Government Contract Compliance: Ethics and Compliance Risk for the World’s Largest Buyer

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Contracting with the U.S. Government

• Background: The U.S. Government procures > $500,000,000,000 in goods and services annually
• Including billions to international and small business contractors who must be:
  o sufficiently sophisticated in their compliance and ethics functions to succeed in a dynamic regulatory environment, and
  o able to manage their subcontractors and suppliers in this environment
• Changing rules and priorities, and moving regulatory targets make compliance more difficult
Ethics and Compliance in Government Contracts – Why it Matters

• Government contracts entail significant transparency, substantial audit and investigative resources

• Compliance failures can result in:
  o Re-work, rejected goods, rejected invoices, schedule delays, price reductions, increased inspections and audits, contract termination
  o Negative publicity; impacted employee morale
  o Negative performance evaluations (CPARS) – leading to lost future opportunities
  o Mandatory disclosure requirements, ensuing investigations
  o Civil or criminal False Claims Act liability, Suspension and Debarment

• Can result from your actions or the actions of subcontractors and suppliers

Key Government Contract Compliance Issues

1. Ethics & Compliance Program Requirements – the Contractor Code of Business Ethics and Conduct clause
2. Unique Government Employment Laws and Regulations
3. “Buy American” and Similar Protectionist Regulations
4. Small Business Regulations
5. Truthful Cost Or Pricing Data
6. Conflicts of Interest
7. False Claims Act
8. Suspension and Debarment
1. Contractor Code of Business Ethics and Conduct

- For Government contractors, which of the following statements are true?

  A. A Contractor Code of Conduct could be 2 pages long and still be compliant with relevant Government regulations.
  B. Subcontracts performed entirely outside of the United States are not required to post Hotline posters.
  C. Contractors are required to report criminal conduct to the Government, and to disclose documents and cooperate in ensuing investigations.
  D. Small businesses are not required to have business ethics awareness or compliance programs.

Contractor Code of Business Ethics and Conduct, and Hotline Posters

- FAR 52.203-13 Business Ethics clause required if contract exceeds $5 million and 120 days
  - Applicable to subcontracts meeting same standards
  - FAR 52.203-14 (Display of Hotline Poster(s), applicable to contracts and subcontracts over $5.5 million
  - Portions of these clauses are inapplicable to: Commercial Items under FAR Part 12, contracts performed entirely outside the United States, and small businesses
Contractor Code of Business Ethics and Conduct

• Must have a written Code of Business Ethics and Conduct within 30 days of contract award
• Clause does not address the quality or content of a contractor’s code or even require that a copy be given to the Government
• Business ethics awareness and compliance program must be established within 90 days of contract award
• Mandatory disclosure rule

“Establish awareness”

• Contractors must establish an ongoing business ethics awareness and compliance program
  o Assignment of responsibility at a sufficiently high authority level
  o Reasonable efforts to exclude potential non-compliant participants
  o Periodic reviews of business practices and procedures, and internal controls
  o Internal reporting mechanism
  o Disciplinary action for improper conduct or the failure to take reasonable precautions to prevent improper conduct
Contractor Code of Business Ethics and Conduct

• Contractors shall “exercise due diligence to prevent and detect criminal conduct,” and
• “promote an organizational culture that encourages ethical conduct”
• “There is to be timely reporting, in writing, to the agency Office of the Inspector General, with a copy to the Contracting Officer, whenever the contractor has credible evidence that a principal, employee, agent, or subcontractor has committed a violation of federal criminal law in connection with the award or performance of any government contract performed by a contractor or a subcontract thereunder.”

Mandatory Disclosure

• Timely disclosure to agency IG of “credible evidence” of Title 18 violation or False Claims Act violation
• Possible Suspension and Debarment for failing to disclose credible evidence of fraud or Government overpayment
• Contractors and subcontractors must demonstrate full cooperation with any Government agencies responsible for audit, investigation, or corrective actions
• Statistics
  o Government receives ≈200 disclosures each year
  o About 70% are related to labor mischarging
Display of Hotline Posters FAR 52.203-14

- Hotline Posters required unless the contract is for commercial items or is to be performed entirely outside of the U.S.
- Best practices suggest they should be posted as a part of your comprehensive program, even if an exemption exists

2. Employment Laws and Regulations

For Government service contracts, the Government cannot require contractors to provide its service employees minimum:

A. Wage rates
B. Holidays
C. Life insurance
D. Vacation days
E. Paid sick leave
Employment Laws and Regulations

• Employment laws in the federal contract arena pose an entirely different set of issues than commercial contractors may see
• Wage and hour laws, unique benefits and reporting requirements
  o Service Contract Act
  o Davis Bacon Act
  o Federal contractor minimum wage rule
  o Paid Sick Leave rule
• Affirmative Action requirements
• Reporting and data collection – e.g. EEO1 and VETS forms
• Restrictions on Hiring Government Officials

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Employment Laws and Regulations

• Overtime rule (enjoined, subsequently withdrawn)
• Paid Sick Leave rule (effective Jan. 1, 2017) FAR 52.222-62
• Minimum wage for federal contractors, FAR 52.222-25
• Non-retaliation for disclosure of compensation information, FAR 52.222-26
• Equal pay data rule (revised EEO1 was scheduled to be due 3/31/2018; implementation currently suspended)
• Non-Displacement of Qualified Workers FAR 52.222-17
• Executive compensation: caps, reporting requirements FAR 31.025-6, 52.204-10, 10 U.S.C. 2324(e)(1)(P) and 41 U.S.C. 4304(a)(16)

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Restrictions on Former Government Officials, Ethics in Government Act

- Prohibits “revolving door,” and prevents personal gain for Government personnel entering private employment
- Prohibits personnel involved in acquisition or “personally and substantially” involved with certain matters from participating in certain future matters
- Industry and Government officials have run afoul of these rules, resulting in lost job opportunities, reputational damage, and criminal liability
- Can also result in bid protests and lost work

Restrictions on Former Government Officials, Ethics in Government Act

- Representation on particular matters - lifetime ban
- Two year restrictions concerning particular matters under official responsibility
- One year restrictions on aiding or advising
- One year restrictions on certain senior personnel of the executive branch and independent agencies
- Restrictions on lobbying - remainder of administration or 2 years
- Procurement Integrity Act also applies to certain procurement officials
- Analyses are very fact dependent and should be viewed thoroughly with both agency and company HR and counsel
3. “Buy American, Hire American”

• Which one of the following procurement actions would be prohibited under relevant “Buy American” and related laws?
  A. Purchasing $250,000 of office supplies from an Israeli supplier
  B. Purchasing $1 million of cocoa beans from a Sierra Leone based corporation
  C. Buying a $1000 ticket on British Air from LA to London, where a similar United flight would cost $2200
  D. Buying an aircraft component for $1,000,000 from a German supplier, where the least expensive U.S. supplier sells the same component for $1,550,000.00

“Buy American, Hire American”

• Key coverage areas
  o Buy America Act
  o Trade Agreements
  o Balance of Payments Program
  o Fly America Act
  o Cargo Preference Act
  o Ocean Transportation by U.S. Flag Vessels
  o E-Verify
  o Miscellaneous – Berry Amendment, food and clothing, metals and textiles; Specialty metals, recent executive orders

• Clauses generally flow down to subcontractors at every tier
Buy America Act (BAA), FAR 52.225-1,9

- Designed to promote economic growth by requiring only USA made products or services be provided for work performed in the U.S.
- Provides preferential price evaluation treatment for domestic manufactured goods and construction materials
- Remedies: fines, termination, rejection, re-work
- Domestic end product test
- Exceptions include: public interest, non-availability, and unreasonable cost

Trade Agreements, FAR 52.225-5

- Implements Trade Agreements (FAR 25.400 et seq.) and opens procurement to designated countries
  - WTO Government Procurement Agreement (GPA) and Free Trade Agreements (FTA) countries
    - including: NAFTA, FTAs of Chile, Singapore, Australia, Morocco, CAFTA-DR, Bahrain, Oman, Peru, Korea, Columbia, Panama
  - Least developed countries
  - Israeli Trade Act
  - Caribbean Basin Trade Initiative
  - Reciprocal Defense MOUs, e.g. Agreement on Trade in Civil Aircraft
- Dollar thresholds - supply and service contracts over $191,000 and construction contracts over $7,358,000 for WTO GPA; FTAs vary
Buy American/Balance of Payments Program (BPP)

• BPP applies to supplies and construction contracts performed outside of the USA - same general premise and goals as BAA, with additional exemptions
• Does not apply to purchases under $150k
• Special rules for Afghanistan, and other exemptions such as petroleum, spare parts, items for commissary re-sale
• DFARs 252.225.7000 et seq.

Fly America Act (FAA), 49 U.S.C. 40118

• Requires use of domestic carriers on Government funded air travel
• Minimal exceptions and waivers
  o No waivers for cost differential
  o Schedule waivers are complex and outdated – e.g. 24 hour extensions, 2 or more additional stops
  o Health/emergency
  o Open Skies Agreements - permits some use of non-U.S. carriers (EU, Switzerland, Australia, Japan) for non-DOD travel
• See FAR 47.4, 52.247-63, Air Transportation by U.S. Flag Carriers
Ocean Transportation by U.S. Flag Vessels

• Preference to U.S. Flag vessels whenever ocean transportation is required
  o Generally requires DOD to use U.S. flag vessels for transport of supplies for DOD unless vessels not available at reasonable rates
  o A vessel owned by U.S. resident but registered in a foreign country is NOT a U.S. flag vessel
  o Waivers may be available from the Contracting Officer
  o FAR 47.5, 52.247-64; Ocean Transportation by U.S. Flag vessels

E-Verify, FAR 52.222-54

• E-verify compares information on an employees’ I-9 form to the Dept. of Homeland Security and Social Security Administration databases
• Used by many employers nationwide, but mandatory for Government contractors
• Flowdown required for U.S. based subcontracts over $3,000 for commercial or noncommercial services or construction
4. Small Business Rules

The standard to qualify as a small business concern for Government contracting is:

A. Average annual revenues of $38.5 million
B. 500 employees
C. Average annual revenues of $21 million
D. Any privately-held company
E. Complicated

Small Business Rules

• Small Business Act - 23% of federal procurement dollars go to Small Business Concerns
  o Set-asides
  o Subcontracting
• Small business status depends on industry – 13 C.F.R. 121.201
  o >1000 NAICS codes
  o Service and construction contracts generally based upon average annual revenues
  o Supply contracts generally based upon number of employees
  o Companies self-certify, but subject to protests
  o Status complicated by affiliation rules – 13 C.F.R. 121.103
Small Business Category Rules

• Small business categories
  o Small Disadvantaged Business and 8(a) program - 13 C.F.R. 124
  o Service Disabled, Veteran Owned Small Business - 13 C.F.R. 125
  o HUBZone Small Business - 13 C.F.R. 126
  o Women-Owned Small Business - 13 C.F.R. 127

• SBA rules for small business categories
  o Set-asides by category
  o Complex rules for ownership and control to qualify
  o Rules not consistent between categories
  o Differing certification rules and status subject to protest

5. Truthful Cost and Pricing Data

True or False:
When negotiating with the Government, Contractors may be compelled to provide the Government with access to all of the contractor’s actual cost data and internal cost and pricing information.
Truthful Cost or Pricing Data

• Unique Government contracts rule regarding the disclosure of contractor data in a negotiation situation
• P. L. No. 87-653, formerly known as “Truth in Negotiations Act” (TINA); (see FAR 15.403)
• Applicable to negotiated contracts (and modifications) exceeding $750,000, unless
  o Adequate price competition
  o Commercial items and other limited exemptions
  o 2018 NDAA raises threshold to $2,000,000
• Intended to place Government in equal bargaining position
• FAR 52.215-10 et seq.

Truthful Cost or Pricing Data

• Requires contractors and subcontractors to disclose complete, accurate, current cost and pricing data
  o All data a prudent buyer would expect to affect price negotiations
  o E.g., wages, indirect rates, subcontractor costs and quotes, hours, quantities, profit
  o Certified as of date of agreement on price
  o Applies to modifications, even if not applicable to basic contract
• “Defective pricing” clauses entitles the Government to cost reductions for inadequate disclosure
6. Conflicts of Interest

True or false?
Organizational Conflicts of Interest (OCI) are strictly prohibited in Government contracting and the existence of an OCI shall cause a proposal to be rejected.

Conflicts of Interest (COI)

• Two main areas: Personal and Organizational
• Conflict of Interest rules include both civil and criminal regulations
  o 18 USC §208 - executive branch employees may not participate in a matter that will have a predictable effect on their financial interests
• Organizational COI falls into three basic areas:
  o Impaired objectivity
  o Unfair access to non-public information
  o Biased ground rules
Personal Conflicts of Interest

- Key area of concern for subcontractor selection
- Conflicts can exist with regards to family, friends, neighbors
- Can exist in the context of hiring or procurement
- Need not rise to the level of a kickback
- Companies should have a policy and a mechanism for formal disclosure
- FAR 52.203-16

Organizational Conflicts of Interest (OCI)

- Unequal Access To Information - when one firm has access to non-public information that may provide the firm a competitive advantage in a Government procurement
- Biased Ground Rules - where a company, as part of its performance of a Government contract, has some input or effect on the ground rules for a subsequent procurement
- Impaired Objectivity - when a firm’s work under one Government contract may involve the firm evaluating its own (or affiliated company) performance
- Organizational conflicts of interest often occur in contracts for: management support services; consultant or professional services; contractor performance of technical evaluations; or systems engineering and technical direction work
- See FAR 9.5
**Plans and Procedures for OCI Mitigation**

- Firewalls
- NDA Templates
- Procedures for handling, storage and transfer of sensitive information
- Subcontract templates which include clauses for subcontractor compliance and reporting
- Planned internal audits

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**7. False Claims Act**

- Which of the following statements are true regarding False Claims in U.S. Government contracting?
  A. The Government can seek actual damages, trebled, plus interest.
  B. False Claims allegations can lead to criminal charges as well as civil remedies.
  C. Contractors can be penalized an additional $20,000 for every invoice they submit to the Government.
  D. The False Claims Act was enacted as a response to Contractors taking advantage of the Government during a time of war. The Civil War.
  E. “Relators” can sue Contractors under the False Claims Act on behalf of the Government, even if the Government asserts there has been no wrongdoing.
False Claims Act 31 U.S.C. § 3729

- Imposes liability on persons and companies who defraud Government
- Enacted in 1863, the Act has been broadened by Amendments and case interpretation and serves as the Government’s primary fraud tool
- Actual damages are tripled, plus per claim penalties which range from $10,781 to $21,563 per invoice
- Qui tam provision allows “relators” to sue on behalf of the Government
- FCA cases are prominent in pharmaceuticals and healthcare, military spending, and contingency environments
- Justice Department recovered $4.7 billion from FCA cases in FY 2016, and $3.7 billion in FY 2017

Liability for any person, who: (paraphrased)
- Knowingly presents a false or fraudulent claim for payment or approval
- Knowingly makes, uses a false record or statement material to a false claim
- Has possession, or control of property or money used by the Government and knowingly delivers less than all of that money or property
- Is authorized to make or deliver a document certifying receipt of property to be used by the Government and, with intent to defraud, makes or delivers the receipt without completely knowing that the information is true
- Knowingly buys, or receives public property from an officer or employee of the Government, who lawfully may not sell or pledge property
- Knowingly makes or uses a false record or statement material to an obligation to pay money or property to the Government, or knowingly conceals or improperly avoids an obligation to pay money/property to the Government
FCA liability can be triggered by almost any aspect of Government contract performance

- Resumes, certifications, licenses
- Time cards
- Prevailing wages, worker classifications
- Invoice rates or quantities
- Quality control inspection and test results
- Small Business participation or identification
- Subcontractor substitution
- Buy America Act
- Sale/lease back agreements
- Key personnel
- Progress payments
- Substituting materials or equipment
- Indirect rates
- Third party invoices
- Travel costs
- Environmental compliance
- Overbidding and Underbidding
- Delay claims
- Design or schedule documents

8. Suspension & Debarment

- In addition to punitive remedies that can be implemented for past actions, the U.S. Government also has a system for determining “present responsibility”
- Individuals or companies found not to be presently responsible can be proposed for debarment, and suspended while these proceedings occur
- While suspended or debarred, an entity may not bid on, or be awarded any new contracts or subcontracts for more than $30,000
  - Ongoing contract work may continue
  - New awards or modifications may be allowable if in the best interest of the Government
  - Individuals may not serve as agent or representative of a Government contractor
- Debarments generally last 3 years, and an entity could be debarred more than once
Suspension & Debarment

• Each procuring agency has its own debarring official and regime
• Some agencies are more active than others (DOD most active; GSA, HUD, DHS, EPA also active)
• But activities for all agencies are on the rise – actions grew by over 130% from 2009-2016

• What is “non-responsible”
  o Unethical, dishonest, non-compliant, unable or unwilling to comply with contract requirements and laws
  o Past history of such behavior, absent any mitigation or corrective action

• SDO will review past actions, current personnel, policies and corrective actions to assess “present responsibility”
Suspension & Debarment

• What kind of actions could result in a proposed Debarment?
  o Fraud, false claims issues, bribery or kickbacks, bid rigging, embezzlement, theft, time card fraud, making false statements, crimes involving dishonesty or lack of integrity, misuse of Government property
  o Willful violations of contract terms, history of poor performance of contract non-compliance
  o Inaccurate statements on representations and certifications (reps and certs)

• SDOs have substantial discretion
  o debar entities based on “imputed conduct” of related parties
  o extend to affiliates
  o conduct can be unrelated to a Government contract (e.g. commercial fraud),
  o allegations alone are generally sufficient

Suspension & Debarment

• Exclusion is immediate; removal from the list will take months at a minimum

• Getting “off” the list will generally involve meeting with, and presenting your case to the SDO, to demonstrate present responsibility

• At such a meeting, the company will
  o present evidence and management testimony
  o answer questions and present new policies and procedures
  o propose possible independent monitoring and periodic reporting requirements
Suspension & Debarment

• FAR Factors for SDO Consideration
  o Internal controls; voluntary disclosure, disciplined employee(s)
  o Remedial measures, cooperation with investigation, ethics policy and training
  o Full cooperation, time elapsed since event, restitution, management acknowledgement of the issue

• The process is expensive
• Even once you are off the list, reputational and other damages may linger

Summary: Compliance Risk Questions for Contractors

• Which law(s) apply to your contract?
• Where is the project located? What is the dollar value?
• Is the contracting entity DOD or another Government agency?
• Are you a large or small business?
• Is your contract FFP or cost plus?
• What waivers and exemptions are available?
• What is your contract timeline?
  o The legal ability to obtain waivers is often overcome by practical schedule requirements and the cost/benefit of pursuing and waiting for a waiver
• How can you mitigate the risk of noncompliance by you or a subcontractor or supplier?
Government Contractor Best Practices

- Risk assessments
- Subcontracting drafting and indemnifications
- Employee and Subcontractor training
- Regular risk assessments
- Regular policy and procedure review
- Training (targeted)
- Review of certifications (BAA/TAA/DBA/Invoices etc.)
- Record keeping and documentation best practices
- Audits
- Corrective action
- Repeat

Conclusion

- Because of public trust issues involved in dealing with the U.S. Government (in any capacity), contractors, subcontractors and suppliers working Government contracts must be acutely aware of the many rules impacting compliance and ethical behavior
- Many of these rules may have no commercial equivalent, or a significantly more relaxed commercial equivalent
- Under the new administration we have some inconsistent trends – relaxed regulation in some areas (e.g. employment) and increased regulation in others (e.g. Buy American)
- Generally, we have seen minimal action and virtually no new regulation
- Nonetheless, contractors and subcontractors should pay careful attention to existing rules and the changing regulatory landscape
Questions?

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Glenn Sweatt is a counsel in Pillsbury Winthrop’s Government Contracts & Disputes Practice in the Silicon Valley office. He has 25 years of experience in contracts management and compliance. Previously, Mr. Sweatt was the General Counsel at a large international construction and energy government contractor. He represents clients from a wide variety of industries including construction, software and cyber security, environmental, aerospace, robotics and other service providers.

Mr. Sweatt has hands-on government contracting experience for the major Department of Defense (DOD) and civilian agencies, including the Dept. of State, Dept. of Homeland Security, and the Environmental Protection Agency (EPA), including significant experience on classified contracts. He has handled claims before the Armed Services Board of Contract Appeals (“ASBCA”) and numerous arbitrations. Mr. Sweatt’s broad background covers many facets of government contracting, with a focus on ethics and compliance issues, small business, contract administration and interpretation, and claims. He has significant audit experience with the Defense Contract Audit Agency (DCAA), Defense Contract Management Agency (DCMA), Department of Labor, and state audit agencies. Mr. Sweatt is a Certified Ethics and Compliance Professional (CCEP) with SCCE, and a CPCM and Fellow, with NCMA.

Mr. Sweatt has published numerous articles in the National Contract Management Association’s Contract Management Magazine, related to contract management, and compliance and ethics, focused on Government Contracting.
Richard Oliver is a partner in the law firm’s Government Contracts & Disputes practice and is located in the Los Angeles office. Mr. Oliver has more than thirty-five years of experience representing clients dealing with a wide range of government contract issues concerning the Department of Defense and the civilian agencies. In the course of his practice, he has frequently represented clients at the Government Accountability Office (“GAO”), the United States Court of Federal Claims (“COFC”), the Small Business Administration’s (“SBA”) Office of Hearings and Appeals (“OHA”), in state and federal courts, and before administrative boards of contract appeals, including the Armed Services Board of Contract Appeals (“ASBCA”). He has also represented clients in major criminal and civil investigations.

Mr. Oliver has counseled clients, written professionally and lectured on the Federal Acquisition Regulation (“FAR”), small business rules, bid protests, service contracts, debarment and suspension, quality assurance, changes and claims, contract compliance, and subcontractor-prime contractor disputes. He has counseled numerous clients regarding various government contracts labor and socio-economic requirements, including the coverage and requirements of the Service Contract Act.