THOMPSON HINE

Business Law Update

Spring 2021

Business Perspectives

Spring Has Sprung

By Frank D. Chaiken, Practice Group Leader, Corporate Transactions & Securities

Every spring, the Chicago River is dyed green for St. Patrick's Day (with a secret eco-friendly, vegetable-based recipe). Every spring until last year, that is.

Thompson Hine opened our office in Chicago in late 2018. When I moved there in summer 2019 to help get things going, I was looking forward to this spring ritual. We all know what happened. So, it was great to see that tradition resume this year, albeit under strict news embargo as to when the greening would commence. But with parkas against the late winter chill, and despite snow in the forecast, residents and visitors came out and were treated to the verdant spectacle, in a hopeful sign of better times ahead.

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For more details on any of the topics covered in this *Business Law Update*, please contact the authors via the links at the end of each article or David R. Valz, editor-in-chief. For information on our Corporate Transactions & Securities practice, please contact Frank D. Chaiken, practice group leader.

And yet, all is not flowers blooming and birds chirping. Yes, the market is up, the vaccine rollouts continue, and people are coming out of winter hibernation. Pent-up consumer spending and related activity are on the rise. One starts to hear about supply chain bottlenecks and shortages. Just try to find a house to buy in many U.S. cities. Many have lost employment in jobs that may never return but may find new ones in whole industries and service categories that are newly relevant, or even came into existence, as a result of the pandemic.

Just as many of you, our firm is thinking hard about how we will operate and succeed in the post-COVID world. How will we stay engaged with our clients and customers? How to maintain our esprit de corps? How will we train and develop our younger talent (and our older talent, for that matter)? How much office space do we really need? How can we safely and effectively integrate a continuing pattern of working from home into our regular workflows? How can we respond and act on our aspirations for diversity, equity and inclusion in our business? In other words, life goes on, with all its challenges, problems to be solved, and new legal developments to be reported. In this edition of the *Business Law Update* we address the following topics:

- Proposed amendments to rules promulgated under the Hart-Scott-Rodino Antitrust Improvements Act and what they will mean for investment funds and master limited partnerships
- Context, cautions and considerations regarding the United States-Canada-Mexico Agreement (USMCA), which became enforceable law on January 1, 2021
- How the PRO Act, which has been passed by the House, could have a profound impact on franchise operations
- A review of government procurement priorities and practices under the new presidential administration and Congress

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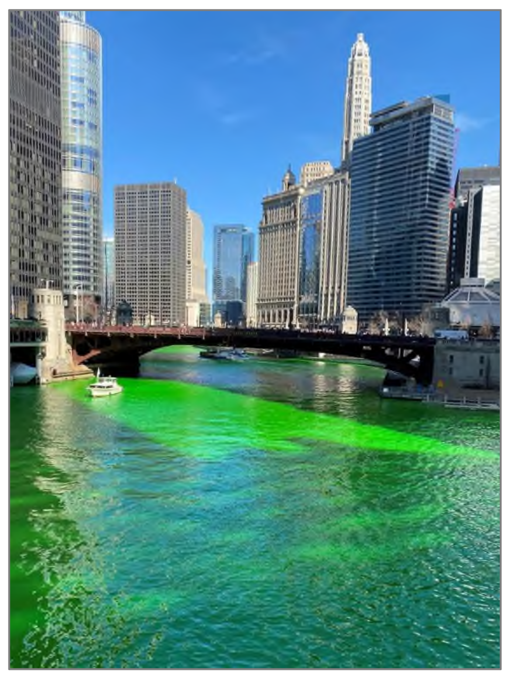
Wishing everyone good health, and happy reading.

Frank Chaiken leads the firm's highly regarded Corporate Transactions & Securities practice and its more than 100 professionals, representing clients of all sizes across virtually every industry. If you have questions or would like to share your thoughts, please contact Frank at 513.352.6550 or by email to Frank.Chaiken@ThompsonHine.com.



M&A – Private Equity

Proposed Amendment to HSR Rules Would Increase Filing Obligations for Private Equity Funds

By Mark R. Butscha, Jr. and Joshua Shapiro

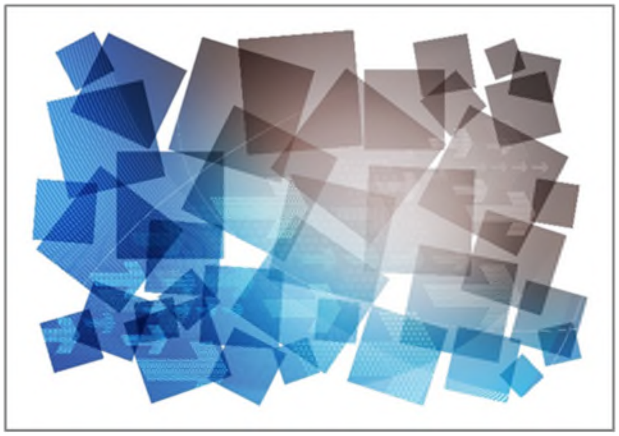
Late last year the Federal Trade Commission (FTC), with the agreement of the U.S. Department of Justice's Antitrust Division (collectively with the FTC, the "Agencies"), proposed amendments to rules promulgated under the Hart-Scott-Rodino (HSR) Antitrust Improvements Act that would significantly increase the filing obligations of investment funds and master limited partnerships. The proposed rules have not been finalized as of this writing, but the public notice-and-comment period expired on February 1, 2021, clearing the way for the Agencies to finalize the proposed rules. The impetus behind the proposed amendment is that the Agencies seek additional information to better assess the competitive significance of transactions involving private equity funds that share common operational or investment management control with related funds. As might be expected, some investment funds have expressed concern, with one firm warning that "an exponential increase in the number of HSR filings" would "impair funds' ability to operate, severely impacting the ability of underlying investors to meet their investment objectives." The purpose of this article is to provide some context for this looming rule change and summarize what it will mean for investment funds.

Current HSR rules often do not require the submission of detailed information about all funds under common operational or investment management. Under current rules, a filing "person" is "an ultimate parent entity [UPE] and all entities which it controls directly or indirectly."[1] For this purpose, "control" only means having the right to 50% of the entity's profits or, upon dissolution, 50% of its assets.[2] To determine the UPE, one starts with the legal entity making the acquisition and moves up the chain of "control" to the entity or individual that is not "controlled" by any other entity. In many cases, the individual investment fund making the acquisition qualifies as a filing "person" because no other entity "controls" it. Some other entity (e.g., an investment management company) may manage the fund's investments and operations, but often it does not "control" the fund for HSR purposes. These other entities are called "associates" of the UPE, with "associates" also including other funds under common investment management and their portfolio companies. Current rules require some limited information to be submitted about "associates," but the most detailed information is reserved for the UPE (the individual fund) and its controlled entities (portfolio companies).

The Agencies are concerned that the information required by current rules does not provide enough visibility to assess the competitive implications of some transactions. The FTC believes that requiring more detailed reporting from entire fund families will "allow the Agencies to 'receive the information they need to get a complete picture of potential antitrust ramifications of an acquisition.'"[3] To achieve that goal, the proposed new rules would require many private equity buyers "to disclose additional information about their associates … and to aggregate acquisitions in the same issuer across their associates when making an HSR filing."[4] To do so, the HSR rules would simply fold "associates" into the definition of "person," which means that detailed information would have to be provided from not only the fund making the acquisition but also all other funds and entities under common investment or operational management control. This additional information would include:

- Financial statements;
- Revenue information, broken down by NAICS code;
- Identity of all entities controlled by "associates"; and
- Identity and ownership stake of minority investors in "associates."

[1] 16 C.F.R. § 801.1(a)(1).
[2] 16 C.F.R. § 801.1(b).
[3] 85 Fed. Reg. 77056.
[4] 85 Fed. Reg. 77054 (Dec. 1, 2020).



Implementation of the proposed rule would result in more HSR filings. Another effect of including all "associates" as part of a filing "person" is that more transactions will be reportable. Under current rules, a transaction is not reportable unless it satisfies the annually adjusted thresholds for "size of transaction" (currently $92 million) and "size of person" (the buyer and seller must have sales/assets of $184 million and $18.4 million, respectively). The proposed amendments affect both thresholds:

- **Size of Transaction:** Under current rules, only the value of the interest acquired by the UPE is considered in determining the size of transaction. The proposed new rule would require the UPE's interest to be aggregated with the interest of any associates. For example, consider a situation in which Fund 1 and Fund 2 are not "controlled" by any other entity, but they are "associates" given that they are managed by the same investment management company. If Fund 1 and Fund 2 were to acquire interests in Target valued at $80 million and $20 million, respectively, the deal would not be reportable under the current rules because neither Fund 1's interest nor Fund 2's interest would meet the $92 million size-of-transaction threshold. Under the proposed new rules, however, the interests of Fund 1 and Fund 2 would be aggregated, pushing the value of the deal beyond the $92 million threshold and therefore requiring a filing (assuming the size-of-person test is also met and no applicable HSR exemptions apply).
- **Size of Person:** Under current rules, a newly formed acquisition vehicle ("NewCo") often will not be "controlled" by any other entity and therefore be its own "person." NewCo also may have little or no revenue or assets prior to the acquisition, which means it would not satisfy the size-of-person test. Under the proposed new rules, however, NewCo probably would not be its own "person" because it would have "associates" under common investment or operational management. The revenue and assets of the broader family of "associates" would be included in determining the size of person, and this ordinarily would exceed the threshold.

Conclusion

Investment funds soon may be required to make more HSR filings, and those filings will require more detailed information than what is required under current rules. These increased obligations likely mean increased delay and expense, and it remains to be seen whether they also will result in increased government investigations or enforcement. For now, private equity buyers and sellers should be aware of these impending changes and bear them in mind when planning for future deals.

Please contact Mark Butscha or Josh Shapiro with any questions.

International Trade

New Year, New NAFTA – Evaluating USMCA's Impact on Current Operations and Due Diligence Procedures

By Dan Ujczo

The "new NAFTA," now known as the United States-Canada-Mexico Agreement (USMCA), entered into force this past summer in a manner similar to a pandemic-impacted wedding—the three countries got formally "hitched" but the large celebration and rollout were reserved for a later day. Specifically, USMCA launched on July 1, 2020, but the respective government agencies exercised "restrained enforcement" for the first six months of implementation. However, as of January 1, 2021, USMCA is the enforceable law of the land and companies, as well as their advisers, must account for potential competitiveness, compliance and due diligence impacts going forward.

USMCA Is Not NAFTA

The threshold consideration is assessing whether an entity's current operations qualify for preferential (e.g., duty-free) treatment under USMCA. Qualifying under NAFTA does not automatically lead to qualification under USMCA. Even where this process is relatively straightforward, USMCA imposes stricter certification and record-keeping requirements, requiring companies to "show their work," overhaul supplier contracts and re-align data management/record-keeping systems. Traceability and transparency within global supply chains are the hallmarks of USMCA. Companies should rest assured that in the event they elect to bypass a USMCA analysis, it will not be long before a customer, supplier or government agency comes knocking to request documents verifying USMCA certification and compliance.

USMCA also includes unprecedented labor protections and enforcement mechanisms that will require robust diligence by those companies having operations in Mexico and/or that rely on Mexico-sourced goods in their supply chains. The labor reforms in Mexico, enforced by USMCA, will be the most dominant issue in North American trade for the next three to five years and, potentially, beyond. The COVID-19 pandemic has muted the issues over the past year; however, U.S. and international labor unions repeatedly have stated that they intend to use the USMCA enforcement mechanism in early 2021. U.S. companies operating in Mexico will be the target. Accordingly, all U.S. companies operating in Mexico need to closely evaluate and internally audit their labor-management/HR relationships "in country" to ensure compliance.

The North American "Renovation"

The positive news is that companies can readily achieve USMCA compliance. Contrary to then-President Trump's assertion that he would "rip up" the NAFTA, the USMCA includes approximately 60% of the same or similar terms found in the NAFTA and other trade agreements. Yet, the USMCA is more than a "rebrand." The approximately 40% that contains changes greatly impacts the foundation of North American and global supply chains in areas such as manufacturing, agriculture and textiles. The best way to evaluate USMCA is to envision the new agreement as a three-stage "renovation": (1) there are fresh coats of paint on more than half of the NAFTA that provide some new advantages to companies; (2) there are upgrades to the fixtures and appliances such as new provisions regarding digital trade, e-commerce, intellectual property, regulatory cooperation, competitiveness, small and medium-sized enterprises and customs facilitation (e.g., the "border"); and (3) some walls have been knocked down to establish new structures in areas such as automotive, textiles, labor and the environment. But as Tom Hanks learned in "The Money Pit," any large-scale renovation takes more than "two weeks." Companies that devote the human and time resources toward USMCA compliance will benefit from the improvements. Those that do not will be left with lost customers, compliance costs and potential labilities arising from customs, labor and environmental penalties.

USMCA "Wins" – Raw Material Imports

Before turning to the challenges, it is important to emphasize that USMCA provides competitive advantages to companies that utilize its provisions. The agreement enhances key sectors such as food processing, chemicals, polymers, coatings, electronics, and other areas where companies import raw materials or unfinished goods into North America for further production. For example, under NAFTA, North American companies were required to "trace every molecule" in the formulation process to determine if a paint, polymer, plastic or rubber product was "made in North America." Under USMCA, there are several straightforward tests that can be summarized as "if you mix it in North America, it is from North America." These streamlined processes and rules apply across a number of sectors including food production and electronics. Exploring these provisions will result in reducing compliance costs for companies and fostering greater continental competitiveness.

USMCA Challenges – Semi-Finished/Finished Imports

USMCA includes, however, significant changes that seek to prevent the duty-free entry of semi-finished and finished products into the North American supply chain. As much as USMCA concerns North American trade, its main targets are goods sourced from non-market economies (NMEs) such as the People's Republic of China. For example, the headline-capturing automotive rules of origin (ROO) raise thresholds for North American-made passenger vehicles and light trucks from NAFTA's 62.5% to USMCA's 75%. These auto ROO cascade throughout the supply chain, raising regional value content thresholds for auto parts as well as imposing 70% steel and aluminum content requirements. The auto ROO also require that at least 40% of the vehicle be produced with labor making at least $16 per hour. This labor value content (LVC) requirement restricts parts sourced from low-cost NMEs and Mexico (although some non-U.S. original equipment manufacturers (OEMs) have raised wages in Mexico to account for the LVC) in order to promote sourcing from the United States and Canada. Setting aside the political rhetoric, there is no expectation that companies will pull up stakes on existing manufacturing facilities and return to the United States. Rather, the objective is to stop the overseas and southward movement of existing supply chains as well as ensure that next-generation technologies emerge from the United States, Canada and, to some degree, Mexico. The companies most impacted by USMCA are those that have semi-finished goods from Asia in their supply chains and/or are operating in emerging areas such as electric batteries, autonomous/intelligent technologies, 5G and other telecommunications. These companies will need to closely examine their existing supply chains to determine USMCA compliance.

USMCA Certification – From a Noun to a Verb

The USMCA attempts to strike a balance by providing companies flexibility regarding the "certificate" needed to demonstrate USMCA compliance while imposing strict substantive requirements for the "certification" process. This is a sea change, as for nearly three decades, companies seeking NAFTA treatment submitted a prescribed certificate of origin (COO) that ostensibly demonstrated the criteria for claiming duty-free treatment. Companies would secure COO from their suppliers, add their information, and issue a new certificate up the chain. Over time, many companies became less rigorous in their analysis and the certificates of origin became perfunctory and, in many cases, resulted in faulty stacks of COO. Form prevailed over substance.

The USMCA fundamentally alters this certification process. The new agreement changes the passive "certificate" to the more active "certification" of origin. This is more than semantics. USMCA eliminates a prescribed form, thereby giving companies more flexibility on how to demonstrate USMCA compliance. However, companies must "show their work" and keep on file the analysis performed by in-house purchasing and finance teams, legal counsel and customs brokers demonstrating USMCA compliance. This requires companies to not accept at face value a supplier's or distributor's assertion that a good is USMCA-qualified. The company needs to "trust but verify."

Looming Labor Issues

Beyond customs compliance, the most transformative change emerging from USMCA is labor-management relations in Mexico, creating potential liabilities for U.S. companies managing their Mexico-based facilities and/or relying on products from Mexico.

Prior to USMCA, Mexico independently made constitutional reforms in areas of labor and workers' rights, yet the implementation remained stalled. The 2018 election of Mexico's President Andrés Manuel López Obrador, coupled with calls from the U.S. Congress, catalyzed the labor implementation process. Mexico thereafter commenced a review of more than 600,000 existing collective bargaining agreements, sought to adjudicate more than one million pending labor claims brought by workers, and began the formation of the regulatory and judicial infrastructure to enforce these reforms. USMCA's Labor Chapter includes many of these labor reforms and adds "teeth" in the form of a Facility-Specific Rapid Response Labor Enforcement Mechanism.

This dispute resolution mechanism is unlike anything found in the NAFTA or any other trade agreement. Any worker, union or nongovernmental organization can assert claims against any plant operating in Mexico and the governments are obliged to investigate and resolve the issue under strict timelines. The investigation may include facility audits and inspections, as well as arbitration by a standing roster of labor-minded panelists that have been selected by the countries. Penalties can include enforcement under domestic laws, imposing duties or stopping imports from that facility, and, if there are repeated offenses, stopping all cross-border shipments from the company writ large (not just from that facility/plant).

Ensuring Compliance

The honeymoon is over and now is the time to ensure compliance with USMCA. Key steps include:

- Examine the company's current use of NAFTA/USMCA commencing with an examination of existing COO/USMCA certifications issued by the company and its suppliers. A starting point may be requesting such documents from the purchasing/shipping team as well as from third-party providers such as customs brokers.
- Ensure that the company has properly classified the goods under the Harmonized Tariff Schedule of the United States and properly assessed the valuation of the goods. In many cases, the company performed this initial classification/valuation exercise years ago during NAFTA, but has not made updates during product improvements and/or consideration under USMCA. This is analysis that will require purchasing and the finance team to ensure alignment between procurement, pricing and tax strategies.
- Perform the rules of origin analysis under USMCA to determine if duty-free preferences apply, and maintain strict record-keeping procedures documenting this analysis.
- Develop a USMCA certification of origin document (many templates are available; however, do not skip the step of performing the actual analysis).
- Update purchasing documents, invoices, standard terms and conditions and shipping documents to account for USMCA changes.
- Determine areas where USMCA may provide benefits/challenges to the company and adjust processes/sourcing as needed.
- Scrutinize labor-management issues in Mexico. "Scorecards" are available and are being distributed by OEMs to suppliers. While scorecards can be useful guides, ensure that the company's internal assessments are performed by counsel, with accompanying legal and privilege protections.
- Utilize the USMCA review to update customs compliance programs. The first step in a customs verification/audit is to review the company's customs compliance manual, organizational chart and import/export records, including procedures for internal reviews/audits/spot-checks. Does your company have these policies in place?
- Incorporate USMCA issues into due diligence checklists.

After performing hundreds of USMCA reviews, experiences teaches that no company has moved from NAFTA to USMCA without making changes. Every company needs to tweak, many need to transition, and some need to transform supply chains and processes. There are lurking liabilities in faulty NAFTA COOs, failure to perform the analyses and record keeping needed under USMCA, and labor-management issues in Mexico.

Please contact Dan Ujczo with any questions.

Franchising

The PRO Act and Its Potential Negative Effects on the Franchise Industry

By Jennifer L. Maffett-Nickelman and Alan Weeter

Background

While its passage in the Senate does not appear to be imminent or likely, at least in its current form, H.R. 842 – Protecting the Right to Organize Act of 2021 (the "PRO Act"), which passed the House on March 9, 2021, and its proposed changes to employment law could upend the franchising industry as it currently exists. Among the specific topics at issue are the regulations governing joint employer status and the test for determining employee versus independent contractor status. While the National Labor Relations Board (NLRB) under the Obama administration attempted to make some of the changes proposed in the PRO Act, during the Trump administration the NLRB and the courts had essentially rolled back those attempted changes and put these issues back on a franchise-friendly footing. Not surprisingly, the tennis match is continuing under the Biden administration.

Joint Employer

Historically, the standard for assessing whether one business is a joint employer of another company's workers and, therefore, liable as an employer for any violations of labor or employment law, focused on the exercise of the right to hire or fire an employee, supervise or control an employee's work schedule, set an employee's pay rate and maintain employment records. Without the exercise of this direct control, no joint employer liability would be found.

The proposed amendment to the National Labor Relations Act in the PRO Act would broaden the definition of "Joint Employer" by considering the employer's direct control **and indirect control** over the employee's essential terms and conditions of employment. Because most franchise agreements arguably provide for some level of indirect control over the employees of the franchisee through the imposition of standard operating procedures and brand standards that necessarily impact the conditions of employment, this indirect control standard would significantly alter the currently understood and accepted franchisor-franchisee relationship.

Under the PRO Act and the expanded definition of joint employer, franchisors could be considered the direct employer of both the franchisees in their system, as well as the employees of those franchisee owners. This undermines one of the main strengths of the franchise system, which is that franchisees are the owners of their own businesses. Such an expansive joint employer standard would effectively turn franchisee owners into middle managers and increase legal liability for franchisors for treatment of employees the franchisors do not actually control. This may not only discourage entrepreneurs from starting a business as a franchisee, but franchisors may simply not be willing to take on that additional liability risk, which is truly outside of their control, and stop franchising altogether. The expected impact on the franchise industry of this proposed change cannot be overstated.

ABC Test

The PRO Act would also institute the so-called "ABC Test" to determine when individuals can be classified as independent contractors, which would result in the classification of more workers as direct employees. The proposed amendment to the National Labor Relations Act would amend the definition of "Employee" by qualifying an individual as an employee, and not an independent contractor, unless **the employer** can prove all three of the following prongs: (A) the individual is free from control and direction in connection with the performance of the service, both under the contract for the performance of service and in fact; (B) the service is performed outside the usual course of the business of the employer; and (C) the individual is customarily engaged in an independently established trade, occupation, profession, or business of the same nature as that involved in the service performed. The ABC Test has been adopted in California, and the PRO Act would make this test the national standard.

The combination of this change with the expanded definition of joint employer would likely result in making it easier for employees of franchisees to unionize, perhaps even on a franchise system-wide basis even though each franchisee is a separate, independently owned business. Other provisions of the PRO Act are also designed to generally make unionization of employees easier and provide union-friendly protections and support of union employees. The prospect of the unionization of employees across a brand would be seen by many as undermining the very concept of the franchise industry.

Whether the PRO Act, or any part of it, will gain enough support to be enacted into law remains very uncertain, but the franchise industry is watching closely.

With any questions, please contact Jennifer Maffett-Nickelman or Alan Weeter.

Government Contracts

Biden Administration Proposed Policies and Executive Actions Impacting Federal Procurement

By Francis E. "Chip" Purcell, Jr.

President Biden's new administration, both prior to and since taking office, has proposed and begun to implement policy changes that will impact federal procurement across multiple industries. While many of the policy objectives will require congressional approval and likely will evolve and change as a result of the legislative process, the president also has relied upon his executive authority to issue directives and executive orders meant to implement his objectives. Given the breadth of the new administration's pre-inaugural policy statements and post-inaugural actions, companies across the spectrum of American industry – both traditional government contractors and companies in the federal contracting supply chain – stand to benefit from actions taken by the Biden administration. We review several areas of both proposed policy initiatives and recent executive actions.

Investment in American Procurement

During the campaign, then-candidate Biden announced a $400 billion proposal to "make a historic procurement investment" that would "power new demand for American products, materials and services." The plan would support U.S. manufacturing and the domestic industrial base through new federal procurement, which would "provide a strong, stable source of demand for products made by American workers and supply chains composed of American small businesses … in vital sectors from steel and cars to robotics and biotechnology." Among the areas of focus in the plan are clean vehicles and clean energy generation capacity; American steel, cement, concrete, building materials and equipment; critical medical supplies and pharmaceuticals; and future purchases in "advanced industries like cutting-edge telecommunications and artificial intelligence." The new administration still must work with Congress to translate these objectives into specific legislation, with significant changes to the president's agenda.

Investment in Research and Development

President Biden's campaign plan for federal procurement support of American industry included a $300 billion investment over four years in domestic research and development. The plan outlines support in areas of domestic industry including advanced materials, health and medicine, biotechnology, clean energy, automobiles, aerospace, artificial intelligence, telecommunications and emerging technologies. The plan focuses on R&D conducted throughout the United States, and includes support for small businesses through a program similar to the existing Small Business Innovation Research program to assist small businesses in commercializing R&D technologies.

Infrastructure Investment

Similar to the Trump administration, President Biden has outlined a plan for significant investments in American infrastructure and transportation. The president's plan proposes a $1.3 trillion investment over 10 years focused on revitalizing existing infrastructure and implementing new transportation technologies. The plan includes an expenditure of $50 billion during the first year to "kickstart the process of repairing our existing roads, highways, and bridges" and to support federal research for new low-carbon trucking, shipping and aviation technologies. In addition, the plan would fund investment in municipal transit, aviation and airports, and freight infrastructure (including waterways and ports). As with the other aspects of the president's policy proposals, the new administration will have to work with Congress to develop specific infrastructure legislation, which may be delayed by more immediate legislative needs focused on the government's pandemic response.

Buy American Changes

While Congress has yet to take up the new president's policy objectives regarding federal procurement, President Biden has used his authority to issue several executive orders that directly impact federal procurement. Among these is an executive order issued on January 25 that would change aspects of how the federal government implements domestic preference laws, primarily the Buy American Act (BAA). Aspects of the executive order include:

- The order calls for the creation of a "Made in America" office within the Office of Management and Budget. Pursuant to the order, before an agency can grant a waiver of Buy American requirements, the agency must provide the Made in America office with a description of its proposed waiver and a detailed justification for the waiver. The director of the Made in America office must review each waiver request and make a determination in writing whether to grant the waiver request.
- The order calls for creation of a website that includes information of all proposed waivers of Buy American requirements to allow manufacturers and other parties to identify proposed waivers and whether they have been granted.
- The order directs the Federal Acquisition Regulatory Council (which oversees publication of the Federal Acquisition Regulation (FAR), the federal government's procurement regulations), within 180 days of the order, to consider proposing amendments to existing FAR requirements that would (i) replace the current component test in the FAR's Buy American Act requirements used to identify domestic end products with a test under which domestic content is measured by the value that is added to the product through U.S.-based production or U.S. job-supporting economic activity; (ii) increase the numerical threshold for domestic content requirements for end products; and (iii) increase the price preference for domestic end products.
- The order directs the FAR Council to review existing constraints on the extension of the Buy American requirements to information technology that is a commercial item, and develop recommendations lifting these constraints to further promote the policies of the executive order.
- The executive order revokes certain Buy American executive orders issued by President Trump; however, the order does not revoke the executive order issued in July 2019 that formed the basis for a FAR rule published on January 19 that implemented changes to the Buy American Act requirements in the FAR. Under that rule, the FAR's BAA requirements are changed to increase the price preference for domestic end products from 6% to 20% for small businesses and from 12% to 30% for large businesses, increase the domestic content requirement for end products from 50% to 55% calculated as a percentage of cost, and create a new domestic content requirement for commercial off-the-shelf (COTS) items that "consist wholly or predominantly of iron or steel of a combination of both" (but does not change the COTS exemption for end products outside of this new definition). (The FAR rule states that changes in the rule would apply to solicitations issued on or after February 22, 2021 and resulting contracts.)

On January 20, the new administration instituted a "regulatory freeze," directing agencies to withdraw any newly finalized rules that had not been published and consider 60-day postponements of already published rules that had not yet taken effect. However, the regulatory freeze does not affect the new FAR BAA rule based upon the FAR Council's clarification that the rule took effect on January 19, prior to the regulatory freeze. As a result, the new FAR BAA rule will govern new solicitations and contracts, and the Biden administration likely will pursue additional regulatory changes implementing the BAA.

Supply Chain Review

On February 24, President Biden issued an executive order directing a two-phase review of U.S. supply chains, aimed at assessing the overall strength of supply chains supporting various industries deemed critical. The order calls for an immediate 100-day review across specified federal agencies to address vulnerabilities in the supply chains of four key product areas: semiconductors, high-capacity batteries, critical minerals (including rare earth minerals) and pharmaceuticals and active pharmaceutical ingredients.

The order also directs a more detailed analysis over one year of broader U.S. supply chains. The one-year review will examine six key sectors: the defense industrial base; the public health and biological preparedness industrial base; the information and communications technology industrial base; the energy sector industrial base; the transportation industrial base; and supply chains for agricultural commodities and food production. The year-long review directs agencies to review risks to these industrial bases and their supply chains, including identification of critical goods and materials within supply chains, the manufacturing or other capabilities needed to produce those materials, and the vulnerabilities created by the failure to develop domestic capabilities. The review also requires the identification of locations of key manufacturing and production assets, the availability of substitutes or alternative sources for critical goods, the state of workforce skills and identified gaps for all sectors, and the role of transportation systems in supporting supply chains and industrial bases.

The review likely will yield changes to federal procurement priorities as well as the methods by which the federal government procures products and services that fall within the identified supply chains. The executive order places a priority on strengthening domestic capacity to support supply chain in the four key product areas identified by the administration. One result likely will be increased federal procurement of supply chain items in these four key product areas. The year-long analysis directed by the executive order also will focus on additional areas of the supply chains where the government will devote federal procurement funding to ensure that the various industrial bases can overcome identified weaknesses and vulnerabilities.

Conclusion

Although President Biden has been in office for less than two months, he has used his executive authority to initiate broad reviews and other actions by federal agencies that will shape federal procurement during the president’s term. The recent executive order directing the supply chain review reflects areas of priorities for federal procurement, such as pharmaceuticals and semiconductors, meant to respond to pandemic-related challenges as well as international threats. The president’s Buy American executive order also reflects a focus on prioritizing procurement from domestic sources, which will impact longer-term legislative priorities such as infrastructure spending. Both the initial executive actions and the proposed legislative priorities stand to benefit companies across a wide range of industries, particularly those with domestic manufacturing and supply capacities. Companies should continue to monitor the new administration’s executive actions and legislative proposals to track the impacts on their business, particularly with respect to opportunities related to federal procurement.

With any questions, please contact Chip Purcell.