

President Trump Uses the Defense Production Act To Compel Production of Ventilators, Prohibit Hoarding in Response to COVID-19

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After first invoking the Defense Production Act (DPA) on March 18, 2020, President Donald Trump has taken several actions to formally deploy the authorities we discussed in our March 20, 2020, client alert, “President Trump Invokes the Defense Production Act in Response to COVID-19.” Most prominently, the president ordered General Motors Co. to prioritize certain contracts for the production of ventilators.

To briefly recap, the DPA grants the federal government an array of relatively broad powers in responding to national emergencies like the current public health crisis created by COVID-19, including:

- **Title I authorities:** ordering companies to prioritize certain contracts, allocating materials and prohibiting hoarding of scarce materials;
- **Title III authorities:** providing financial support, such as loans and loan guarantees, to private companies in order to increase the production of necessary materials; and
- **Other DPA authorities:** halting certain foreign investments in companies headquartered in the United States and approving “associations of private interests” to “coordinate actions” in support of the national defense and exempting them from antitrust liability.

The Federal Government’s Use of DPA Authorities To Combat COVID-19

President Trump has contemplated using most of the foregoing authorities in response to the public health crisis created by COVID-19. Taking Title I authorities first, President Trump’s Executive Order on Prioritizing and Allocating Health and Medical Resources to Respond to the Spread of COVID-19 issued on March 18, 2020, includes a finding that personal protective equipment and ventilators meet criteria to be considered “scarce and critical material essential to the national defense” under the DPA. The executive order delegates the authority to prioritize certain contract performance to the secretary of the Department of Health and Human Services (HHS).

Although the administration previously signaled that it may not need to use Title I’s authorities to direct companies to prioritize contracts in response to COVID-19, the president deployed that authority on March 27, 2020. Specifically, the president issued an order delegating authorities to the HHS secretary to “use any and all authority available under the [DPA] to require General Motors Co. to accept, perform and prioritize contracts or orders for the number of ventilators” deemed appropriate by HHS. The president’s order came shortly after General Motors announced a joint venture with Ventec Life Systems to build ventilators at one of the automaker’s manufacturing facilities. Perhaps signaling that the federal government may further utilize Title I, the president appointed White House trade adviser Peter Navarro as the national DPA policy coordinator.

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The president also has invoked Title I's authorities that guard against hoarding of scarce medical supplies. To do so, the president directed the HHS secretary to designate certain essential supplies as scarce, which makes it a crime to hoard them in excessive quantities in order to sell them above prevailing market prices. In conjunction with announcing this executive order, Attorney General William Barr stated that the Justice Department has launched investigations into those who are hoarding supplies "on an industrial scale for the purpose of manipulating the market." HHS later responded to the president's executive order by issuing a notice, effective March 25, designating 15 materials as "scarce materials or threatened materials," including medical supplies such as N-95 medical masks, ventilators, disinfecting devices and a variety of health-related personal protective equipment. Under the notice, the term "materials" includes raw materials (including critical components) and any technical information or services ancillary to the use of any such materials. The secretary's designations self-terminate in 120 days unless superseded by a subsequent notice.

On March 27, 2020, President Trump also issued an executive order invoking Title III authorities and the DPA's antitrust exemptions. The executive order, titled Executive Order on Delegating Additional Authority Under the DPA with Respect to Health and Medical Resources to Respond to the Spread of COVID-19, delegates the president's Title III authorities to the HHS secretary "to guarantee loans by private institutions, make loans, make provision for purchases and commitments to purchase, and take additional actions to create, maintain, protect, expand, and restore domestic industrial base capabilities to produce" health and medical resources. As for the DPA's antitrust exemption, the president's executive order provides that "[t]o enable greater cooperation among private businesses in expanding production of and distributing such resources," the secretary of Homeland Security and the secretary of HHS are authorized to submit any proposed voluntary agreements among private companies for presidential approval.

DPA Procedures

In light of the administration's apparent intent to use Title I's prioritization authorities, there are several important procedural considerations a company should be aware of when receiving contracts or orders relating to materials that may relate to the federal government's response to COVID-19. The Defense Priorities and Allocations System (DPAS) provides for procedures guiding the federal government's use of the DPA's Title I authorities. The DPAS provides for two different ratings for contracts issued pursuant to Title I: DX and DO. DX-rated orders have

the highest priority — taking priority over DO-rated orders and unrated orders — and DO-rated orders take priority over unrated orders. 15 C.F.R. § 700.

Orders issued pursuant to Title I generally contain certain hallmarks alerting recipients that they have been issued pursuant to the DPA. Those hallmarks include the rating, requested delivery date and following certification: "This is a rated order certified for national defense use, and you are required to follow all the provisions of the Defense Priorities and Allocations System regulation (15 C.F.R. part 700)." 15 C.F.R. § 700.12. Notably, the DPAS prohibits placing a rated order unless authorized by the DPAS. 15 C.F.R. § 700.18.

Once a company identifies the order as being issued pursuant to the DPA, three avenues present themselves. First, a company must accept a rated order if it is capable of fulfilling the order and may not discriminate against rated orders by charging higher prices or by imposing different terms than it imposes on comparable unrated orders. 15 C.F.R. § 700.13(a). The other two options are to reject the order, which are divided between mandatory and permissive rejections. A contractor must reject a rated order if it is unable to meet the date specified in the contract, but the contractor must indicate the nearest possible alternative date it can produce the goods. 15 C.F.R. § 700.13(b). Subject to the DPAS' requirement that the company does not discriminate among customers, it provides for several permissive bases for rejecting a rated order:

- if the customer placing the order is unwilling or unable to meet regularly established terms of sale or payment;
- if the order is for an item not supplied or a service not performed;
- if the order is for an item produced, acquired or provided only for the company's own use for which no orders have been filled for two years prior to the date of the receipt of the rated order. If, however, the company has sold some of these items, it must accept rated orders up to the quantity or portion of production, whichever is greater, sold within the past two years, and;
- if the customer placing the order, other than the federal government, makes the item or performs the service being ordered.

15 C.F.R. § 700.13(c). Timing is often key because if a company invokes either a mandatory or permissive basis for rejecting the contract, it must ordinarily do so within 15 business days of receiving a DO-rated contract and within 10 business days after receiving a DX-rated contract. Furthermore, if the contract is a rated order sent pursuant to a declaration of emergency, the sender may accelerate the recipient's timeframe for rejection in certain

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circumstances. The minimum time for rejecting a rated contract issued in connection with responding to an emergency is six hours after receiving the contract if the order is issued in response to a hazard that has occurred, or 12 hours after receipt if the contract is issued to prepare for an imminent hazard. 15 C.F.R. § 700.13(d) (2). Companies will be deemed to have accepted rated orders if they do not reject them within the requisite time period.

Given the narrow timeframes to reject rated orders, companies may face tensions between “social distancing” policies enacted at the state and local level mandating closures of production facilities (and personnel shortages) and their abilities to fulfill a contract issued pursuant to the DPA. Companies should determine if the applicable state or local government’s order contains an exception that would allow the company to remain open.

Lastly, companies should be aware that the DPAS obligates them to keep accurate and complete records for three years

for any rated-order transaction. Records must be maintained in sufficient detail to permit the determination, upon examination by the Department of Commerce, of whether each transaction complies with the DPAS. The DPAS does not specify any particular method for recordkeeping. 15 C.F.R. §700.91.

Conclusion

Companies should bear in mind that the extent to which the federal government will use the DPA in response to COVID-19 continues to evolve, as do legal questions posed by those actions. In all events, companies must be diligent in reviewing orders received relating to medical supplies or services and respond to them promptly, given the relatively narrow timeframe to lodge any permitted objections.

Associate **Sam Auld** assisted in the preparation of this client alert.