

**And You Thought You Were Confused:  
GAO and COFC Reach Different Results on TAA Compliance**

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The Government Accountability Office (GAO) and the Court of Federal Claims (COFC) recently reached very different results in bid protests involving application of the Trade Agreements Act (“TAA”) to the same procurement. See Klinge Corporation, B-309930.2, 2008 C.P.D. ¶ 102 (Feb. 13, 2008) and Klinge Corp. v. U.S., 82 Fed. Cl. 127 (2008). The principal issue in both protests was whether the agency had acted reasonably in accepting the awardee’s certificate of TAA compliance. The GAO held that the agency had acted reasonably and denied the protest; the COFC subsequently held that the agency had not acted reasonably, sustained the protest, and set aside the award.

The protests involved a best value procurement by the Marine Corps for an indefinite delivery/indefinite quantity (ID/IQ) contract for Large Field Refrigeration Systems (LFRSs), together with a spare parts support package. The procurement was subject to the TAA, which requires that the “end product” to be acquired must be (i) “mined, produced, or manufactured” in the U.S., or “wholly the growth, product or manufacture” of a “designated country” or (ii) substantially transformed [in the U.S. or “designated country”] into a new and different article of commerce with a name, character or use distinct from that of the article or articles from which it was transformed.” DFARS 252.225-7021(a)(4)(12); see also FAR Subpart 25.4; 52.225-5, Trade

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Agreements; Thomas Barletta, et al., “The Basics of the Trade Agreements Act,” Off the Shelf, Coalition for Government Procurement (March 2006), available at <http://www.steptoel.com/assets/attachments/1062.pdf>. (The current threshold for application of the TAA to most, but not all, procurements of supplies and services is \$194,000.)

**Critical Facts**

Both offerors proposed to use the same Chinese-made (non-designated country) containers for the LFRSs, but the awardee, Sea Box, proposed attaching and integrating a Singapore-made (designated country) refrigeration unit (“RU”) to the container in China before the item was shipped to the U.S. for additional manufacturing (e.g., painting and electrical), parts integration and quality assurance. The protester, Klinge, proposed to use a U.S.-made RU and to integrate the RU and container and perform all additional manufacturing in the U.S.

The agency awarded the contract to Sea Box based on initial proposals, but took corrective action in response to a GAO protest by Klinge, which, among other things, challenged Sea Box’s TAA compliance. The corrective action included conducting discussions with the offerors regarding their TAA compliance. Following discussions and submissions of FPRs, the agency again awarded the contract to Sea Box, finding that its proposal was the best value.

Klinge protested again, first to the GAO and then to the COFC. Both decisions framed the key issue as whether the agency had acted reasonably in accepting Sea Box’s certification of TAA compliance, but came to very different conclusions. The different outcomes were based in part on differences in how each forum addressed the issue of “substantial transformation” under the TAA.

**GAO Decision**

GAO noted that while an agency may ordinarily accept an offeror’s certification of TAA compliance (which in turn obligates the offeror to furnish TAA compliant products during performance), an agency is required to go beyond the offeror’s representation if, prior to award, it “has reason to believe that a firm will not provide compliant products.” 2008 C.P.D. ¶ 102 at 5. GAO also stated that in such cases it “will review the [agency’s] evaluation and resulting determination [regarding TAA compliance] to ensure that they were reasonable.” Id.

Here, GAO recognized that since Sea Box proposed to use a non-designated country container which was joined with the RU in China, compliance with the TAA depended on whether there “was a substantial transformation of the Chinese-made insulated container in the U.S.” Id. at 4. In addressing that question, GAO observed that “neither the FAR nor DFARS provides guidance or examples to illustrate the circumstances under which an article is ‘substantially transformed’ into a new and different item.” Id. at 5. GAO also appears to have accepted the approach taken by the agency for determining whether there had been “substantial transformation,” which “looked to whether significant work or processes necessary to the functioning as a refrigerated container system would occur in the U.S.” Id.

The GAO found that the information available to the agency concerning Sea Box’s production process supported its conclusion that “significant production work would take place in the U.S. before Sea Box’s LFRS could be delivered to the agency.” Id. at 5; see also id. at 6. In addition to information provided by Sea Box in its responses to discussion questions and FPR, the GAO also relied on information obtained by agency counsel in an informal, pre-award, post-discussion telephone communication with Sea Box in which Sea Box apparently indicated that the work performed in China was limited to bolting the RU onto the container. (In doing so, GAO rejected Klinge’s claim that this communication with Sea Box constituted impermissible

discussions, concluding that Klinge had failed to show how it would have improved its proposal through additional discussions and therefore had not established competitive prejudice. The GAO also refused to consider Klinge’s argument that information provided by Sea Box regarding testing the LFRSs in China further indicated that they were not a designated country item, on the ground that this argument was untimely because it was raised after the agency report. See id. at 4-5 n2.)

**COFC Decision**

After GAO denied its protest, Klinge protested the award in the COFC. The COFC set aside the award to Sea Box, concluding that the agency missed several “red flags” in its evaluation of Sea Box’s proposal and had applied an incorrect standard for assessing TAA compliance.

According to the Court, there were at least three issues presented by Sea Box’s submissions which should have provoked further inquiry into Sea Box’s certificate of compliance. First, the schedule of work in Sea Box’s FPR listed China as the place of “final assembly” and for various types of testing. See 82 Fed. Cl. at 130. Second, Sea Box’s responses to the discussion questions indicated that the RUs would be “mechanically and electrically integrated” into the Chinese-made containers in China. See id. Finally, Sea Box had indicated that “substantially every one” of the 32 spare parts required by the RFP were U.S.-made, while the TAA required 100 percent compliant parts. See id.

The Court also was critical of the lack of documentation in the record of the agency’s consideration of Sea Box’s TAA compliance. See id. at 135-36. Further, the Court rejected the information obtained by agency counsel in the pre-award telephone call with Sea Box. The Court stated that this communication could not supplant what it viewed as contradictory

information in Sea Box’s written responses to the discussion questions, stating: “At some point, Sea Box must be held to its written representations.” See id. 136.

The Court rejected the agency’s position that TAA compliance is essentially a matter of contract administration. See id. at 135. Like GAO, it acknowledged that an agency may rely on an offeror’s certificate of compliance but also stated that an agency must go beyond that representation if, prior to award, it has reason to believe the offeror will be providing non-compliant products. See id. Here, the Court was critical of both the agency’s inquiry into Sea Box’s TAA compliance and its consideration of what the Court concluded was conflicting information provided by Sea Box. See id. at 136-37.

The Court also addressed the issue of what constitutes “substantial transformation.” In doing, so it relied on an early Supreme Court case that involved duties on imported corks used in bottling beer. In that case, Anheuser-Busch Brewing Ass’n v. United States, 207 U.S. 556 (1908), the Supreme Court emphasized that for there to be substantial transformation; “a new and different article must emerge, ‘having a distinctive name, character or use.’” Id. at 562 (citation omitted). Accordingly, the COFC stated that the “proper inquiry” for determining whether and where substantial transformation occurs is “at what point the article acquires its distinct name, character, or use.” 82 Fed. Cl. at 135. The COFC found that China was the place of both “final assembly” and significant operational testing of the Sea Box LFRS, and thus held that “[i]t is apparent that the [Sea Box] LFRS is substantially transformed in China,” not in the U.S. Id. at 136. (The decision also touched on the differences between the TAA and the Buy American Act. See id. at 129, 136 & n 15; 137.)

Based on the record before it, the Court held that it was arbitrary and capricious for the agency to have accepted Sea Box’s certificate of TAA compliance. See id. at 137-38. The Court

also concluded that the agency’s failure to properly consider Sea Box’s TAA compliance deprived Klinge of the chance to have its bid “fairly and lawfully considered,” and that there was a public interest in ensuring that the government makes proper inquiry into TAA compliance when required, and does not award contracts that do not comply with the TAA. See id. 138-39.

**Lessons Learned**

The GAO correctly noted that the FAR and DFARS do not provide guidance on what constitutes substantial transformation. However, the GAO has previously noted that the legislative history of the TAA indicates that its rule of origin provision is derived from Customs law principles for determining duties on imports. See Becton Dickinson AcuteCare, B.-238942, 90-2 CPD ¶ 55 (July 20, 1990). Further, there is an extensive body of Bureau of Customs and Border Patrol (Customs) rulings regarding substantial transformation in that context. Those decisions tend to be fact specific but can be instructive in addressing issues of TAA compliance and have been relied on in other bid protest decisions. See, e.g., Pacific Lock Co., 2007 C.P.D. ¶ 191 (Oct. 25, 2007). While the COFC’s “name, character, or use” standard is more like that traditionally used in determining substantial transformation than the formulation applied by the GAO, neither the GAO nor the COFC discussed Customs rulings, and perhaps both concluded that none were relevant to the specific TAA issue presented. (A company faced with a country of origin issue, also can seek an advisory ruling or final determination from Customs as to specific products or classes of products. Note, however, that Customs has recently proposed to change from focusing on “name, character, or use” in determining if there has been substantial transformation in making most country of origin determinations, and to look instead to changes in tariff classifications (“tariff shifts”). See 73 Fed. Reg. 43385 (July 25, 2008).)

Agencies and contractors need to recognize that protests are becoming a more frequent mechanism for policing TAA compliance. When faced with a question regarding TAA compliance, a procuring agency should elicit further information from offerors; be alert for “red flags;” properly consider, as appropriate, whether there has been substantial transformation in the U.S. or a designated country; and document the basis for its decision regarding the offerors’ TAA compliance.

Contractors need to consider TAA compliance before submission of proposals. If TAA compliance is questioned, an offeror must fairly and accurately provide relevant information regarding the U.S. or designated country status of its product, which is likely to require addressing issues of substantial transformation. Because protests involving TAA compliance issues are likely to require access to proprietary and source selection information that will be subject to a protective order, the effective prosecution or defense of such a bid protest is likely to require retaining outside counsel. (The COFC noted that Sea Box was represented only by its inside counsel who was not admitted under the GAO and COFC protective orders and therefore did not have access to protected material.)

Finally, contractors need to remember that TAA non-compliance is not limited to potential protest risks, but can create issues of contract performance and, potentially, civil fraud or even criminal exposure. See, e.g., Ran-Paige Co. v. U.S., 35 Fed. Cl. 117 (1996) (involving default termination for TAA non-compliance).