

Ethics Corner

Final Rules on Mandatory Disclosure

**BY DORN C. MCGRATH
& SEAN M. CONNOLLY**

The April 2008 Ethics Corner, “New Rules For Federal Contracts,” explained the Federal Acquisition Regulations (FAR) mandate for contractor codes of ethics effective Dec. 24, 2007. Although the ethics program provisions required attention and implementation, they were largely unobjectionable.

By contrast, additional changes to the same ethics program rules were proposed in November 2007, as requested by the Department of Justice and later mandated by Congress. This included highly controversial “self-reporting” requirements. This proposal to impose a system of “mandatory voluntary disclosure” on government contractors triggered much discussion in 2008. There was some hope that the final rules would represent a balanced and well thought-out approach to ethics and compliance, rather than a blanket self-reporting of any possible occurrence of a criminal law or civil False Claims Act (FCA) violation. That hope was dispelled with the publication of the final self-report rules on Nov. 12, 2008. (FAR Case 2007-006, Contractor Business Ethics Compliance Program and Disclosure Requirements, found at 73 Fed. Reg. 67,064.)

Effective Dec. 12, 2008, government contractors will face what rule authors characterize as a “sea change” in how government enforcement authorities expect to govern in the future. The final rules require new standard contract clause language for contracts projected to exceed \$5 million and 120 days of performance and extend to small businesses, commercial item contracts, and contracts performed entirely overseas. Subcontracts also are covered, requiring prime contractors to “flow down” the self-disclosure and related requirements.

Casting inspector generals as the focal

point for contract administration issues represents the most dramatic change. Contractors must now self-report to the IGs where there is “credible evidence” of FCA and federal criminal law violations (involving fraud, conflict of interest, bribery, or gratuities). This will have a huge effect on contract administration, for both contractors and the government’s contracting officers. The new rules will drive contractors to seek legal analysis of issues historically resolved informally with the contracting officer. Going forward, informal resolution with contracting officers may not be a viable option, at least until the cognizant IG has reviewed the language and performance of contract work, and formed legal opinions on myriad procurement issues.

More now than before, contractors must gauge accurately what constitutes “credible evidence” of those violations covered by the rules. This obligation cannot be easily ignored. The new rules call for suspension or debarment for “knowing failure” to make timely disclosures. The suspension and debarment regulations do not limit mandatory self-disclosure to FCA and federal criminal law violations. Any “significant overpayment” now triggers this obligation. The suspension and debarment rule appears to be retroactive, and applies to any government contracts, including contracts entered before the rule’s effective date and until three years after final contract payment. A contractor’s record of integrity and business ethics also is now specifically listed in the FAR as relevant past performance information for purposes of future contract award competitions.

Many questions remain unanswered by the new rules. For example, what is a “timely” disclosure? What is a “significant” overpayment? What is “credible evidence?” However, in one important concession, after many comments filed by industry and other interested parties over the course of 2008, the rule writers admit that contractors still may rely on attorney-client privilege in working through procurement issues, without risking failure to be in “full cooperation” with the government.

The Defense Department and the General Services Administration, among other agencies, plan to set up a web-based disclosure process. The rule provides that the

government must notify a contractor if a third party seeks release of this proprietary or confidential information under the Freedom of Information Act (FOIA). It may be possible to prevent or limit government-released records depending on how the FOIA process unfolds, as well as the administrative FOIA appeals, or lawsuits to block disclosures.

Contractors, other than small businesses or commercial item vendors, must also maintain an “internal control system” to ensure timely disclosures to the government. The rule explains that it was the government’s intent to “spell out” requirements for internal control systems. At a minimum, contractors should compare their current compliance plans to FAR 52.203-13(c)(1), and (2) to examine the requirements for the following:

- Assignment of responsibility at a high level and adequate resources to ensure effectiveness of an ethics and compliance program;
- Reasonable efforts to exclude individuals as “principals” if they have engaged in conduct that conflicts with the code of business ethics;
- Periodic compliance reviews of business practices and procedures;
- An internal reporting mechanism, such as a hotline;
- Disciplinary action for improper conduct or for not taking reasonable steps to prevent or detect such conduct;

This new era of self-reporting is just the beginning, and it inevitably will raise novel and difficult issues that will challenge government contract administrators and counsel alike. It therefore is critically important that contractors be proactive in educating a broader spectrum of their workforce as to what is and what is not lawful conduct, periodically reviewing company business practices, procedures, policies, and internal controls; and carefully self-reporting whenever there is “credible evidence” of wrongdoing expressly covered by the new rules.

Dorn C. McGrath is a Shareholder (mcgrathd@gtlaw.com) and Sean M. Connolly (connollys@gtlaw.com) is a Senior Associate with Greenberg Traurig LLP, as members of the government contracts practice group. The views expressed are solely those of the authors.