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Arbitrary Factors May Hinder Buy American Rule Changes

By **Daniel Wilson**

Law360 (August 6, 2021, 8:24 PM EDT) -- The Biden administration has introduced significant changes to prioritize domestic content in federal procurements, but the implementation of its most radical change to calculate that content by value created rather than the source of components may be hampered by undefined characteristics such as brand value.

The Federal Acquisition Regulatory Council's proposed rule, published July 30 and based on a January executive order from President Joe Biden, would steadily increase the minimum value of domestic components required for federal procurements from the current 55% to 75% over time. The White House said the proposal includes the "most robust changes to the implementation of the Buy American Act in almost 70 years."

But the council — a coalition of the U.S. Department of Defense, General Services Administration and NASA — held off on implementing the most significant suggestion in the executive order: to replace that component test with one based on the "value that is added to the product through U.S.-based production or U.S. job-supporting economic activity."

Changing to a value-added test would upend a compliance regime for the BAA and similar laws that has been "honed into sharpness over the 70 years that President Biden is talking about," in which courts and boards of appeal have found ways to legally define some of the more difficult terms in the law, such as what counts as a "component" or "manufacturer," said Matthew Moriarty, founding member at Schoonover & Moriarty LLC.

"At least it's something that people know, and know how to comply with," he said. "If that were to be replaced by value-add, then you just have a lot more questions."

The FAR Council has asked for public input on how value can be measured, whether and why such a test would actually be superior to the current approach, and if there are superior alternatives not included in the executive order or current law.

One likely reason for punting on that issue is that the idea of a value-added test expressed in the executive order was "always a little vague," and the FAR Council perhaps didn't believe it had enough relevant information available, said McCarter & English LLP associate Cara Wulf.

"I think what we'll see happening now is a conversation with industry about how to institute that value-added test," she said. "I think it will take more time for both the … administration and industry to try to

figure out, okay, how can we how can we use this concept in a way that's going to benefit the American economy but also, realistically, how can we change our supply chains to meet that new concept?"

Trying to determine how much domestic value is added could be complicated by having to include hard-to-judge factors such as the value of brand names, Moriarty said.

"Theoretically, attaching a brand name to a product adds value to it, if it's a valuable brand," he said. "Even if it is sold by a seller with a good reputation, that adds value to the items that are being sold."

And the relatively short window between the release of the underlying executive order and the proposed rule, especially without pre-existing feedback, would also have made it "extraordinarily challenging" to come up with a proposal for a value-added test within that time frame, said Covington & Burling LLP partner Mike Wagner.

"I think the course that has been taken is prudent, in that they're seeking feedback and hopefully going to be building some consensus about whether and, if so, how to make that sort of change," he said.

For now, the rules that have been proposed are fairly narrow, said Crowell & Moring LLP partner Adelicia Cliffe.

"I would describe it as addressing low-hanging fruit; the phased increase to the domestic content requirements under the traditional component test and [then] they're really punting on the more ambitious changes ... I think it's narrower than they describe," she said.

Areas where the proposed rule keeps to the status quo include the continued exclusion of commercial off-the-shelf, or COTS, and commercial information technology items from Buy American requirements, despite a directive in the executive order asking the council to "promptly review" and make recommendations on how to extend those requirements to commercial IT.

For COTS items, tracking down and precisely analyzing the source of components can be difficult, especially for smaller suppliers, Wagner said. The council has asked for feedback about the potential impact of narrowing or removing those waivers.

The proposed rule also doesn't address the broad range of foreign products that are covered by the Trade Agreements Act.

The TAA effectively treats items from countries that have a free trade agreement with the U.S. or participate in the World Trade Organization's Government Procurement Agreement, as well as items from certain developing countries, as if they were domestic products for most federal procurements.

That includes products from more than 125 countries, with some notable exceptions such as China and India, and the TAA effectively supersedes the BAA for most federal contracts above $182,000, with an even lower threshold for goods from a few countries.

Changes to the BAA are more important for construction contracts, where the threshold for the TAA to kick in is a little over $7 million, with DOD contracts also having more stringent Buy American requirements. But a March Congressional Research Service report, citing a 2017 study, estimates that potentially 80% of federal contracts are open to foreign suppliers.

Changing that aspect of the TAA would require renegotiating trade deals with other countries, which are often multilateral and which the FAR Council said was beyond the scope of the proposed rule.

"You're still going to have a whole swath of products that these domestic content requirements — the increased thresholds, the new price preferences — won't apply to," Cliffe said.

But the limited subset of federal acquisitions where the BAA does apply is still worth potentially tens of billions of dollars and for those contracts, the changes in the proposal will have a significant impact. The government spends nearly $600 billion on procurement each year, according to the proposed rule.

"It's not a complete sea change, but I do think it's fair to say that this is a significant and meaningful advancement in the implementation of the BAA," Wagner said.

In recognition of the potential impact of the ramp-up in the domestic content requirement, the proposed rule includes a "fallback threshold," meaning that if an increase — the steps go from an immediate 60% when the rule is implemented, to 65% after two years and then 75% after five more years — leads to product shortages or unacceptable costs, agencies can temporarily fall back to the previous threshold to give more time for supply chain adjustments.

"I think that's an acknowledgment by the FAR Council that this could, in fact, be quite difficult for companies to achieve," Cliffe said. "It takes time, and money and resources to make changes to the supply chain."

It's not clear when the administration expects to finalize the rule, but given the relatively short lag between the executive order and the proposed rule, it may happen quickly. Comments on the proposal are open for 60 days, with a virtual public meeting also scheduled for Aug. 26.

"I was surprised to see [the proposed rule] happen so quickly, but I think it really speaks to the fact that the Biden administration is making this a priority," Wulf said.

--Additional reporting by Dave Simpson. Editing by Emily Kokoll.
