

## GAO RELEASES REPORT PROVIDING COLOR ON THE DEPARTMENT OF DEFENSE'S USE OF ITS OTHER TRANSACTION AUTHORITY FOR PROTOTYPE PROJECTS

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### U.S. Public Policy and Law and Government Contracts & Procurement Policy Alert

By: Nicholas A. Leibham, Steven A. McCain, Amy Conant Hoang, Erica L. Bakies

On November 22, 2019, the Government Accountability Office ("GAO") released a report on the Department of Defense's ("DoD") use of its other transaction ("OT") authority for prototype projects [1] from fiscal year ("FY") 2016 through FY 2018 ("Report"). OTs enable certain agencies (including DoD) and companies to negotiate terms and conditions specific to a project without requiring them to comply with most federal regulations that apply to U.S. government procurement contracts. The process encourages awards to small businesses, research institutions, and nontraditional defense contractors ("NDCs"). While OTs are not new, statutory provisions in the FY 2016 and FY 2017 National Defense Authorization Acts helped to simplify and clarify the use of OTs and increased approval thresholds, resulting in an increased use of OTs, which the Report confirms.

GAO analyzed Federal Procurement Data System - Next Generation ("FPDS") data and examined relevant documents from a nongeneralizable sample of 11 prototype OTs. GAO's report provides unique insight into how DoD agencies evaluate and award OTs, which, unlike traditional procurement contracts, are not subject to challenge by unsuccessful offerors through the GAO's bid protest process.

### KEY TAKEAWAYS:

- Overall, DoD increased its use of OTs for prototype projects fivefold, from a total of \$1.4 billion to \$3.7 billion during the review period.
- The Army issued the most new awards and contract actions, [2] for a total of 73% of all obligations, but often makes awards on behalf of other DoD components, such as the Air Force, Navy, and Defense Innovation Unit.
- The vast majority of OTs (88%) are awarded on the basis of significant participation from at least one NDC or research institution.
- The Report provides helpful examples of what constitutes "significant participation" by an NDC. [3]
- The top five recipients by OT award value (i.e., amount obligated to the OT) were three consortium managers and two traditional defense contractors.

### REPORT IN DEPTH: WHAT WE LEARNED

- **Where the money is.** Three DoD agencies accounted for 97% of the total \$7.2 billion obligated to DoD OT prototype awards and contract actions from FY 2016 to FY 2018. The Army accounted for the vast majority, with 73% (\$5.2 billion) of total obligations, followed by the Defense Advanced Research Projects Agency ("DARPA") with 13% (\$972 million) and the Air Force with 11% (\$829 million).
- **Where the money is going.** The Report found that the top five recipients by obligations were three consortium management firms and two traditional defense contractors. Awards to these five recipients accounted for \$5.1 billion or 71 percent of the obligations on new awards and contract actions for FY 2016 to FY 2018. Half of the awards to the two traditional defense contractors were made on the basis of at least one-third "cost-share" contributions, while the other half of the awards were made on the basis of significant participation from at least one NDC or research institution.
- **How long it takes the money to get there.** The Report provided limited information on how long it takes DoD to award an OT. Because this data is not available in FPDS, GAO reported numbers based solely on the 11 projects that it reviewed in depth. For those projects, award times ranges from 45 to 370 days.
- **Authority used to justify the OT award.** According to the Report, 88% of OT awards and contract actions were awarded on the basis of significant participation from at least one NDC. Traditional contractors, who must generally provide at least a one-third cost share under an OTA award, accounted for 11% of the awards. The remaining one percent of OTs were awarded to traditional contractors under DoD's justification of exceptional circumstances. [4]
- **What qualifies as "significant participation" from an NDC.** The Report noted that, for OTs awarded on the basis of significant participation from an NDC, the NDC participation ranged from 16% to 100% (i.e., the percentage of the total dollar value received by the NDC). DoD does not define "significant participation"; though, the DoD OT Guide (the "OT Guide") provides high-level examples of what may constitute significant participation. The Report contains helpful details as to what contributions were deemed "significant" in the 11 OTs that it reviewed:

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- o Nine of the 11 OTs reviewed by GAO had significant participation from at least one NDC.
- o In five instances, the NDC participation ranged from 75% to 100% of the total award value.
- o In three instances, the NDCs were determined to be significant participants, while only receiving 16% to 25% of the total award value. Agreements officers provided the following assessments for those determinations:

- Company providing a critical service: a unique dataset to test the prototype (systems engineering toolset to design cyber resiliency for military systems);
- Company providing a critical service: testing equipment, engineering unit, and flight unit materials for the prototype (space-based adaptor and power port for a satellite maintenance vehicle); and,
- Company providing critical services: vessel, crew, and logistics support for prototype (large unmanned surface vehicle capable of autonomous and manned operations).

- **Key takeaway regarding significant participation.** DoD has considered the NDC significant participation requirement met based on a contribution of unique/valuable data, unique/valuable materials and/or assets, and/or unique/valuable human capabilities.
- **A more detailed report from DoD is coming soon.** The Report noted that DoD is expected to submit its own report on its use of prototype OT authority. This DoD report in response to Congressional direction will provide more detailed information on DoD organizations using the authority, the purpose and status of those projects under an OT, and whether those transactions of have led to follow-on production contracts.

## REPORT IN DEPTH: WHAT WE DIDN'T LEARN

- **Who is performing OT projects.** The Report included data on which entities received the highest number of OTs (by contract value) as reported in FPDS. When DoD awards an OT to a consortium, however, FPDS lists the consortium management firm as the recipient, not the technology/solution provider. For instance, GAO reported that consortium manager Advanced Technology International ("ATI") received 49% of prototype OT funds awarded by DoD, but did not report on which of the 13 ATI-managed consortia were involved, nor which specific consortium member was the *actual* technology/solution provider. GAO noted in the Report that FPDS "did not show which consortium members carried out the projects." [5]
- **The extent to which OT projects are competitively awarded to consortium members.** FPDS tracks whether a base contract was awarded competitively but does not track whether individual projects awarded under that base contract were also awarded competitively. The Report noted that modifications made to transactions awarded to consortiums automatically retain the same competitive or noncompetitive designation as the base contract. FPDS allowed agreements officers to record whether an OT base contract was awarded competitively. Accordingly, if the overall base contract was awarded competitively, FPDS would indicate that all projects were awarded competitively, regardless of whether that was the case. This fact, like the one above, highlights the limitations of the FPDS data used to assess OTs.

## HOW TO POSITION YOUR COMPANY FOR OTS

The Report demonstrates that DoD remains focused on using OTs to further pursue and obtain cutting-edge technologies that further their mission effectiveness. For companies interested in obtaining an OT, it is important to remember these key facts:

- **Seek out opportunities.** OTs allow agencies flexibility to create their own solicitation methods, as long as they are using competitive procedures to the maximum extent practicable. These can include technical demonstrations, design sprints, hackathons, and prize contests. Look out for different types of opportunities from DoD.
- **Join a consortium.** According to the Report, three out of the top five recipients of OTs are consortia, which then manage the various project awards. Consortia generally focus on industry or specialty, which means joining one can help identify relevant opportunities in that domain space.

- **Negotiate the terms.** OTs are not subject to most U.S. government procurement regulations, and therefore, most of their terms and conditions will be negotiable (e.g., IP and data rights). Keep in mind, however, that a consortium's management contract can require that it flow down certain terms and conditions to awardees, which could limit whether they are negotiable and that negotiations can result in the delay of the issuance of the OT subaward.
- **Understand intellectual property and data rights.** Often OTs will include terms from the Federal Acquisition Regulations to delineate intellectual property and data rights between the parties. These terms generally are favorable to contractors, but parties to an OT will want to ensure that they understand the scope of how they will apply to a particular contract, especially in a prototype contact, and modify them accordingly.
- **Understand the non-negotiable terms and conditions.** Although OTs are not subject to most U.S. government procurement regulations, some standard terms and conditions will continue to apply to OTs, including fiscal laws, such as any antideficiency requirements. Such terms and conditions will not be negotiable.
- **Ensure the NDCs are playing a significant role in performance.** If seeking an opportunity with a traditional contractor, be sure to identify how the NDC will be performing the OT to a "significant extent." "Significant extent" is addressed in the OT Guide but is not defined, allowing for some flexibility in what constitutes "significant extent." In proposals, be specific about the NDC's performance and why it is critical to the OT and consider the examples provided in the Report.

## CONCLUSION

When it comes to OTs, the K&L Gates public policy and government contracts & procurement policy teams can assist to develop strategies for targeting various opportunities; our professionals have assisted NDCs, traditional contractors and research institutions in all manners of OT awards. Contact any of the authors listed on this alert for more information on OTs or any other related topic.

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### NOTES:

[1] Pursuant to 10 U.S.C. § 2371b, DoD may use its OT authority "to carry out prototype projects that are directly relevant to enhancing the mission effectiveness of military personnel and the supporting platforms, systems, components, or materials proposed to be acquired or developed by the DoD, or improvements of platforms, systems, components, or materials in use by the armed forces." DoD also has OT authority to enter into OTs for research and production purposes, which were not included in GAO's analysis.

[2] For purposes of the Report, contract actions include modifications and orders that result in a change in obligations.

[3] Because "significant participation" is not defined via statute or regulation—and 88% of all OT awards have at least one NDC—the Report is especially insightful on this subject.

[4] 10 U.S.C. 2371b(d)(1) lists four circumstances in which DoD may use its prototype OT authority: (1) significant participation from at least one NDC or research institution, (2) significant participation exclusively from NDCs, research institutions, or small businesses, (3) at least one third of the total cost of the prototype project is paid out of funds provided by sources other than the federal government, or (4) *exceptional circumstances apply*. FPDS did not include data on whether DoD awarded OTs under the third justification (all significant participants are NDCs, research institutions, and small businesses).

[5] Report at 17.

## KEY CONTACTS



**NICHOLAS A. LEIBHAM**  
PARTNER  
WASHINGTON DC, ORANGE COUNTY  
+1.202.778.9284  
NICHOLAS.LEIBHAM@KLGATES.COM



**STEVEN A. MCCAIN**  
GOVERNMENT AFFAIRS COUNSELOR  
WASHINGTON DC  
+1.202.661.3747  
STEVE.MCCAIN@KLGATES.COM



**AMY C. HOANG**  
ASSOCIATE  
WASHINGTON DC  
+1.202.778.9468  
AMY.HOANG@KLGATES.COM



**ERICA L. BAKIES**  
ASSOCIATE  
WASHINGTON DC  
+1.202.778.9887  
ERICA.BAKIES@KLGATES.COM

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