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## DOD

### **FY 2013 NDAA Passes Without Many of the More Controversial Contracting Provisions**



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**O**n January 2, 2013, President Obama signed the \$633 billion Fiscal Year 2013 National Defense Authorization Act (NDAA). As has become common in recent years, this year's NDAA was not without controversy and political posturing on both sides of the aisle. Given that much of Washington's attention over the past few weeks has been focused on negotiations over the looming "fiscal cliff," there was genuine uncertainty this year about whether an NDAA would be passed at all. In addition to the usual last-minute bill amendments and conference negotiations, President Obama threatened to veto the final bill over several provisions that ultimately were (or were not) included. In

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the end, Congress and the President successfully passed defense authorization legislation for the 51st consecutive year.

The final version of the FY 2013 NDAA contains several dozen acquisition policy provisions that will affect contractors doing business with the Department of Defense. Following passage of the House (H.R. 4310) and Senate (S. 3254) versions of the bill earlier this year, industry groups raised significant concerns over several of these proposed provisions, including, most notably, an amendment that would require DOD to cut contractor and civilian jobs by the same percentage as any cut to military personnel, a provision lowering the cap on contractor compensation, and a provision allowing the Defense Contract Audit Agency (DCAA) access to a contractor's internal audit reports. The good news for contractors is that these and several other of the more controversial contracting provisions were removed, or significantly watered down, in the final bill.

Nevertheless, the FY 2013 NDAA contains many important new requirements and restrictions with which contractors will need to grapple. Below is a summary of the significant contracting-related provisions included in (or excluded from) the final NDAA:

■ **Trafficking in persons (Sections 1701-08).** The NDAA substantially amends the Trafficking Victims Protection Act of 2000, 22 U.S.C. § 7104, by directing the President to ensure that federal government contracts include a condition that authorizes the Government to take punitive action against a contractor, subcontractor, their employees, or agents if they engage in certain activities related to sex or labor trafficking. For all contracts that exceed \$500,000 and are performed outside the U.S., contractors will be required to maintain a compliance plan and make annual certifications related to anti-human trafficking efforts. Of particular significance, the NDAA imposes mandatory disclosure obligations on contractors that receive information from "any source" of "credible information" that an employee engaged in trafficking-related activities.

■ **Counterfeit electronic parts (Section 833).** Section 833 amends Section 818 of the 2012 NDAA to pro-

vide certain protections for contractors performing rework or corrective action to remedy the use of counterfeit electronic parts. Specifically, Section 833 makes the costs of such work allowable if (i) the contractor has an operational detection and avoidance system as required under Section 818, (ii) the counterfeit electronic parts were provided to the contractor as government property, and (iii) the contractor provides timely notice to the Government.

■ **Cybersecurity (Section 941).** Section 941 requires DOD to establish procedures that would require certain defense contractors to report successful penetrations of their networks and information systems. The procedures will include mechanisms for DOD personnel to obtain access to equipment or information of the contractor necessary to conduct a forensic analysis to determine whether sensitive DOD information was successfully extracted from the contractor's network or information system. In response to industry objections to earlier versions of this provision because of concerns over the potential compromise of contractor proprietary information, the final NDAA includes a new requirement that DOD "provide for the reasonable protection of trade secrets, commercial or financial information, and information that can be used to identify a specific person."

■ **DCAA access to contractor internal audit reports (Section 832).** Although previous versions of the legislation included provisions that would have vastly expanded DCAA's ability to access contractors' internal audit reports and materials, these provisions were substantially revised in the final language. The Senate bill included provisions that would have given DCAA essentially unlimited access to contractor internal audit reports and working papers. It also provided that if a contractor refused to provide its internal audit reports and supporting materials, its internal system could be declared inadequate on that basis alone. The final NDAA ensures that DCAA cannot use contractor internal audit reports and supporting materials for purposes other than assessing risk and evaluating the efficacy of contractor internal controls and the reliability of associated contractor business systems. It also provides that while internal audit reports "may be considered" in assessing a contractor's system of internal controls, they "shall not be the sole basis" for finding a system inadequate.

■ **Limitation on use of cost-type contracts (Section 811).** Section 811 prohibits DOD from using cost-type contracts for the production of major defense acquisition programs (MDAPs) unless the Under Secretary of Defense for Acquisition, Technology and Logistics certifies to Congress that a cost-type contract is needed to provide a required capability in a timely and cost-effective manner.

■ **Contractor profits (Section 804).** Section 804 requires DOD to review its profit guidelines in order to identify any necessary changes to ensure an appropriate link between contractor profit and contractor performance. The review must consider the appropriate levels of profit needed to sustain competition, contractors' assumption of risk and incentives for superior performance in delivering quality products and services in a timely and cost-effective manner.

■ **Contractor employee compensation (Section 864).** In a major win for contractors, rather than tying

allowability limits on contractor compensation to the salary of the Vice President, as the Senate bill would have done, the final NDAA requires the Government Accountability Office (GAO) to conduct a study on the effects reducing the allowable costs of contractor compensation.

■ **Contingency contracting (Sections 841-53).** The NDAA contains a litany of provisions relating to government contracts in support of contingency operations, including several major acquisition reforms from the Comprehensive Contingency Contracting Reform Act (S. 3286) introduced by Sen. Claire McCaskill (D-Mo). These provisions would, among other things, (i) require DOD to develop and issue guidance establishing the chain of authority and responsibility within DOD for the planning and execution of overseas contingency operations (Section 843), (ii) require DOD to develop risk mitigation plans for the use of contractors performing critical functions in support of contingency operations, including private security functions, training of foreign government personnel, intelligence and information operations, and other functions closely associated with inherently governmental functions (Section 846), (iii) extend governmentwide the DOD requirement that contractor past performance evaluations be posted within 14 days regardless of whether the contractor has provided any comments (Section 853), and (iv) require that the information in the Federal Awardee Performance and Integrity Information System (FAPIIS) on a contractor also include information about any parent, subsidiary, or successor entities of the contractor (Section 852).

■ **Small business (Sections 1631-1699).** The NDAA contains a host of provisions aimed at increasing contracting opportunities for small business, including provisions that would (i) authorize the Small Business Administration (SBA) to establish a mentor-protégé program for all small business concerns similar to the program currently in place for participants in the 8(a) Business Development program (Section 1641), (ii) require that small business prime contractors not expend on subcontractors more than 50 percent of the amount paid to the concern under the contract, with exceptions for subcontractors that qualify as a "similarly situated entity" (Section 1651), (iii) require an offeror to notify any potential subcontractors that it intends to include in its subcontracting plan and require the SBA to establish a reporting mechanism that allows a subcontractor or potential subcontractor to report "fraudulent activity or bad faith by a contractor with respect to a subcontracting plan" (Section 1653), and (iv) require the SBA to conduct a study every five years to identify industries, as defined under the North American Industry Classification System (NAICS), underrepresented by small business concerns owned and controlled by women.

■ **Suspension and debarment (Section 861).** The final NDAA requires that each DOD military department and the Defense Logistics Agency (DLA), the Department of State, and USAID have at least one suspension and debarment official that does not report to, and is not supervised by, the acquisition office or the inspector general of the respective departments or agencies. The NDAA also directs that such suspension and debarment officials develop written policies for the (i) consideration of formal referrals (and non-formal referrals) of suspension and debarment matters and (ii) documenta-

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tion of any final decision taken pursuant to a formal referral.

■ **Extension of contractor conflicts of interest limitations (Section 829).** Section 829 requires DOD to review the guidance on personal conflicts of interest for contractor employees performing acquisition functions closely associated with inherently governmental functions in order to determine whether it should be extended to contractor personnel performing functions other than acquisition functions that are closely associated with inherently governmental functions, personal services contracts or contracts for staff augmentation services.

Although it could have been much worse for defense contractors, the final NDAA still includes many significant new requirements and restrictions that will affect virtually every company that does business with DOD. Contractors should closely review these provisions to assess the potential impact on their business. For now, defense contractors were spared new requirements in several areas—including profits, allowable costs of employee compensation, and personal conflicts of interest—but the provisions calling for studies and reports on these issues will also merit close attention, as those issues may very well end up the subject of contracting provisions in future NDAAAs.