

# Government Contracts Advisory

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## Obama Memorandum on Government Contracts—Déjà-vu with a Dangerous Twist

President Obama's March 4, 2009 Memorandum to Agency Heads on Government Contracts plows little new ground; however the Memorandum contains some blanket generalizations that could harm some small business interests and could trigger a wave of audits. The Memorandum harkens back to the first Clinton Administration re-inventing government initiatives, which criticized cost reimbursement contracting in favor of fixed price formats.

The Memorandum targets three contracting practices: sole source contracting, A-76 Competitions, and cost reimbursement contracting. The Memorandum also directs a broad contract review process, calling on agencies to identify, and then change or cancel certain wasteful or abusive contracts.

### Non-Competitive Contracting

The Memorandum conditions the use of non-competitive contracting on situations in which the format can be fully justified, with adequate safeguards. This does little but restate existing law. The Competition in Contracting Act, on the books since 1982, and 27 years of interpretative decisions have already well defined these contours.

The Memorandum's broad generalizations against sole source contracting could however sweep into its grasp established sole source preferences affecting smaller businesses in the 8(a) program and/or preferences to Native American groups. The Memorandum did not address whether the policies on non-competitive contracting are intended to apply to these established preference programs. While the Memorandum cannot change the statuto-

ry sole-source preference programs, it will affect the executive agencies' exercise of discretion in choosing to resort to non-competitive contracts when that discretion exists. This could harm 8(a), Native American and other groups who are granted these preferences.

### Cost Reimbursement Contracting

Like sole source contracting, the acquisition regulations have long contained extensive guidance of the use of different contracting formats and the circumstances when cost reimbursement contracting is appropriate. Many would agree that the Gulf and Iraq wars saw abuses in the use of the cost reimbursement format. The Memorandum restates the existing preferences for fixed price contracting. The restriction on the use of cost reimbursement contracting does not apply the lessons learned from Vice President Gore's push toward fixed pricing: forcing a square peg into a round hole often increases costs by causing contractors to price risk into bids (protective inflation) and produces claims, disputes and delays when the wheels inevitably fall off.

### A-76 and Outsourcing

The Memorandum is correct in citing the confusion in distinguishing between inherently governmental activities and those suitable for outsourcing or service contracting. Years have been spent trying to develop some coherent approach to this issue, with little success. The Memorandum directs that there be clarification of the circumstances when outsourced service contracts are or are not appropriate.

For all practical purposes, the contracting community has largely given up on A-76, as recent changes to the OMB guidance and Bid Protest Rules

have made the award process too uncertain to justify investing the huge resources necessary to produce a successful proposal. But, as long as the government lacks the staffing to fully perform inherently governmental and non-governmental activities, who else will do the work other than contractors?

### Wasteful Contracts

The Memorandum's greatest challenge will be in the implementation of the direction to identify and modify or terminate wasteful and inefficient contracts. This contemplates some form of top down audit, under guidelines to be developed. This part of the Memorandum has the potential to create disruption within government acquisition offices and between contractors.

One wonders if the Memorandum's drafters appreciate that terminating a potentially "inefficient" fixed price contract for the government's convenience may have the effect of converting the terminated fixed price contract into a cost reimbursement contract- exactly counter to the Memorandum's mandate to avoid cost contracts.

There is no dispute that there are inefficient contracts and billions could be saved. If this part of the Memorandum is implemented with a focus toward acknowledged areas of waste and inefficiency, this could be effective in saving costs. Those implementing the rule would be well served by examining the effects of the IDIQ system on competition and on costs, and whether the best value award criteria is really delivering the best value or not. Rather than searching for waste and efficiency on a contract by contract basis, the greatest divi-

dends would be yielded by a 40,000 foot review of other contracting formats that have stifled competition and harmed small business in the name of reducing the acquisition workload.

On the government side, developing the guidance in response to the Memorandum will be difficult and politically charged. Contractors need to start focusing on the return of investment they are providing their customer. Contractors will also have to look at how they will fare in response to a newly energized and funded IG, who will increase the number and scope of audits, looking for contractor non-compliance and cost allowability issues. Both sides need to fasten their seat belts.

### For Additional Information

If you have questions or desire assistance, please contact:

**Albert B. Krachman**

**202.772.5812**

**Krachman@BlankRome.com**

**Brian A. Bannon**

**202.772.5905**

**Bannon-B@BlankRome.com**

**Brian S. Gocial**

**215.569.5424**

**Gocial@BlankRome.com**

**Andrew W. Dyer, Jr.**

**202.772.5918**

**Dyer-A@BlankRome.com**



### Office Locations

One Logan Square • 130 North 18th Street • Philadelphia, PA 19103-6998 • 215.569.5500

Watergate • 600 New Hampshire Avenue NW • Washington, DC 20037 • 202.772.5800

The Chrysler Building • 405 Lexington Avenue • New York, NY 10174-0208 • 212.885.5000

Chase Manhattan Centre • 1201 Market Street • Suite 800 • Wilmington, DE 19801 • 302.425.6400

210 Lake Drive East • Woodland Falls Corporate Park • Suite 200 • Cherry Hill, NJ 08002 • 856.779.3600

301 Carnegie Center • 3rd Floor • Princeton, NJ 08540 • 609.750.7700

201 East Fifth Street • 1700 PNC Center • Cincinnati, OH 45202 • 513.362.8700

1200 North Federal Highway • Suite 312 • Boca Raton, FL 33432 • 561.417.8100

1925 Century Park East • 19th Floor • Los Angeles, CA 90067 • 866.569.5585

5605-07 The Center • 99 Queen's Road Central • Hong Kong • 852.3528.8300