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Hurricane Katrina's Tangled Impact on U.S. Procurement

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FEATURE COMMENT: Hurricane Katrina's Tangled Impact On U.S. Procurement

The popular press—and the contracting community—have been full of stories of contracting failures in the wake of Hurricane Katrina's terrible devastation. The truth behind those stories will become clearer in the coming months, as investigators review the Federal Government's response. What is already certain, however, is that the hurricane has forced open several major gaps in federal procurement rules, which may open the way to a much broader deregulation of our procurement system.

On September 8, just over a week after the hurricane passed over New Orleans, President Bush issued a proclamation that suspended, indefinitely, application of the Davis-Bacon Act to federal contracts entered into across storm-ravaged counties in Alabama, Florida, Louisiana and Mississippi. (Available at www.whitehouse.gov/news/releases/2005/09/20050908-5.html.) AFL-CIO President John Sweeney promptly denounced the president's action as "outrageous." See Thomas B. Edsall, "Bush Suspends Pay Act in Areas Hit by Storm," *The Washington Post*, Sept. 9, 2005, at D03. The president's proclamation means, in effect, that the wage guarantees of the Davis-Bacon Act will not apply to *any* federal contracts—whether related to reconstruction or not—across a broad swath of the South.

On the same day, Congress passed, and the president signed, a second supplemental appropriation, providing \$52 billion for Hurricane Katrina relief. See H.R. 3673, now P.L. 109-62.

The bill had been introduced only the previous day, Sept. 7, 2005. Buried in the hastily enacted legislation were provisions which, with regard to "property or services determined by the head of an executive agency to be used in support of Hurricane Katrina rescue and relief operations":

- Raise the micro-purchase threshold from \$2,500 to \$250,000, and
- Allow the use of simplified acquisition procedures for contracts worth up to \$10 million.

Of the two exceptions, the radically increased micro-purchase exception has probably garnered the most attention (and criticism). See, e.g., Yochi J. Dreazen, "No-Bid Contracts Win Katrina Work," *Wall Street Journal*, Sept. 12, 2005, at A3. Rep. Henry Waxman (D-Calif.) criticized the proposed new exception as potentially dangerous in a Sept. 8, 2005 letter, available at www.yubanet.com/artman/publish/article_24827.shtml, and *The Washington Post* reported that Sens. Charles Grassley (R-Iowa), Susan Collins (R-Maine) and Joseph Lieberman (D-Conn.) signed a letter opposing an increased micro-purchase limit because of concerns regarding oversight and accountability for spending. See Peter Baker & Amy Goldstein, "Congress Approves \$51.8 Billion for Victims," *The Washington Post*, Sept. 9, 2005, at A01. In response to those concerns, Government Executive reported, the Administration is considering requiring a Contracting Officer's review for any micro-purchase over \$50,000, see Amelia Gruber, "Procurement Provision in Hurricane Bill Raises Eyebrows," *Government Executive*, Sept. 9, 2005 (available at www.govexec.com), though it remains unclear what, if any, legal protections would return to these purchases with the CO's review.

Traditionally, the micro-purchase threshold had rested at \$2,500, and certain critical procurements, such as those for contingency operations, had been subject to higher micro-purchase thresholds of \$15,000 and \$25,000. See Federal Acquisition Regulation 13.201. Until Hurricane Katrina, however, there was never any serious public discussion of raising the micro-purchase threshold at least ten times over, to \$250,000.

The broadened micro-purchase exception, which reportedly was added at the request of the Administration (see Rep. Waxman's letter, cited above), drew concern on the House floor during the bill's abbreviated debate. In practice, the increased micro-purchase exception will likely mean that most normal procurement requirements, including special protections for small-business contractors, will not apply to post-Katrina reconstruction contracts up to \$250,000.

The radically increased zone of exception for micro-purchases raises concerns for the small business community, which depends on the FAR's special protections for small businesses. During House debate of the bill, Rep. Donald Manzullo (R-Ill.) noted that, as chairman of the House Committee on Small Business, he was concerned that the law may, in effect, hurt small businesses' ability to "play a significant role in the recovery." Chairman Manzullo received a commitment from the bill's sponsor to work with the Administration "to ensure that our small businesses are fully utilized and that we maintain appropriate controls over contracting." See Congressional Record at H7782 (Sept. 8, 2005).

Chairman Manzullo's concerns are sound—the new exemptions will indeed leave small businesses without any of their normal protections in federal procurement—but those concerns are also merely the tip of a much larger problem.

To understand why, it is important to remember that procurements under the micro-purchase threshold (traditionally, \$2,500) are generally exempt from all procurement requirements. As Karen Manos has pointed out, purchases of supplies or services at or below the micro-purchase threshold "are exempt from virtually all procurement laws, and do not require any clauses or contract provisions other than those necessary to make payment by electronic funds transfer." As a result, "micro-purchases are not subject to CAS [Cost Accounting Standards], TINA [Truth in Negotiations Act], the cost principles, or any Government audit requirements." Karen L. Manos, 1 Government Contract Costs & Pricing § 2:E:2 (Thomson/West 2004). While the statutory exemptions for micro-purchases are somewhat skeletal (see 41 USCA § 428) the regulations that implement the micro-purchase exception state explicitly that, though additional requirements *may* be imposed by the customer

agency, micro-purchases are exempt from almost all the normal contractual provisions and clauses.

By raising the micro-purchase exemption from \$2,500 to \$250,000, the new law likely means, in practice, that thousands of purchases across the Federal Government—so long as they are below \$250,000 and can be linked to the hurricane relief efforts—will be exempt from the normal panoply of procurement requirements. Those purchases will be exempt from competition, from socioeconomic requirements and from many other federal procurement requirements. With one stroke, thousands of federal purchases, worth potentially billions of dollars, have been stripped out of the federal procurement apparatus.

There is a darker side to this micro-purchase exemption, as Rep. Waxman's September 8 letter pointed out. Government purchase cards, which have often been misused, are now open to even more serious abuse. Until now, the low micro-purchase threshold (\$2,500) has capped the amount for which authorized users can purchase *and* pay for supplies using Government purchase cards, outside the normal competitive procurement process. Now, with the cap lifted to \$250,000 for hurricane-relief purchases, authorized Government credit-card holders will be able, in one sitting, to purchase and pay for hundreds of thousands of dollars in goods, without any real check on their actions. The potential for abuse is staggering.

There is another long-term problem tucked away in this expanded micro-purchase exemption. Micro-purchases, because they are exempt from most federal procurement requirements, are also by definition exempt from most enforcement actions grounded in those requirements. This new, vastly expanded exemption may well entangle enforcement actions far into the future, for vendors subject to investigation and enforcement will likely argue that at least some of the contracting actions under review were hurricane-relief efforts that came under this high micro-purchase exemption. For years to come, therefore, federal contracting enforcement officials may be struggling with the unforeseen effects of Hurricane Katrina.

Nor will the problems stem only from micro-purchases. Beyond the micro-purchase exemption, as noted, the new law allows hurricane-relief procurements to use special "streamlined" competitive procedures. The new law allows any agency doing

relief-related procurement up to \$10 million to use the special emergency procurement procedures authorized by 41 USCA §§ 427a(2) and 428(a)(c), and by 10 USCA § 2304(g)(1)(B). Those special procurement procedures, set out in FAR subpt. 13.5, require minimal, if any, competition. This means, in practice, that agencies embarking on relief efforts will be able to make procurements up to \$10 million without any real competition—a radical departure from the competition requirements that are the cornerstone of our procurement system.

Did the Federal Government need these exceptions to clean up after Katrina? Probably not. The procurement reforms of the mid-1990s created a system with extraordinary flexibility, including streamlined competitions and task-order contracts that can be used to procure goods and services in minutes. The system was flexible enough to respond to the September 11 attacks, and it was in all likelihood flexible enough to respond to Hurricane Katrina. At the very least, it would have been impossible to tell, in the few days after the hurricane, whether these deep exemptions will be necessary over the coming years of reconstruction.

Why, then, did Congress and the Administration rush to embrace these new exemptions? In the short term, it was probably to forestall any criticism that contracting “red tape” was slowing recovery. With billions of dollars in relief efforts stripped out of the procurement system’s requirements, no one will be able to complain that the system itself is slowing the Government’s response.

The knottier question is whether these exemptions are part of a longer-term trend—if the Administration and Congress, as some have contended, are using Hurricane Katrina as a springboard for a broader effort to deregulate Government, including the procurement system. See, e.g., Tom Curry, “Hurricane Spawns Flurry of Deregulation,” MSNBC, Sept. 9, 2005, available at msnbc.msn.com/id/9259887/; Jonathan Weisman & Amy Goldstein, “In the Floods, Parties’ Agendas Surface: Post-Hurricane Crisis Presents an Opportunity to Pursue Longtime Goals,” *The Washington Post*, Sept. 10, 2005, at A04. The president’s decision to suspend the Davis-Bacon Act for *all* federal procurements across the affected areas, whether related to the hurricane or not, suggests that these latest changes are indeed part of a broader effort to roll back regulatory requirements.

If that’s the case, however, and we are embarking on a long-term effort to dismantle the federal procurement system, prudence suggests that we should proceed more cautiously and incrementally, rather than sweeping billions of dollars out of the procurement system in legislation that becomes law in less than two days. The U.S. has what many believe to be the best procurement system in the world, and we should be careful before we too quickly abandon the competition and transparency that are the hallmarks of that system. The alternative—a system open to manipulation and corruption—is, after all, precisely the kind of problem that Hurricane Katrina taught us we should try to avoid.



This FEATURE COMMENT was written for THE GOVERNMENT CONTRACTOR by Christopher R. Yukins, associate professor of Government contract law, The George Washington University Law School.

