

Suspension is not Debarment

Written by Nick Sanders
Friday, 19 June 2020 00:00

Suspension and debarment are discussed in FAR Subpart 9.4. Both are very, very serious actions that, when taken, prevent a contractor from receiving future government contract awards. But they are not the same thing.

Suspension is a serious action to be imposed on the basis of adequate evidence, pending the completion of investigation or legal proceedings, when it has been determined that immediate action is necessary to protect the Government's interest. ... Suspension shall be for a temporary period pending the completion of investigation and any ensuing legal proceedings, unless sooner terminated by the suspending official or as provided in this subsection. If legal proceedings are not initiated within 12 months after the date of the suspension notice, the suspension shall be terminated unless an Assistant Attorney General requests its extension, in which case it may be extended for an additional 6 months. In no event may a suspension extend beyond 18 months, unless legal proceedings have been initiated within that period.

While suspension is temporary and should not exceed a period of 18 months (unless legal proceedings have been initiated), a debarment lasts much longer.

Debarment shall be for a period commensurate with the seriousness of the cause(s). Generally, debarment should not exceed 3 years ... The debarring official may extend the debarment for an additional period, if that official determines that an extension is necessary to protect the Government's interest.

Government contractor KST Data, Inc. was suspended by NASA in September, 2015 based on allegations of serious misconduct. The suspension was lifted in November 2015. However, after the suspension was lifted, NASA continued to consider that KST was not a "presently responsible" contractor as that term was defined in FAR Part 9. KST considered that it had been "cleared" of the allegations of wrongdoing.

Before, during, and after the NASA suspension, KST was performing under a "Corporate Award" with Northrop Grumman. The Corporate Award was not a government contract or subcontract; instead, it was a contract to fulfill Northrop's internal needs for IT equipment such as computers and related products. KST had performed under that Corporate Award since 2010, and had met its responsibilities. One of those responsibilities was to maintain, at all times, "inventory equal to the amount of products in Northrop's quarterly forecast, plus an additional

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25%.” In other words, KST received a quarterly forecast from Northrop and had to have on hand the required amount of inventory to fulfill Northrop’s needs.

Even though the Corporate Award expressly prohibited KST from subcontracting with other firms to meet the needs of the Award without Northrop’s consent, KST entered into a supplier agreement with Synnex, who actually held the inventory until KST called for it, which would happen when Northrop issued an order to KST.

Anyway, KST was performing its duties under the Corporate Award and by all accounts Northrop was satisfied with KST’s performance.

And then KST was suspended.

KST notified Northrop of its suspension. It was clear that the suspension applied only to government procurement contracts, and was not applicable to the Corporate Award between KST and Northrop. However, upon learning of the suspension, Northrop entered KST into an internal tracking system, which prohibited all of Northrop’s operating elements from purchasing any products from KST under the Corporate Award (or any other contract).

The Corporate Award had termination provisions, but Northrop did not exercise them. It was doubtful that the suspension was sufficient to justify a termination in any case, if only because the suspension did not apply to the Corporate Award. Instead, soon after learning about the suspension, Northrop decided to “pause” placing orders under the Corporate Award pending resolution of KST’s Suspension. As a result of its decision, by October, 2015, Northrop had made a “final decision” to stop purchasing from KST (pending resolution of the suspension) but did not inform KST of that fact. At that time, Northrop decided to solicit a bid from another supplier for all of the units of computer equipment Northrop needed from its latest forecasts to KST. Not only did Northrop did not inform KST of that fact, but instead continued to tell KST that it would resume purchasing once the suspension had been resolved.

Northrop continued is “pause” until the Corporate Award expired in 2016, leaving KST Data with unsold inventory it had acquired (or contracted to acquire) pursuant to the last quarterly forecast it had received from Northrop Grumman.

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KST Data sued Northrop Grumman for breach of contract.

In the Central District of California, Judge Fitzgerald found for KST Data. Judge Fitzgerald wrote—

Quite simply, the Corporate Award did not expressly cover KST's legal situation in the Fall of 2015 – where KST does not violate the law, but was under investigation for doing so, such that Northrop did not want to continue doing business with KST. Northrop may have wished, in hindsight, that such a situation would allow it to terminate the Corporate Award for cause, but that is not how the Corporate Award was written. Instead, the Corporate Award designated several scenarios (none of which apply here) when the Corporate Award could be terminated for cause, otherwise the Corporate Award had to be terminated for convenience, which subjected Northrop to Section 6.4's requirement of purchasing up to 4,500 units it forecasted. Northrop cleverly tried to avoid the requirements of Section 6.4 by arguing that there never was a termination, just a "pause." Of course, this argument would read Section 6.4 entirely out of the contract. Under this reading, Northrop would always choose to "pause" the Corporate Award and avoid paying KST for the forecasted units at any time and for any reason, and such a reading is not plausible in light of the extensive negotiation regarding Section 6.4 specifically, and Section 6.4's importance to KST. And despite Northrop's arguments that it intended to order from KST as soon as the Suspension was lifted, its actions suggest otherwise.

Judge Fitzgerald found for KST Data and awarded the company \$3.6 million in damages. We do not know whether Northrop plans to appeal the decision.

This story is interesting in several ways.

First, notice how Northrop's purchasing system was not set up to clearly distinguish between its government subcontracts/purchases and its corporate agreements. Had the system been more robust, Northrop could have excluded KST from any government-funded purchases while continuing to use corporate funds. (Yes, you could argue that Northrop's indirect purchases were funded with government funds, but that's not how privity works.)

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Second, notice how a government suspension became a *de facto* debarment in Northrop's system. NASA suspended KST while an investigation was being conducted, but Northrop decided to take it a step further and effectively debar KST. We don't know the rationale for that decision because it was covered by attorney-client privilege. (Which tells us that legal counsel was involved in that decision.) Under oath, Northrop employees mentioned concerns about "reputational risk." Hey Northrop, how's your reputation now?

Third, notice how Northrop "cleverly" got around the financial implications of terminating the Corporate Award with KST by simply deciding to stop ordering—while telling KST that future orders were just around the corner. In essence, Northrop executed a constructive termination for convenience but didn't want to admit it had done so. Nor did it want to pay the price for having done so.

Based on the facts related in the case, we think Judge Fitzgerald got this one right.