

Sequestration

Impact of the March 1 Budget Cuts on Federal Contractors

BAKER DONELSON

EXPAND YOUR EXPECTATIONS[®]

BAKER DONELSON

Who We Are Government Contracts Team



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- Head of firm's government contracts practice
- Lead counsel in GAO, SBA and District Court government contracts cases



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- Government contractor labor and employment issues
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- Federal and state government contracts and bid protests
- U.S. Department of Defense - General Counsel's office

**Who We Are
Geographic Presence**



**Who We Serve
Aerospace**

NASA

Dept. of Defense



International Space Station

Space Shuttle



SOPHIA

Unmanned Aerial Vehicles



Helicopters

Who We Serve
Defense

Battlefield



Weapons systems and munitions



Uniforms and supplies

Support and Peacetime



Military construction



R&R

Who We Serve
Energy

Nuclear

- Production
- Storage
- Disposal
- Closure



Oak Ridge Nat'l Laboratory
Y-12 Nat'l Laboratory
Savannah River
Nevada Testing Grounds
Bevatron, Plumbrook,
Bellafonte

TVA

Largest legal service provider in TVA footprint



Alternative

- Solar
- Wind
- Natural gas/fracking



Who We Serve
Technology

IT Contractors



Infrastructure
Networks
Software

Intellectual Property

- Data rights
- Source code protection
- Patents and Licenses
- Security
- Non-disclosure Agreements

Who We Serve
Construction

Public Construction Contractors

58 attorneys

- Contracting/bidding
- Designs/E&A
- Litigation
- Liens and claims
- Insurance and sureties
- LEED certificaion



Who We Serve
Disaster Recovery

Debris Removal and First Responders



World Trade Center



Hurricane Katrina



Alabama and Joplin, MO tornadoes



Bark Beetles

Who We Serve
GSA Contractors

Legal services tailored for Multiple Award Schedule/Federal Supply Schedule contractors (and "GSA Advantage!")



Who We Serve
Types of Clients

- Federal, state and local**
- Large and “small” businesses
- Current contract holders and new to the federal market**
- Full-time and mostly commercial
- Primes, subs and suppliers**
- National market

Who We Serve
Legal Services

Bids and Proposals

- Contracting opportunities
- Marketing
- Bid preparation

Certifications and Reporting

- CCR and ORCA
- FAPPIS

Protests

- GAO
- Size protests

Award

- Contract negotiation
- Transition

Subcontracting

- Drafting
- Disputes
- Flowdown clauses

Changes

- Contract modifications
- Change orders

Disputes

- Claims and REAs
- Litigation

Labor Issues

- Wage and hour investigations
- Dept. of Labor audits

Ethics

- False Claims
- Gratuities

Accounting

- Cost or pricing data
- Truth in Negotiations Act
- DCAA audits

Buy American and International

- Export control
- Foreign Corrupt Practices Act
- Treaties and Trade Agreements

What Is Sequestration?

What Is Sequestration?

- Mandatory budget cuts starting March 1
- Part of “fiscal cliff” to address deficit
- Automatic reduction in spending
- \$1.2 trillion over next nine years

Events Leading to Sequester

- August 2, 2011 - predicted date U.S. reaches borrowing limit
- August 2, 2011 - Budget Control Act of 2011
- Budget Control Act:
 1. Raise debt ceiling
 2. "Super Committee"
 3. Sequester set for January 1, 2013
- S&P downgrades U.S. credit rating

Events Leading to Sequester

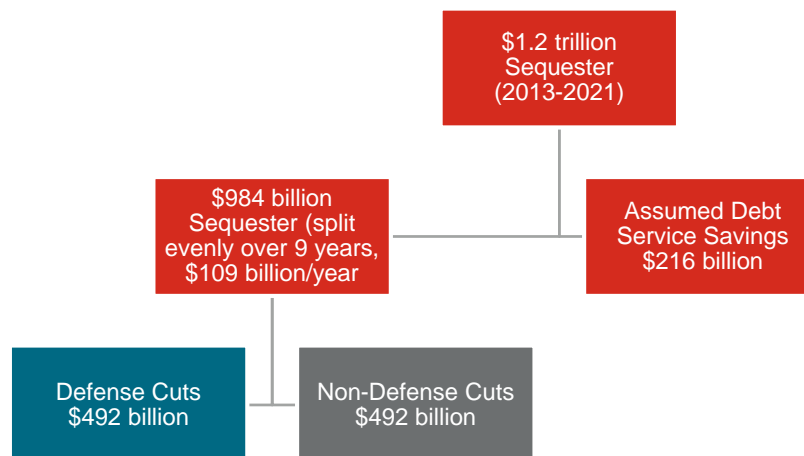
- November 21, 2011 – "Super Committee" joint statement:

"After months of hard work and intense deliberations, we have come to the conclusion today that it will not be possible to make any bipartisan agreement available to the public before the committee's deadline."
- January 1, 2013, 2:00 am EST – American Taxpayer Relief Act of 2012
- March 1, 2013 – scheduled automatic spending cuts

Events Leading to Sequester

- *Sequestration is now the most likely scenario.* – National Journal, February 11, 2013
- *Wall Street survey: Sequester likely, will take stock market toll.* – The Hill, February 11, 2011
- *"You need to be aware that this is probably going to happen."* – Virginia Congressmen Jim Moran (D-8th)
- *Sequestration is going to happen, or something like it.* – Examiner.com, January 29, 2013
- *Like it or not, the sequester is coming.* – MSNBC Maddow Blog, January 30, 2013
- *As of now, it looks increasingly likely that the cuts are going to happen, as both sides refuse to budge.* – Business Insider Politics, January 31, 2013
- *"From what I hear, I have to conclude that it is more likely than unlikely that we'll actually have to do this... We are serious about being ready."* – Deputy Defense Secretary Ashton Carter, January 30, 2013

What Will Happen?



What Will Happen?

Exemptions

- Defense: “Overseas Contingency Operations”
- Domestic: Social Security, Medicaid, Veteran’s Benefits

What Will Happen?

Implementation

- Congress: appropriates
- OMB: apportions
- Agencies: obligate
- Agency discretion is limited: reprogramming and transfer

(For sequester, OMB directs cuts down to project,
program and activity level)

Effects on Contractors and Grantees

Federal side first:

- Hiring freeze
- Furloughs
- Firing temporary employees
- Cessation of travel
- Cessation of supply purchases and maintenance contracts

Effects on Contractors and Grantees

Direct contractor impacts:

- Option periods
- IDIQ Task Orders
- GSA/Supply Schedule purchases
- Termination for Convenience and deductive changes

Preparing for Sequestration

Current contracts:

- Get contract in order
- Get close to your customer
- Be flexible, offer to restructure
- Claims and equitable adjustments
- Performance assessments
- Communicate with CO about funding, options and Task Orders

Preparing for Sequestration

New contracting opportunities:

- Expect: Fixed Price and IDIQs
- Subcontract to fully funded, long-term prime contractors
- Alternative markets: state and local, international
- Bid protests

What about your workforce?

- How can you reduce labor costs?
- If you lay off employees, who do you lay off? And how?
- How can you keep your star performers?
- What legal obligations do you have to warn employees of what may be coming?
- How do you combat the negative impact to the morale of your workforce?

Reducing employee costs

- No new hires
- Eliminate discretionary initiatives – travel, tuition reimbursement programs, employee training, parties, etc.?
- Eliminate overtime (non-exempt)
- Reduce employee pay
- Reduce employees hours (furloughs)
 - Nonexempt
 - Exempt
- Lay off employees
 - Voluntary
 - Involuntary

Eliminating discretionary initiatives

- Make sure you aren't contractually bound (CBA, employment contract, offer letter)
- Make sure your employee handbook manages employee's expectations
- Other ways to save – non-required travel, training, parties

Eliminating Overtime

- Tell employees not to work OT
- Don't tell employees not to record OT
- Pay employees OT even if they violate the no-OT policy

Reducing Employee Pay

- Must be done prospectively (before the employee has worked the hours)
- Must not violate any CBA or contract
- Must not reduce non-exempt employees below minimum wage
- Must not reduce exempt employees below \$455 per week
- Benefit – Simple
- Drawback - Will undoubtedly hurt morale

Reducing Employee Hours (Furloughs)

- Downside – potential effect on benefits, decreased pay
- Upside – some employees might appreciate more time off
- Nonexempt
- Exempt

Furlough of exempt employees

- One day a week? Probably a non-starter
- Full workweek? Exercise caution:
 - Make sure the furlough week corresponds with your “workweek”
 - Don’t let the exempt employee perform ANY work during that furlough week
- Reclassify them as non-exempt to avoid the issue?
 - Provide advance notice of change
 - Employee morale will go down
 - Flipping them back when work picks up is a problem

Layoffs

- Can you still meet the requirements of the Government contract with fewer people?
- Consider the method you will use and how you would justify your decisions if you had to in court
- Consider whether you want to provide consideration to employees in exchange for a release of claims
- Consider what kind of notice you want to/have to give employees
- Assemble a team to administer (should include HR and employment counsel)

Layoffs – Different approaches

- If unionized, look to the CBA; if employee has contract; look to contract
- Select everyone assigned to the particular contract that is affected by the Sequestration
- Select employees for layoff in accordance with their seniority
- Select employees for layoff whose skills can't be utilized on another contract
- Select employees for layoff based solely on merit

Severance Agreements

- Never give an employee severance without getting a release of legal claims in return
- Must comply with OWBPA for employees over 40 to effectively waive their claims of age discrimination
- Give employees a few days to think about it (even if you're not required to)
- Consider covering outplacement services
- But be careful promising extended benefits
- Remind employees of restrictive covenants such as nondisclosure and noncompete agreements
- Consider no-rehire clauses

Payout of other benefits

- Do require employees to turn in all reimbursable expenses before they terminate
- Consider whether you have to or want to compensate employees for unused vacation/PTO
 - If employee has CBA, look to CBA; if employment contract, look to contract
 - In TN, only have to pay out vacation at termination if employment policy says you will
 - Other states differ – particularly CA
 - Follow the law, but also consider employee morale

Notice – WARN Act

Worker Adjustment and Retraining Notification Act (WARN)

- Applies to companies with 100 or more employees
- Requires 60 days' advance notice of a "plant closing" or "mass layoff"
 - Plant closing – Permanent or temporary shutdown of a single site of employment or one or more facilities or operating units
 - Mass layoff – A RIF that results in employment loss at a single site of employment of either 1/3 or more of the site's active employees (at least 50 employees) or 500 or more employees
- Failure to provide notice = back pay and benefits for the entire period of liability + \$500 per day penalty

Who Must Receive Notice

- Affected employees, either individually or through their collective bargaining representatives
- The state dislocated worker unit
- The highest elected local official where the layoff will occur

Date _____

Employee's Name etc. _____

Re: Notice of layoff

Dear _____:

Unless business circumstances change significantly, Company XYZ anticipates conducting a mass layoff lasting longer than six months beginning on _____ [date at least sixty days after date of letter]. We anticipate that your layoff will commence between _____ and _____ [fourteen-day window beginning on date from previous sentence]. Company XYZ expects your layoff to be temporary. **[If you are a union employee, choose one of the following: You do not have bumping rights; in other words, you do not have the right to take another employee's job. OR You do have bumping rights; in other words, you may have the right to take another employee's job.]**

This notice is being given to you pursuant to the Worker Adjustment and Retraining Notification Act of 1988. This federal Act requires employers to give notice to affected employees regarding certain layoffs.

Should you have any questions, please contact _____ at _____ [provide telephone number].

Sincerely,
[Fill in]

State “mini-WARN”

Tennessee is one of 16 states with “mini-WARN laws”

- Applies to companies with 50 to 99 employees
- Over 3 month period
- 60 days’ advance notice required
- Only obligation is to notify State dislocation official
- No monetary liability

Is WARN Act notice required in the event of sequestration?

- Exceptions to WARN requirement include “unforeseeable business circumstances”
- The Administration has declared in a memo that no WARN notices are not required for government contractors affected by the sequestration
- Memo isn’t law
- Memo says nothing about state WARN laws

Careful consideration required

- Such a notice could cause workforce disruption, causing critical employees to depart
- Potential adverse impacts on continued performance, creating termination for default excuse
- Longer-term risk to future contracts and competitions (workforce resources, performance ratings, task orders, etc.)
- Think about potential strategic business effects, and consult with employment counsel

Takeaway: Unclear whether WARN notices are required or desirable; review decision with legal counsel

What about independent contractors?

- Don't assume you can terminate at will – review the contract
- Give any notice that is required under the contract
- Don't engage an independent contractor to do work that you previously had an employee doing

Parting thoughts

- Be prepared/have a plan
- Think strategically and long-term – avoid knee-jerk reactions to downsize the workforce in favor of a well thought-out plan
- At all times, consider employee morale