

Federal Contracts Compliance: Understanding The Basic Rules

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Agenda

- Introductions
- Compliance system basics
 - Why compliance
 - Components of effective compliance programs
 - Rule update
- The four cornerstones of federal contracts compliance
 - Integrity in dealing with federal employees (prohibitions on bribery and gratuities, post-government employment, etc.)
 - Honesty in exchanges of information (prohibitions on false statements, false claims, etc.)
 - Maintaining proper relationships with third-parties (prohibitions on kickbacks, collusion, bid rigging, contingent fees, etc.)
 - Fairness in competition (conflicts of interest, procurement integrity, etc.)
- Addressing violations



The Case for Contractor Compliance Efforts—Why Comply

- Effective January 2008, many federal contracts (and subcontracts) contain contractor compliance requirements and the remainder recommend contractor compliance systems (see 1/08/08 webinar at <http://www.aporter.com>)
- Compliance systems reduce the likelihood of government prosecution, debarment, etc.
- Effective compliance systems reduce the likelihood of contractor wrongdoing
- Effective compliance systems encourage employee integrity



Some Recent Compliance Cases and Their Outcomes

■ Druyun And Boeing

- Former Boeing CFO Sears pleaded guilty to offering Druyun, a former Air Force top contracting official, employment at Boeing while she was reviewing whether Boeing should get a multi-billion dollar contract
- Druyun allegedly helped Boeing obtain various contracts in return for favors
- In addition to losing their jobs, Sears and Druyun both received prison sentences
- Contract awards overturned

■ Duke Cunningham

- Former Congressman Duke Cunningham pled guilty to accepting at least \$2.4 million in bribes (inflated home purchase, housing gifts, etc.) in exchange for helping several defense contractors get contracts
- Cunningham resigned from the House and received an extended prison sentence and significant fines
- Several contractors and related parties also received prison sentences and steep fines



The Components of an Effective Compliance System

A contractor's system of management controls should provide for—

- (1) **Risk mapping**;*
- (2) A **code of ethics** and **training**;*
- (3) **Periodic reviews** to ensure compliance;*
- (4) A **mechanism** for reporting improper conduct;*
- (5) **Instructions** that encourage employees to report;*
- (6) Internal and/or external **audits**, as appropriate;*
- (7) **Disciplinary action** for improper conduct;*
- (8) **Timely reporting** to the Government; and*
- (9) **Full cooperation** with Government agencies responsible for either investigation or corrective actions.*



Compliance Rule Update

- On 5/16/2008, Councils issued an Amendment to their 11/14/2007 Proposed Rule to amend 11/23/2007 Final Rule regarding Contractor Compliance (see 73 Fed. Reg. 28407)
- 11/14/07 Proposed Rule included several controversial requirements for internal controls relating to “mandatory disclosure” where reasonable grounds exist to believe a violation of criminal law occurred in connection with a federal contract and to “full cooperation” with government agencies responsible for audit, investigation
- 11/14/07 Proposed Rule also added suspension and debarment provisions related to failures to disclose overpayments and violations of criminal law



Compliance Rules Update (cont.)

- Some questioned exemptions in Proposed Rule for contracts performed outside of the United States and commercial items
- 5/16/08 Amendment *removes exemptions* for contracts performed outside the United States subjecting such contracts to code of conduct, compliance, and internal control system requirements
- 5/16/08 Amendment *partially removes exemption* for commercial item contracts extending requirements for code of conduct and prevention and detection of criminal conduct
- 5/16/08 Amendment adds suspension and debarment provisions related to a knowing failure to disclose a civil False Claims Act violation
- 5/16/08 Amendment revises contract internal control system requirements to cover these areas as well
- Comment period is open until 7/15/08



Cornerstone One: Integrity In Dealing With Federal Employees



Prohibitions on Bribery and Gratuities

- Federal law prohibits an offer or promise (directly or indirectly) to a public official (or former public official) of anything of value, for or because of an act to be performed by the official or to allow fraud (18 USC § 201)
- Severe penalties including fines and imprisonment
- Federal law also prohibits government officials from accepting bribes, gifts, and gratuities
- To avoid uncertainty, compliance plan should bar gifts to Government personnel without consent of general counsel or a senior company official

Definition of Gift

- A “gift” includes
 - any gratuity, favor, discount, entertainment, hospitality, loan, forbearance or other item having monetary value
 - services as well as gifts of training, transportation, local travel, lodgings and meals, regardless of whether provided in-kind by purchase of a ticket, payment in advance, or reimbursement after the expense has been incurred





What's Permissible?

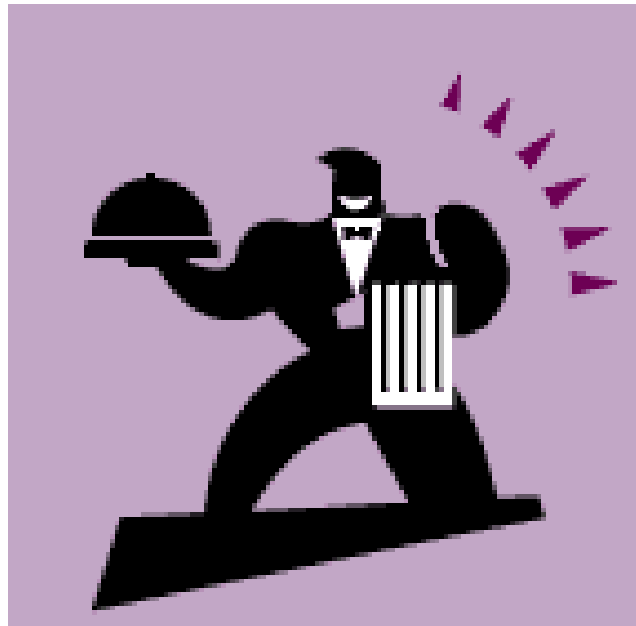
- A gift does not include –
 - soft drinks, coffee and donuts offered other than as part of a meal (*do not offer meals*)
 - items with little intrinsic value, such as plaques, certificates and trophies



Revolving Door Restrictions

- Many laws and regulations apply to post-Government employment (see, e.g., 18 USC § 207, 5 CFR 2637)
- Although most laws restrict the actions of employees, improper job offers can constitute bribes, create organizational conflicts of interest, etc.
- Employees should be directed to refer all discussions of possible employment to a human resources professional
- “Comfort letter” from ethics official and effective pre-interview questionnaires are critical parts of the compliance process (FAR 3.104-7)

Misperception: It's okay to feed a government official





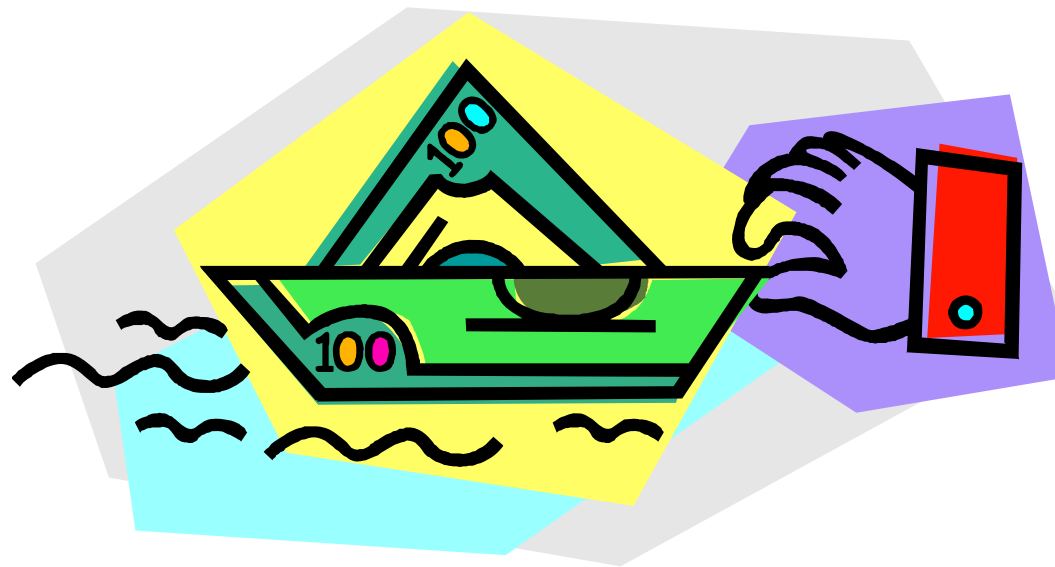
Reality:

- It is potentially against the law—both the criminal law and the government’s ethics rules—for a contractor to give government employees “anything of value,” or for government officials to accept such items
- As a general rule, contractors should not pay for meals to government employees



Misperception:

It's okay for a contractor to loan money to government officials, so long as they promise to pay it back



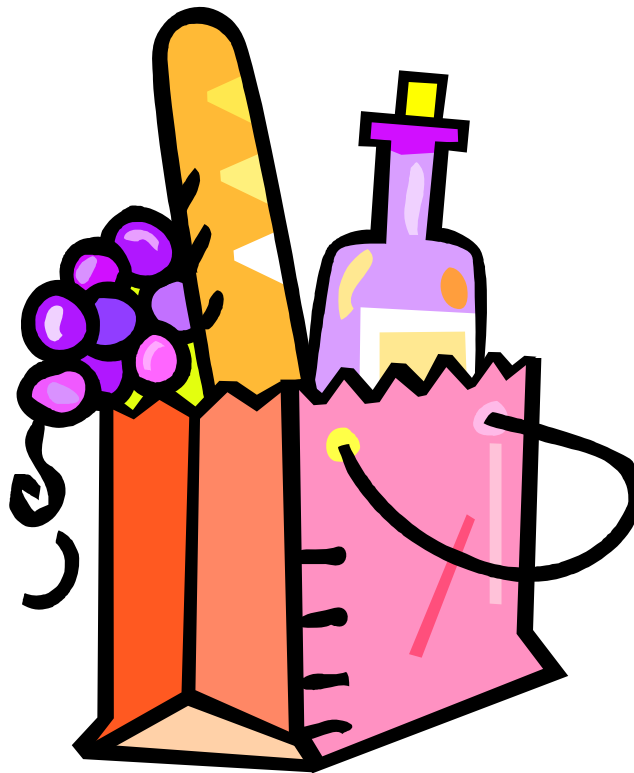
Reality:

A loan can = a criminal gratuity

- Federal law makes it a criminal offense to give “anything of value” to a government official “for or because of” an official act
- A loan is a “thing of value,” and may constitute an illegal *gratuity*
 - Federal law calls for a sentence of up to two years for a gratuity
 - The possible sentence for a *bribe* (a quid-pro-quo) is up to fifteen years in prison



Misperception:
Government employees can accept anything at a trade show



Reality:

“Small Item” exception is limited

- Under the gift rules, government officials may accept up to \$20 per donor, up to a total of \$50 per year, per donor
- This includes low-value items given out at trade shows
- **But the exception extends to all items from a single corporation—they may not exceed \$50/year per official**



Misperception:
It's illegal for a contractor to be friends with a government employee



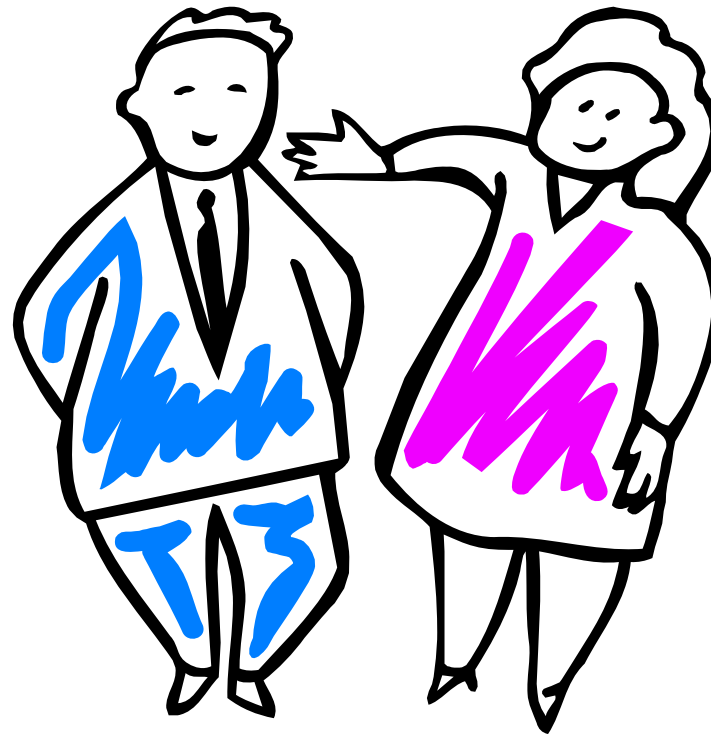
Reality:

Friendship is okay—but be careful

- Items given to a government employee, if there is a true friendship, are not “gratuities” because they are given out of friendship—not “for or because of an official act”
 - but be prepared to explain that friendship to third parties . . . including an investigator
 - do your friend a favor: don’t give or accept gifts that will raise concerns
 - avoid gifts that originate from your company



Misperception: It's Okay for a Contractor To Recruit a Government Employee



Reality:

Recruiting Triggers Ethical Requirements

- The “revolving door” ethical requirements are very complex
- A procurement official may have to **recuse** herself from all procurements
- Other government employees have **similar requirements**, under other laws
- Organizational conflicts of interest can arise
- Job offers can constitute bribes or gratuities in certain circumstances
- **Bottom line: have employees contact HR department or general counsel before even beginning the process**



Darleen Druyun

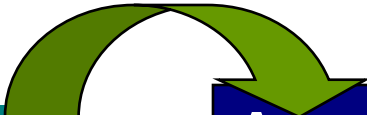


Cornerstone Two: Honesty In Dealings With The Government

Prohibition Against False Statements

**Whoever
makes
A Material False
Statement
To the Government**

Knowingly and Willfully



**Any oral or written
false statement (or
omission) to
support a false
claim, or to corrupt**

**Shall, per 18 USC § 1001, be criminally
liable for up to 5 years in prison and/or
\$10,000**

Avoiding False Statements Liability

- The False Statements Act (18 USC § 1001) provides a sweeping, frequently used mechanism by which the Government can penalize contractors which are dishonest in their dealings with the Government
- To reduce the likelihood of liability, contractor compliance systems should (at a minimum):
 - prohibit employees from making knowingly false statements or statements in deliberate ignorance of the facts
 - require employees to take reasonable steps to confirm the accuracy of information before submission to the Government
 - centralize material contract communications
 - develop a centralized proposal preparation and review process
 - develop a centralized plan for certification review and submission

Prohibition Against False Claims (18 USC § 287 and 31 USC § 3729)

Basis for Liability

1. Submission of “claim for payment” to the federal government;
2. The claim is “false” or “fraudulent;” and
3. The defendant acted “knowingly.”

DAMAGES:

1. Triple the amount of damages suffered by the United States PLUS
 2. A civil forfeiture of between \$5,500 and \$11,000 per false claim;
- damages can be reduced in some cases from triple to double
*criminal penalties also exist

Means . . .



1. Actual knowledge;
2. Acts in deliberate ignorance of the truth or falsity of the information; **or**
3. Acts in reckless disregard of the truth or falsity.

Avoiding False Claims Act Liability

- The False Claims Act is one of the Government's primary weapons against fraud – recoveries exceeded \$15 billion between 1987 and 2005
- Avoiding liability requires training and systems designed to ensure (among other things) that employees
 - charge all labor and material costs accurately and to the appropriate account
 - do not falsify time reports or other records
- Contractors also should
 - develop redundant invoice review systems
 - conduct periodic, random audits to verify rates, amounts, etc.
 - promptly correct errors (including return of mischarges)

Cornerstone Three: Maintaining Proper Relationships With Third Parties

The Federal Government's Interest in Other Relationships

- Recognizing that corruption below the prime contract level also impacts the federal government contracts system, many statutes and regulations also target contractor relationships with third parties
- A number of commonly applicable statutes and regulations impact relationships with third parties by
 - prohibiting kickbacks - the Anti-kickback Act of 1986, 41 USC § 51, *et seq.*, FAR 52.203-7
 - prohibiting bid rigging, FAR 52.203-2
 - prohibiting sharing of price information with competitors, FAR 52.203-2
 - restricting the use of contingent fee arrangements, FAR 52.203-5
 - barring use of federal appropriated funds to lobby the Government in connection with award of contract, cooperative agreement, or loan, FAR 52.203-11

Prohibition Against Kickbacks

- The Anti-Kickback Act of 1986, 41 USC § 51, *et seq.*, prohibits offering, providing, soliciting, or receiving kickbacks in connection with Government contracts and subcontracts
- The Act defines a "kickback" as "any money, fee, commission, credit, gift, gratuity, thing of value, or compensation of any kind which is provided, directly or indirectly" to any prime contractor or subcontractor or their employees "for the purpose of improperly obtaining or rewarding favorable treatment in connection with a prime contract or in connection with a subcontract relating to a prime contract"
- Any person who knowingly and willfully engages in conduct prohibited by the Act can be imprisoned for up to 10 years, subjected to a fine, or both
- Mandatory reporting where reasonable grounds exist to believe a violation occurred

What Can Be a “Kickback”?

- Meals
- Money
- Trips
- Souvenirs
- Gift Certificates
- Invitations to attend or participate in any sporting, hunting, or other event
- Any other item of value



Avoiding Compliance Issues Related to Dealings with Third Parties

- Avoiding liability requires training and systems designed to ensure (among other things) that employees:
 - do not provide, solicit, or accept gifts or entertainment from other contractors
 - do not share pricing information with any third party absent management knowledge and consent
 - do not engage in bid rigging or market division schemes of any sort
 - do not offer to pay fees contingent on award of a federal contract absent management knowledge and consent
 - do not use amounts paid from a federal contract to lobby Congress or an executive agency for the award of a contract
 - seek legal or management counsel prior to discussing exclusive teaming or subcontracting relationships with any third party
 - design oversight systems to ensure competitive, fair selection of subcontractors and teaming partners



Cornerstone Four: Fairness In Competition



Selling in Government Contracts

Proper: Exchanges of information among potential offerors and the Government, from “the earliest identification of a requirement through receipt of proposals.” Exchanges broaden Government understanding; agencies are encouraged to foster exchanges. After solicitation is issued, contracting officer is focal point for exchanges. FAR 15.201.

Improper : Procurement Integrity Violations (FAR 3.104):

- No bribe/gratuity
- No official conflict of interest
- No receipt or disclosure of sensitive commercial information belonging to others

POSSIBLE PENALTIES:

**SUSPENSION, DEBARMENT and
CRIMINAL**



Prohibitions Against the Solicitation of Proprietary or Source Selection Information

- The Procurement Integrity Act, 41 USC § 423, restricts the scope of permissible communications between a contractor competing for a procurement and federal employees
- The Act prohibits a contractor, during the course of a federal procurement, from: (i) discussing with or making an offer of employment or business opportunity to any procurement official; (ii) offering or giving, or promising any money, gratuity, or other thing of value to any procurement official; or (iii) soliciting or obtaining, prior to award, any proprietary competitor bid or proposal information or source selection information from any officer or employee of a procuring agency
- The Act provides for criminal, civil, and administrative penalties



Identifying PPA Bid or Proposal Information

- Bid or proposal information means any of the following information submitted as part of a federal procurement and not publicly available:
 - cost or pricing data
 - proprietary information about manufacturing processes, operations, or techniques marked as proprietary by the contractor
 - information marked as “contractor bid or proposal information”
 - information marked with Government restrictions on disclosure and use

Identifying PPA Source Selection Information

- Protected source selection information includes any of the following information used or prepared for bid or proposal evaluation (FAR 3.104-3):
 - bid prices or lists of bid prices prior to public opening
 - proposed costs or prices or lists of same
 - source selection plans
 - technical evaluation plans
 - technical or cost evaluations of proposals
 - proposal rankings
 - competitive range determinations
 - other information marked “SOURCE SELECTION” information



Consulting and Contract Management Support

- If authorized—generally by contract—to have access to source selection information or other contractors' bid or proposal information:
 - use only for official/authorized purposes
 - disclose only to Government and company personnel specifically authorized to receive it
 - safeguard from unauthorized disclosure
 - avoid Organizational Conflicts of Interest

Avoiding Procurement Integrity Violations

- Avoiding liability requires training and systems designed to ensure (among other things) that employees:
 - do not request or accept competitor bid or proposal information or source selection information from Federal Government employees or consultants during the conduct of a federal procurement, unless authorized to do so
 - do not disclose such information to any person not authorized to receive it
 - identify (in advance) and avoid or mitigate personal and organizational conflicts of interest
 - properly mark and handle company proprietary information (e.g., FAR 52.215(e))

Misperception:

It's improper for a contractor to talk to a contracting official about an upcoming procurement





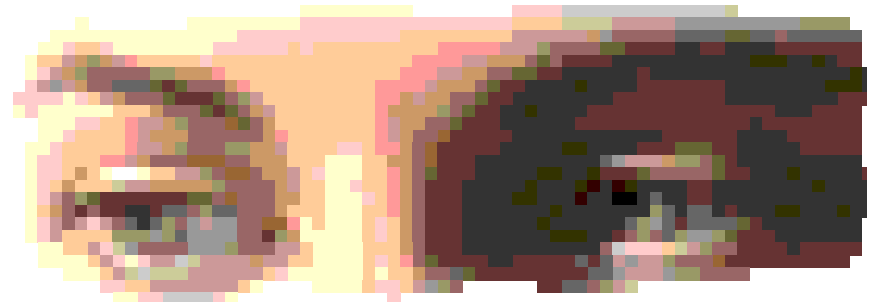
Reality:

- Federal procurement regulations encourage interactions with industry before a solicitation is issued
- After the solicitation is issued, the contracting officer should control any further exchanges





Misperception:



“All is fair in love and government contracting”—it’s okay to use a competition to “sneak a peek” at competitors’ information

Reality:

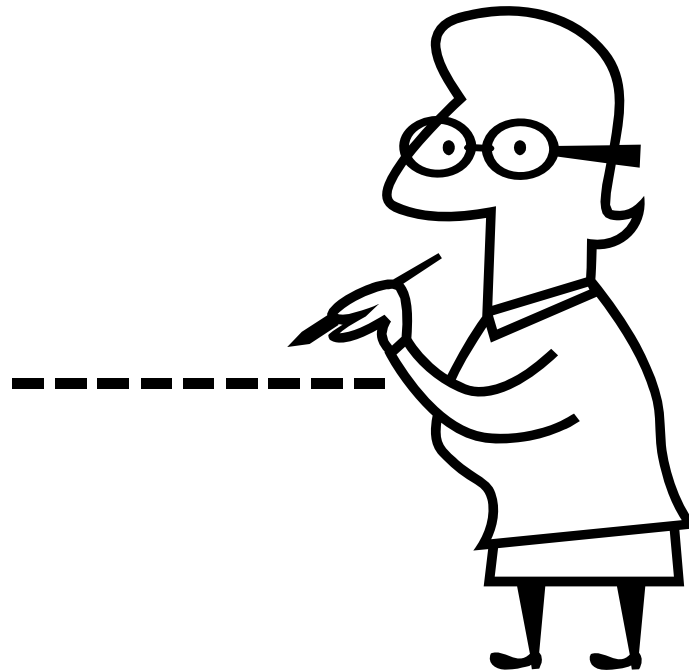
It is illegal to steal inside information

- **Procurement Integrity Act bans improper access to:**
 - Bid and proposal information from other bidders
 - **Source selection information** (information used by the Government evaluators and procurement planners)

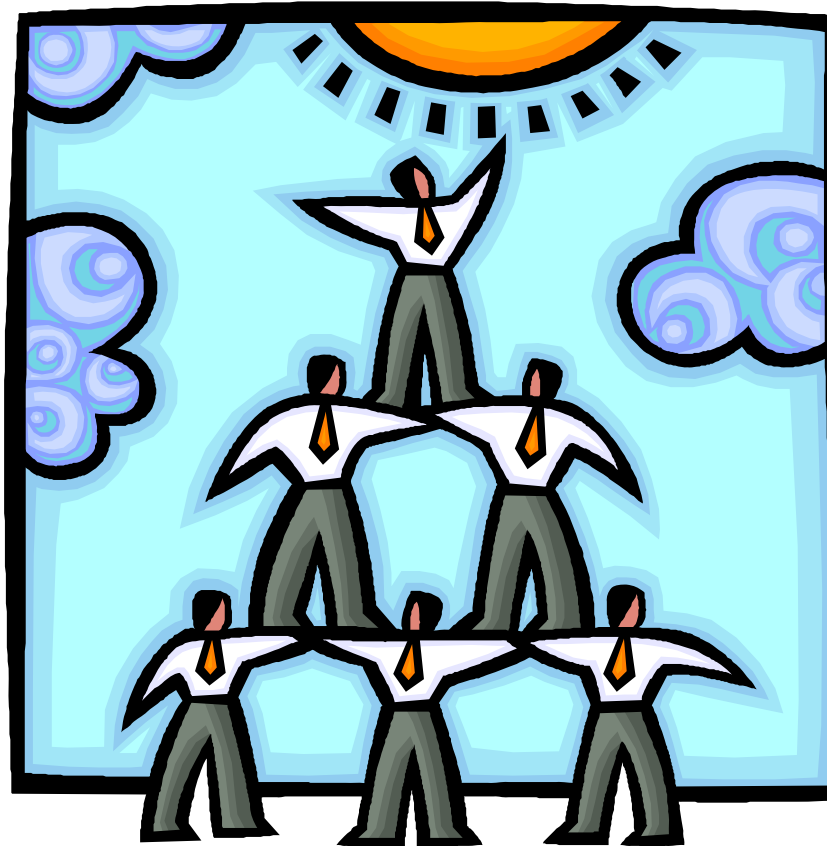


Misperception:

Only the folks in the contracting department need to worry about federal compliance



Reality:
Compliance is everyone's responsibility



Compliance is About Making Sure Perceptions Match Reality

- The ethics and procurement integrity rules are extremely complex
- Too often, the problem is that employees have misperceptions regarding the rules
 - **Goal of compliance training is to align your understanding with the rules**





Handling Reports of Improper Conduct

- Handling reports of contractor misconduct is a topic unto itself and beyond the scope of this briefing
- Some limited comments
 - contractors should encourage reporting
 - except in the most clear-cut instances, contractors should investigate all reports, to include an interview with the source of the report
 - contractors should protect whistle-blower from retaliation
 - contractors should consider involving counsel in the investigation
 - if an investigation identifies potential contractor wrongdoing, the contractor should consider prospective and retrospective corrective action and reporting obligations



The Relationship of the Cornerstones to Compliance

- The cornerstones identified help form the foundation of federal contract compliance but the statutes, rules, and regulations potentially applicable to differing types of government contractors number in the thousands
- Risk mapping is critical to determine other areas of focus, e.g., MAS contractors—price reductions, manufacturers—Trade Agreements Act, substantial cost reimbursement contractors—TINA, etc.
- When all else fails, including time, apply the so-called “Washington Post” test—remembering that not all requirements are intuitive



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