wiltel, Inc., 1 F.3d 1201 (Fed. Cir. 1993), 35 GC ¶ 492.
- 97/ Memorex Corp., Comp. Gen. Dec. B-200722, 81-2 CPD ¶ 334, at 5, 23 GC ¶ 437, clarified on recons., 82-1 CPD ¶ 349.
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- 100/ *Id.* (citing Allied Materials & Equip. Co. v. United States, 569 F.2d 562, 563-64 (Ct. Cl. 1978), 20 GC ¶ 60).
- 101/ *Id.*

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- 105/ *CCL*, 39 Fed. Cl. 780.
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- 174/ Exec. Order No. 10,789, 23 Fed. Reg. 8897 (Nov. 14, 1958); Exec. Order No. 11,051, 32 Fed. Reg. 16,247 (Nov. 28, 1967); Exec. Order No. 11,610, 36 Fed. Reg. 13,755 (July 22, 1971); Exec. Order No. 12,148, 44 Fed. Reg. 43,239 (July 20, 1979); Exec. Order No. 12,919, 59 Fed. Reg. 29,525 (June 3, 1994); Exec. Order No. 13,232, 66 Fed. Reg. 53,941 (Oct. 20, 2001).
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