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Contacts

Norfolk

500 East Main Street, Suite 1000
Norfolk, Virginia 23510-3889

[Kevin J. Cosgrove](#)

(757) 640-5342

kcogrove@hunton.com

[Carl D. Gray](#)

(757) 640-5322

cdgray@hunton.com

DOD Orders Cessation of Contracting Activities that Rely on Preference for Small Businesses

On March 10, 2009, the Department of Defense (“DOD”) issued a Memorandum to its agencies ordering the cessation of all procurement activities relying on 10 U.S.C. § 2323. This statute provides a preference for small business concerns, owned and controlled by socially and economically disadvantaged individuals and qualified HUBZone small business concerns; historically Black colleges and universities; minority institutions; and Hispanic-serving institutions.


The statute sets a goal of awarding 5 percent of the amount of DOD contracts to small business concerns and the other preferred entities. This goal applies to DOD agencies, the Coast Guard and the National Aeronautics and Space Administration. Congress first enacted the statute as Section 1207 of the National Defense Authorization Act of 1987, Pub. L. No. 99-661, 100 Stat. 3859, 3973 (1986), codified as 10 U.S.C. § 2323.

DOD’s Memorandum requires the immediate cessation of any activity relying on 10 U.S.C. § 2323. The Memorandum states that this includes, but is not limited to, the award of new contracts, orders under existing contracts and advance payments under contracts. It also includes the award of grants or scholarships or the addition of funds to existing grants or scholarships.

DOD issued this directive in response to an injunction and final order entered February 26, 2009, in *Rothe Development Corp. v. U.S. Department of Defense*, No. SA-98-CV-1011-XR (W.D. Tex.). The plaintiff in that case challenged the constitutionality of the current version of 10 U.S.C. § 2323 because it takes race into consideration in violation of the equal protection component of the due process clause of the Fifth Amendment.

The facts in *Rothe* involved competing bids on an Air Force contract to maintain, operate and repair computer systems at Columbus Air Force Base in Mississippi. *Rothe*, owned by a Caucasian female, bid \$5.57 million. A competitor, owned by a Korean-American couple and certified as a business owned by socially and economically disadvantaged individuals, bid \$5.75 million. Even though *Rothe*’s bid was in fact lower than the competitor, the Air Force considered *Rothe*’s bid to be \$6.1 million—or higher than the competitor’s bid—because of application of the price evaluation adjustment required by 10 U.S.C. § 2323.

The district court originally denied *Rothe*’s argument of an equal protection violation and refused to enter an injunction. *Rothe Dev. Corp. v. U.S. Dept. of Defense*, 499 F. Supp. 2d 775 (W.D. Tex. 2007). But on appeal, the U.S. Court of Appeals



for the Federal Circuit reversed the district court. *Rothe Dev. Corp. v. U.S. Dept. of Defense*, 545 F.3d 1023 (Fed. Cir. 2008). The Federal Circuit ordered the district court to enjoin application of 10 U.S.C. § 2323.

Due to the complexity of this area of procurement law, DOD's Memorandum warns its agencies that it is not possible for it to give general guidance that would apply to all situations impacted by the injunction. This same warning should apply equally to businesses under contract with DOD agencies or bidding on a contract being solicited by a DOD agency.

Hunton & Williams LLP maintains an active practice in government contracts law and has handled bid protests, claims and litigation involving DOD contracts. Please contact us if you have any specific questions concerning your contract with DOD.

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