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Bringing the Supply Chain Home – New Trade Restrictions Change the Way U.S. Contractors Do Business

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Introduction

Roadmap

- Overview: Bringing the Supply Chain Home – Recent Executive Branch Actions Upend the U.S. Global Supply Chain
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- Compliance Challenges: Section 889 Ongoing Compliance Challenges and Open Issues

Overview: Bringing the Supply Chain Home – Recent Executive Branch Actions Upend the U.S. Global Supply Chain

Trump Administration’s Resounding and Continuous Pronouncements on Bringing Supply Chains Back to the United States Take Many Forms

- Trump Administration’s focus appears to be very broad, touching on numerous industries (*e.g.*, semiconductors, rare earth minerals, apparel, and hair products)
- Large focus on U.S. companies doing business with Chinese companies
 - Encouraging businesses to conduct due diligence on Chinese companies that may employ forced labor
 - Huawei, TikTok, WeChat
- Several Changes to the Buy American Act
 - Executive Order 13788 (Apr. 18, 2017) directed federal agencies to scrupulously monitor, enforce, and comply with various “Buy American” laws
 - Executive Order 13858 (Jan. 31, 2019) encourages agencies to use, to the greatest extent practicable, iron and aluminum as well as steel, cement, and other manufactured products produced in the United States in every contract, subcontract, purchase order, etc.
 - Executive Order 13811 (Jul. 15, 2019)) encourages the FAR Council to update the BAA regulations “to most effectively carry out the goals of the Buy American Act and the Administration’s policy of enforcing the Buy American Act to its maximum lawful extent.”
- Incentives for U.S. Industry to “Come Home”
 - Considering tax incentives and re-shoring efforts as measured to spur changes
 - Discussing reimbursement of moving costs for U.S. companies in Hong Kong or mainland China seeking to move back to the United States

Applicability and Developments: The Buy American Act

Buy American Act (“BAA”) Background

- 41 U.S.C. §§ 8301-8305, implemented at FAR Part 25 & DFARS Part 225
- BAA favors the purchase of “domestic end products” and use of “domestic construction materials” on certain federal contracts performed in the U.S.

BAA Requirements

- Not a prohibition; instead works as a domestic preference through a price evaluation adjustment
 - No prohibition on a federal agency purchasing foreign end product, if that product is cheaper after evaluated price adjustment
 - Civilian agencies: low foreign offer increased by 6% or 12% depending on whether low domestic offeror is large or small business (FAR 25.105)
 - DoD: 50% adjustment (DFARS 225.105)

Applicability: *Buy American Act of 1933*

- Applies to all federal prime supply and construction (not purely service) contracts with estimated value above the micro-purchase threshold, unless the Trade Agreements Act (“TAA”) applies
- Applies to certain types of contracts not covered by TAA (see FAR 25.401), e.g.:
 - Arms, ammunition, war material, or purchases indispensable for national security or national defense
 - Sole-source acquisitions
 - Acquisitions from Federal Prison Industries or nonprofit agencies employing people who are blind or severely disabled
 - Small business set-asides
- Applies only to contracts for products to be used, or construction to be performed in the U.S. generally

Applicability: *Buy American Act of 1933*

Buy American Act Origin Rules - 41 U.S.C. §§ 8302(a)(1); FAR Part 25.003

- *Two-part test* to determine if U.S. product:
 - End product must be “manufactured” in the U.S., and
 - Consist of more than 50% U.S. component parts
- *Components* are items directly incorporated into end products
 - Test does not apply to subcomponents
- Agencies calculate percentage of U.S. components by costs:
 - All costs for purchased components
 - Manufactured components – cannot add profit

Developments: *Buy American Act of 1933*

FAR Council's September 2020 Proposed Rule – Implements Executive Order 13881, “Maximizing Use of American-Made Goods, Products, and Materials” (Jul. 15, 2019)

- New Rules
 - Increases the domestic content requirement from 51% to 55% (most products) and 95% (iron or steel)
 - Removes the COTS exception for iron or steel products
 - Requires foreign-made products to be 20-30 percent cheaper than domestic for BAA price waiver
- Implications
 - The proposed changes may impact entire supply chains subject to the BAA
 - Prime contractors will need to flow down domestic content requirements to subcontractors providing components or materials
 - Contractors may need to determine whether their products qualify as a steel or iron end product

Section 889 of the FY 2019 NDAA: What's Prohibited?

Sec. 889(a)(1)(A) – Prohibition on Government Obtaining Certain Telecommunications Equipment or Services

- Prohibits the Government from obtaining (procuring) products incorporating and services using Chinese technology produced by Huawei Technologies Company or ZTE Corporation (as well as other Chinese companies)
- Annual representations available on SAM starting October 26, 2020

Sec. 889(a)(1)(B) – Prohibition on Government Contacting with Entities that Use Certain Telecommunications Equipment or Services

- Prohibits the Government from contracting with an entity that uses products or services that incorporate or use covered technology, whether or not the products or services are used in the context of a federal contract
 - “Use” is triggered regardless of whether that use is in performance of a federal contract
- Requires prime contractors to conduct a “reasonable inquiry,” designed to uncover covered telecommunications equipment or services used by the contractor

Clearing Up the Confusion

- Reporting clause flows down (FAR 52.204-25); representation clauses do not flow down (FAR 52.204-24 & 52.204-26)
- The representation is limited to use by the offeror itself; it does not concern use by affiliates, parents, subsidiaries, subcontractors, suppliers
 - “Use” does, however, concern use by the offeror of equipment, systems, and services owned or provided to the offeror by other companies
- Only applies to equipment/services that are a “substantial or essential” component of any system, or a “critical” technology as part of any system

Section 889 of the FY 2019 NDAA: What's Prohibited?

Exceptions

- Prohibitions do not apply to telecommunications equipment that cannot route or redirect user data traffic or permit visibility into any user data or packets that such equipment transmits or otherwise handles
 - Exception applies to equipment that cannot route or redirect user data (i.e., the equipment is incapable of doing so). It does not apply to equipment that does not route or redirect user data simply based on its current configuration.
- Prohibitions do not apply to the Government procuring with an entity to provide “a service that connects to the facilities of a third-party, such as backhaul, roaming, or interconnection arrangements”
 - Only allows the Government to procure a service that connects to the facilities of a third-party
- Agencies may seek waivers from the Office of the Director of National Intelligence to exempt contractors for “national security interests” and agencies themselves may provide a one-time waiver for a maximum of two years (delayed implementation)

Open Issues

- Release of final rule
- What does it mean to “use” covered telecommunications equipment or services?
- Telecommunications equipment sold as “Section 889 complaint”

A “Reasonable Inquiry” Into the Impact for Commercial Contractors

Making a “reasonable inquiry”

What does “reasonable” look like?

- Can you identify the equipment and providers that are currently in use?
- What about subs/suppliers and who else is likely to ask?

What does “use” of covered equipment or providers mean?

- Can we agree on “substantial or essential” components or “critical” technology?
- How does what we’re doing align with industry peers?

Key Elements of a Compliance Plan

Establishing 889 compliance involves:

- Learn the regulation and track its evolution
- Enterprise level tracking via reasonable inquiry
- Educate procurement, IT and other key teams
- Replace providers/equipment as applicable
- Make representation that reflects status accurately
- Re-evaluate periodically to ensure compliance

What if...

What if there are different definitions for key terms?

- Conservative approach is likely safest, but FAR Council member agency definitions probably carry most weight

What if I am asked to prove my reasonable inquiry?

- No requirement to document but prudent to keep records of what was done

What if I want to expand on the reasonable inquiry?

- Annual reps/certs refreshers from suppliers re: what's supplied or used

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Marques Peterson's practice focuses on counseling and representing aerospace/defense and civil contractors in both federal procurement and international defense sales.

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Dinesh Dharmadasa focuses on a broad range of government contract law, including contract formation and compliance matters, bid protests, and claims.

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Tom leads the Federal Market Access & Commercial Contracting practice within BDO's Industry Specialty Services Group, supporting clients for whom business-to-business contracts are a critical element of their customer relationships and sales/revenue generating activity. For these clients, the public sector is an important, but not necessarily dominant, segment. His current practice focuses on working to best balance people, process and technology solutions to effectively obtain, manage and comply with their contractual obligations and regulatory requirements.



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