

CONFRONTING ENVIRONMENTAL PITFALLS IN DOD OUTSOURCING AND PRIVATIZATION

**Prepared for:
National Defense Industrial Association (NDIA)**

**Tampa, Florida
April 8, 1998**

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AGENDA

- I. Introduction
- II. Overview - Outsourcing & Privatization
- III. Overview of Potential Environmental Liability
- IV. Integrating Legal, Contractual & Environmental Concerns
 - Legal Review
 - Contractual Analysis
 - Environmental Due Diligence
- V. Questions/Discussion Throughout

DRIVERS BEHIND DOD O&P

- DoD Budget Frozen at \$250B (Projected Budget “Surplus” Slated for Medicare/Domestic Programs)

- **\$15 Billion Annual Procurement Deficit (RDA historic “Billpayer”)**
 - Procurement - \$45B (\$60B per year needed (“tooth”))
 - RDT&E - \$36B
 - Military Personnel - \$69B
 - O&M - \$94B **(Target the “tail” to generate savings for Procurement)**

- “Revolution in Military Affairs” abandons “Force-on-Force” Threat (Rogue Nations & Criminal Syndicates)
 - QDR maintains 2 MRC capability (May 1997)
 - Nuclear, Biological, Chemical (“asymmetric threat”)
 - Infrastructure Attack (“hackers from hell”)

- **“Revolution in Military Affairs” to be paid for by “Revolution in Business Affairs” (RBA) (Defense Reform Initiative, November 1997)**
 - Re-engineer
 - Compete

- Consolidate

- Eliminate

WHAT DOES “RBA” MEAN TO O&P?

➤ **“Commitment to Competition” of 30K Full Time Employees (“FTE”) per year for 5 years**

- Projected savings already POM'd into FY'99 budget)
- GAO projects net savings of only \$2B in entire FYDP

➤ Examples of FTEs to be competed under Revised OMB Cir. A-76 (March 1996) (estimate \$2-3B potential new business capture per year)

- “General Maintenance” (vehicles, automotive fleets)
- “Base Support” (roads & grounds, utilities, facilities, security force, warehousing)
- “RDT&E Support” (“development testing” with data and telemetry, and “operational support” to ensure “soldier proof”)
- “Real Property Maintenance” (carpenters, electricians, painters, plumbers, and HVAC to maintain buildings and “fixtures”)

- “Data Processing” (fairly clean/low risk)
- Depot Maintenance Exempted From A-76 Under new 50/50% Rule (\$2-3B new business capture per year)
 - Fairly Dirty - - high risk operations (McClellan ALC cost \$160M for Remedial Investigation/Feasibility Study, and projected clean-up is an additional \$1.3B)
 - Army - - 13% still available (63% organic)
 - Navy - - 14% still available (64% organic)
 - Air Force - - 22% still available (72% organic)
- “Prime Vendor” and “Just-in-Time” OEM Logistics up for grabs (\$2B)
- Two More (politically charged) BRAC’s TBD (2001 & 2005)
- Utilities to be privatized (electric, gas, water and sewer infrastructure run \$2.2B annually)

“THE FLY IN THE OINTMENT”

- “Wildcard” proposed legislation: “Competition in Commercial Activities Act” (CICA II) just underwent joint hearings on Hill
 - Mandates competition of all commercial activity by 2004 (20% per year)
 - “Inherently Governmental Activity” not competed
 - Would Phase Out A-76 studies by March 1999
 - FAR 15 would then govern competitions (“best value”)
 - Contractors, incumbent agency, or “franchises” could compete
 - Would provide for agency protest of “Inherently Governmental Activity” determination
 - Agency reprograms net savings

- “Fair Competition Act of 1998” (son of “Freedom from Government Competition Act”)

THE IMPACT OF ENVIRONMENTAL LAWS ON DOD

- “Compliance” vs. “Clean-Up” (“caught between Scylla & Charybdis”)
 - Ensure Compliance with Current Environmental Requirements
 - Responsibility & Funding for Clean-Up of Contaminated Sites (\$11-12B projected on BRAC I-IV alone)

- DoD Budget - \$5B per year (“triage”)
 - Compliance (> \$2B)

 - Clean-up (> \$2B)

 - Pollution Prevention

 - Technology

- Conservation

AN OVERVIEW - COMPREHENSIVE ENVIRONMENTAL RESPONSE, COMPENSATION, AND LIABILITY ACT **(“CERCLA”)**

- Purpose - To redress sites contaminated with “hazardous substances”

- Governmental Response
 - US may unilaterally issue a clean-up order to contractor (§ 106)
 - US or State may clean up and then seek to recover costs from contractor

- Private Cost Recovery by “Potentially Responsible Parties” (“PRP”)
 - Mad scramble to “Pin the tail on the liability donkey”

- Only going to focus on CERCLA, instead of “alphabet soup” of environmental statutes (CERCLA ties together liability of other statutes)

AN OVERVIEW - CERCLA LIABILITY

➤ Trigger Elements

- “Release or Threatened Release” [42 USC § 9601 (22)]
(May include movement of previously contaminated soil during excavation/grading)
- “Hazardous substance” [42 USC § 9601(14)]
 - No quantity threshold
 - Not limited to “wastes” (RCRA)
 - approx. 725 listed substances
 - Excludes petroleum and petroleum products
- “Facility” - any place where hazardous substances are located

CERCLA DEFENDANTS

- Current “**Owner**” and Current “**Operator**” (e.g. DoD is owner/contractor is operator in O&P)
- “**Owner**” and “**operator**” at time of release of hazardous substances
- **Bottom line is that EPA/States have incentive to identify an on-site contractor as an “operator” and therefore as a PRP (“share the risk”)**
- **Consequently, “Capture net” of contractors operating on government site in O&P is huge (“embarrassment of riches”)**
- **Many contractors believe EPA/States are reluctant to designate DoD as PRP (identify “deep pocket” contractor as PRP and let it sue DoD for contribution/indemnification)**

CERCLA LIABILITY

➤ Pervasive Liability

- “Strict Liability” - liability without fault (“Liable until proven Innocent”)
- “Joint and Several Liability” - any PRP can ultimately be liable to government, or non-labile private parties, for the entire clean-up cost
- Retroactive Liability - liable for past acts (even acts that occurred prior to enactment of statute in 1980)

➤ CERCLA Defenses

- “Act of God” (rain, floods, fire, all foreseeable) or “Act of war” (not favored)
- “Act or omission of a third party” (“trespasser theory”)
 - No contractual relationship at all
 - Defendant exercised due care and third party’s actions not foreseeable
 - PRP bears burden of proof (“preponderance of evidence”)

- Better probability of winning lottery
- PRPs are liable for all “necessarily incurred response costs”
- Examples
 - monitor, assess, and evaluate the release or threat of release
 - excavation
 - collection of run-off
 - incineration
 - alternative water supplies
 - agency oversight costs (and government’s legal fees)
- Also potentially liable for
 - natural resource damages
 - interest
- “Target rich environment” of PRPs in O&P

CERCLA “CONTRIBUTION”

- Contribution actions among liable parties (§ 107&113)
- Strong industry concern over “orphan shares” of “phantom/defunct” third parties and perceived government “carve-outs”
- Judicial cost allocation based upon “equitable factors” (“In for a dime, in for a dollar”)
 - “Equitable Examples”
 - Volume of hazardous substances contributed
 - Relative toxicity of hazardous substances contributed
 - Degree of Involvement in - - Generation, Transportation, Treatment, Storage and Disposal
 - Degree of care in handling hazardous substances
 - Degree of cooperation with the Government

TWO LIKELY SCENARIOS

- I. “Pay me now/Don’t pay me later”
 - Conduct intelligent pre-award “work up” - integrate complex legal, contractual & environmental issues into coherent strategy to protect both DoD and contractor
 - Contractor performs successfully and sends signal of strong corporate resolve/competence (“deterrence”)
 - US/State do not capture unwary contractor in PRP net
 - Contractor avoids major “defense costs” and potential big ticket liability allocation in out-years (“proving the negative”)
 - If contractor discovers environmental pollution during performance, pre-award baseline facilitates “work around”

solutions to benefit of both DoD and contractor's bottom line
(Constructive Changes, Differing Site Conditions, etc.)

II. "Ignorance is Bliss"

- Pay nothing now, with little or no pre-award due diligence to properly fence off pre-existing contamination
- Pay later
 - improper SEC reporting (civil and criminal)
 - alleged "reverse" False Claims Act violations
 - protracted and expensive litigation (defense costs)
 - potential liability ("rough justice")
 - assumption of "orphan share" for "devil may care" attitude
 - lost customer goodwill
 - potential bankruptcy (hindsight is 20/20)

THREE PILLARS OF DUE DILIGENCE

- **Absolutely the key to profitable new business capture: (must have clear view of battlefield to be price competitive without blind assumption of wholesale risk)**

- I. Legal
 - Statutory/Regulatory Review
 - Proposed Legislation

- II. Contractual
 - Acquisition Planning
 - Contract Review and Assessment
 - Consideration of T&C's

- III. Environmental
 - Environmental Assessment (Three-pronged attack - documents, interviews, site assessment) (See attachments)
 - Compliance Audit - should consider?

- **Must be conducted both pre-award, and post-award, to fully baseline pre-existing contamination and set stage for “win/win” modifications to adapt to site “eccentricities” subsequently discovered during performance**

I. & II. LEGAL/CONTRACTUAL DUE DILIGENCE

- Acquisition Planning
 - Review acquisition plan (E.O. 12873)
 - Comment on RFI and draft RFPs to “massage” final contract
 - Aggressive use of Q&A’s and site visits before award (drive Indemnification T&C’s)

- Review of draft Request for Proposals (RFP)
 - “Performance” vs “design” specifications
 - Cost or fixed-price contract
 - Site Access

- **Must objectively “Firewall” off liability for pre-existing contamination to (1) mitigate downstream liability, and (2) preempt “lose/lose” disputes during performance**

- **Must craft legitimate “win/win” strategy to benefit of DoD and contractors (Options of “No Bid” or excessive price not realistic)**

III. ENVIRONMENTAL DUE DILIGENCE

➤ Environmental Assessment (Most Critical)

- Contractor's baseline for "firewalling" off pre-existing liability
- Decision making tool for "win/win" pricing strategy
- Identification of potential/past environmental liabilities
- Provides a historical document to identify environmental risks

➤ Compliance Audit

- Management tool (In-House)
- Identification of prospective liabilities during performance
- Systematic review of immediate activities (minimal resources)
 - Determine compliance with federal, state, and local environmental laws and regulations pre-award (permits are "license to drive")
 - Tailored to meet needs (e.g. air pollution, waste water control)

- Develop compliance profiles - pre-empt deficiencies during performance (“breathalyzer test”)

ADVANTAGES OF ENVIRONMENTAL AUDITS

- Advantages of Environmental Assessment (“Only get one chance to make a first impression”)
 - Identify hidden risks and on-site liabilities prior to award
 - Assist in negotiation of price, representations and warranties, indemnities, escrows for cleanup and cleanup responsibilities
 - Facilitate third party financing
 - Facilitate efforts to obtain insurance coverage

- Compliance Audits (“Be careful what you wish for”)
 - Identify potential environmental violations which occur during performance
 - Facilitate prompt responses/reporting to EPA, SEC, etc.
(minimize risk of criminal prosecution, similar to DoD IG Voluntary Disclosure Programs)

- Use to prove non-pollution during performance (“proving the negative”)

THE BOTTOM LINE

“BUSINESS IMPACT”

- **Pre-Award Establishment of Contractor’s Environmental Assessment is essential for profitable new business capture**
- Shape the acquisition strategy
- Protect contractor interests with contract provisions
- Legitimately establish non-liability for pre-existing contamination
- Legitimately lay the groundwork for “win/win” contractual modifications in event of contamination first discovered during performance (“Constructive Acceleration,” “Differing Site Conditions,” “Constructive Suspension,” etc.)

- Legitimately deter risk of “pass the buck” liability downstream, and expedite contractor escape from protracted litigation with minimal defense costs and no liability

- Lay groundwork to avoid devastating “Ignorance is Bliss” scenario
 - Avoid False Claims Act allegations by RIF’d employees in “legacy” workforce (treble damages, plus \$5K - \$10K fine per claim)

 - Avoid protracted litigation by early demonstration of non-pollution

 - Avoid potential criminal liability to both contractor and its Senior Management

- **“Return on Investment” from Environmental Assessment, and calculated Compliance Audits during performance, is very**

high, creates “win/win” scenario, and fosters long-term customer goodwill

ENVIRONMENTAL SITE ASSESSMENT RECORDS REVIEW

- Title Search

- Environmental Data Bases
 - Known and suspected waste sites
 - RCRA regulated sites
 - Leaking underground storage tanks (“UST”)

- Aerial Photographs

- Maps and other data
 - Topographic maps
 - Surface and bedrock geology maps
 - Groundwater maps
 - Fire insurance maps
 - Local street directories
 - Land use/zoning records
 - Building Department records

ENVIRONMENTAL SITE ASSESSMENT

SITE INSPECTION

- Potential Areas of Concern (not exhaustive)
 - Foundations
 - Stains/corrosion on floors, walls, or ceilings
 - Utilities (pipelines, transmitter lines)
 - Ancillary structures (e.g. railroad spurs)
 - Water supply source and location (drives “pathways” to humans)
 - Active/inactive wells (oil or gas wells, injection wells, monitoring wells, dry wells)
 - Current/historical fuel sources for heating/cooling
 - Aboveground storage tanks and underground storage tanks (including pumps, fill pipes, vents, access ways, concrete pods, saw cuts in paved areas)
 - Potential asbestos-containing materials
 - Lead-based paint
 - Hazmat storage areas
 - Stained soil or pavement
 - Landfills

ENVIRONMENTAL SITE ASSESSMENT

INTERVIEWS

- Present/former customers, tenants, and employees (e.g., property managers, physical plant supervisors, head of maintenance)
- Documents to be requested/reviewed, if possible, in conjunction with interviews
 - Existing environmental site assessment reports
 - Existing environmental audit reports
 - Environmental permits
 - Community “right-to-know” plan
 - Safety plan, preparedness & prevention plans, spill prevention, countermeasure & control plans, etc.
 - Asbestos abatement documentation, or operation and maintenance plans
 - Lead-based paint operation and maintenance plans

- Hazardous waste generator notices, reports, or manifests
 - Contracts or other information relating to methods used to dispose of solid waste and process waste waters
 - Building blueprints, construction documents, and as-built drawings
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- Inquire regarding any pending, threatened, or past litigation or administrative proceedings relating to hazardous substances or petroleum
 - Federal, state, and local agencies with probable jurisdiction over the property (status of permits, notices of violations, corrective action, on-going investigations)
 - Fire department that serves the property

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