

Inside Calif.'s New Approach To Innovation Procurement

By **Dennis Callahan and Robert Metzger** (February 20, 2019, 5:26 PM EST)

In one of the first acts of his administration, on Jan. 8, 2019, California Gov. Gavin Newsom issued Executive Order N-04-19, establishing a new acquisitions approach for the state called an “Innovation Procurement Sprint,” or IPS. Appropriate in light of Silicon Valley’s important role in the federal government’s recent push for greater use of “other transactions” for U.S. Department of Defense acquisitions, California’s new approach borrows heavily from the federal Other Transaction (OT) Guide. There is a lot of promise in this initiative, but many details yet to be worked out. Absent input from stakeholders, including the private sector, the initiative may promise more than it can deliver, and disappoint both sides of the hoped-for “public-private” partnership.



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The Vision

Newsom looks to modernize the procurement process to capitalize upon California’s “innovation economy.” He proposes a flexible new approach that asks for solutions rather than dictates requirements. Through it, the state will invite innovative proposals for prototype demonstration, with the intent of awarding production contracts to providers of working solutions. The process is designed to enable much faster procurements than can be accomplished with traditional methods.



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The executive order relies upon Public Contract Code Section 6611, which it describes as granting “broad authority” to the California Department of General Services, or DGS, and the California Department of Technology, or CDT, to utilize “flexible approaches.” PCC Section 6611 is an unusual provision, allowing the State — notwithstanding any other provision of law — to use a “negotiation process” if one or more specified conditions exist.

PCC Section 6611 authority has existed since 2003. Until recent years, it has been used sparingly, and almost always to address problems that have surfaced in information technology procurements. It was intended to allow agencies and contractors to have extended exchanges to refine the scope of work, identify potential solutions to complex problems and negotiate flexible terms and conditions. It was not envisioned as a kind of “plenary authority” that could be used outside a competitive process and without regard for other state statutes and policies, such as small business preference, that apply otherwise to all state acquisitions.

Newsom's order relies upon PCC Section 6611 and encourages the use of IPSs in many of the same ways that recent National Defense Authorization Acts have stoked the use of OTs by the Department of Defense under 10 U.S.C. Section 2371b. The federal and California initiatives share rationales, similar procedures and desired outcomes. We outline these similarities here. It is clear that the recent federal emphasis on faster, solutions-driven acquisitions and evolving conceptions of competition are migrating to the state level.

Both opportunities and peril are presented to traditional government contractors. Companies with novel or creative ideas can help the state both to define a problem and to answer the need. At the same time, this method of acquisition is unaccompanied by many of the rules and procedures, developed over decades, which are intended to assure full and fair competition, make public officials accountable for their decisions and provide transparency as to process and outcome when taxpayer dollars are spent.

No doubt, California will test new procurement methods in furtherance of the executive order. Traditional as well as non-traditional government contractors will want to observe carefully and share an interest in seeking to inform the state about how to reconcile speed and innovation with fair competitive opportunity and return on company investment. To exploit this new marketplace, companies will have to be agile, but careful.

Removing Traditional Competitive Processes

To longtime government contracts practitioners who have spent years wading through the Federal Acquisition Regulation, and have litigated breakneck U.S. Government Accountability Office bid protests, the swift advance of OTs has been bracing. The perception among OT proponents is that, over time, prescriptive and proscriptive competitive procedures have grown like barnacles on a hull, exerting a tremendous drag on federal procurements. To anyone who has seen 100,000-page procurement records with frequently amended solicitations, rounds of written discussions, lengthy proposals and best and final offers, multiple layers of technical evaluations and the like, the perception is difficult to discredit.

The process of awarding OTs is not subject to a host of traditional competition-protecting laws and processes, such as the FAR and the Competition in Contracting Act, and GAO has very limited bid protest jurisdiction over OT awards. Likewise, Innovation Procurement Sprints are not IFB or RFP processes subject to California's competitive bidding statute, Public Contract Code Sections 10340-10345, nor are their awards subject to administrative bid protests before the Department of General Services, or DGS.

Shortening the Acquisition Cycle

At the federal level, the tremendous increase in prominence of OTs in Department of Defense awards has been one of the most discussed developments among government contracts attorneys in recent years. As chair of the Senate Armed Services Committee, the late Sen. John McCain grew frustrated at the slow pace of FAR-based acquisition. He spurred the use of OTs as a way to speed the acquisition cycle to counter emerging threats, such as cyber warfare and drone attacks.

Much of the early buzz was created by the formation of the Defense Innovation Unit Experimental, or DIUx, in Menlo Park, California — In August 2018, the Pentagon dropped "Experimental" from the name, recognizing DIU's permanence within the DOD. Situated there to tap the technology hub of Silicon Valley, the DIU brokered OTs for many Department of Defense agencies in fields like artificial intelligence, automated image analysis and simulation technology that have been completed and

contracted for in a matter of weeks, not years.

In another fast-track strategy, there are now over a dozen Defense OT consortia with specific focuses, such as armaments, cyberspace and propulsion systems. These consortia often have hundreds of members, from defense contracting powerhouses to technology start-ups and universities, that have proven their interest and capabilities in the subject field. These consortia provide prevetted rosters that are able to quickly identify collaboration partners and compete for OT opportunities issued to members.

Newsom's executive order expressed themes similar to those which prompted the creation of the DIU. Specifically cited is the emergency condition that has resulted in several deadly and destructive forest fires in California over the past two years. The executive order directs that the first IPS be executed on behalf of the California Department of Forestry and Fire Protection, or CalFire, to address the "pressing need" of the "State's challenges of severe wildfires and degradation of forest health." Illustrating the expected speed advantage of an IPS over traditional IFBs or RFPs, the executive order seeks fielded prototypes this year and full production awards early in 2020. The compressed cycle, from inception to deployment, is representative of what the Pentagon also promoted — a faster transition from the demonstration of a good, innovative idea in a prototype OT to widespread deployment in a follow-on production OT or sole-source contract that benefits deployed forces and missions.

Solutions Not Requirements

A defining characteristic of the Defense OT process is that the solicitations seek solutions to complex problems, rather than providing detailed definitions of the agencies' requirements that must be met by offerors. For example, in 2017, the "area of interest" issued by the DIU and the U.S. Transportation Command for a cloud migration services OT consisted of a single paragraph. The resulting OT prototype award to a small company, REAN Cloud LLC, was initially for less than \$10 million. It grew, without further competition, to a production OT award of nearly \$1 billion before the Government Accountability Office scuttled the award for failing to meet specific statutory requirements for "follow-on production" awards.

Likewise, the executive order creates an area of interest analog, called a "request for innovative ideas." In place of a "traditional RFP process, wherein the state predefines the solution and vendors bid for a narrowly defined contract," the request for innovative ideas will "ask innovators to design solutions to [the State's] most pressing problems." And, further emphasizing the speed to fielding emphasis, the request for innovative ideas approach is designed to align California's "procurement methods with the pace of change of [the] State's greatest innovators in academia and the private sector."

Left unexplained, at least for now, is how — or by whom — the state will parse the potential needs of various departments and agencies and what criteria will be used to evaluate the readiness and potential value of offered innovations. In contrast to the federal practices for OT agreements, the executive order is not clear on whether — much less when — an innovative awardee will be compensated for its development efforts.

Prototypes to Production

The touchstone of OTs is the use of prototypes to prove the ability of a scalable solution to fill a need. So long as the prototype OT was competitively awarded — an undefined criterion, successfully completed as set forth in the agreement and provides for follow-on production, the Defense agency may award a

follow-on production OT without additional competitive procedures. The Defense Department has defined “prototype” very broadly to include designs, models or proofs of concept, and there seemingly need be no relationship between the value of the prototype OT to the value of the production OT. As a result, agencies frequently award multiple prototype OTs and effectively down-select one or more favored solution for follow-on production OTs.

Following the OT model, California’s IPS will use an iterative process where the initial awards will be for “working-solutions prototypes” or demonstrations. Based on the State’s observations and evaluations of the prototypes, the State will then negotiate production contracts. For example, among other things, the CalFire IPS, which is directed in greater detail in a companion executive order, will seek technical prototype solutions aimed at reducing fuel loading in forests and scientific prototype solutions of indicators of fire intensity, such as wind patterns and fire behavior. In rapid answer to the “crisis” of “record-breaking fires” in the last two years, the IPS executive order sets the aggressive goal of “working-solutions deployments in 2019 and final awarded deployments in Spring 2020.”

Prudent Implementation of Innovation

The use of Other Transactions has proliferated at Defense, with OT spending quadrupling over the past few years, to over \$4 billion in 2018. A great deal of public money can be expended via California’s new procurement methodologies as well. Indeed, with the IPS executive order Newsom issued companion Executive Order N-05-19, which suggests that CalFire may spend up to \$1 billion over five years through the IPS method.

To its credit, Defense has issued two fairly comprehensive OT Guides, one in January 2017, and its replacement in November 2018. Even with this considerable effort, hiccups like the REAN Cloud episode may be inevitable. And, with large OT awards routinely at stake, there has been no shortage of news reports of calls for greater transparency in particular OT processes from disappointed applicants and their congressional representatives.

In California, the leveraged statute, PCC Section 6611, while broad, is not a limitless license to “create the new” while “ignoring the old.” It was never intended to bypass competition and should not be so used, because the risk of imprudent or even improper awards is too great. Newsom’s IPS executive order charges DGS and CDT to issue guidance on the methodology. (There appears to be at least some tension between this call for guidance and the off-to-the-races nature of the CalFire IPS initiative.) Among other things, this guidance should address when the use of an IPS is appropriate, how to conduct competitions for working-solution prototypes and how to determine when a prototype is successful, such as to warrant the much greater expenditure of funds for production.

In establishing IPS guidance, the state should work with stakeholders, including industry participants. A collaborative process will improve the prospect of success and mitigate the risks inherent in California’s adoption of streamlined prototyping in acquisitions.

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