



Mandatory Disclosures for Federal Government Contractors: What, How, and When?



Kara M. Sacilotto
Kevin B. Muhlendorf

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Overview

- Statistics of Interest
- Disclosure Obligations
- Whistleblower World
- DOJ Policy Changes
- Tips to Mitigate Risks

Statistics

■ DOD IG

- Over 5,700 contacts to the DOD Hotline from Oct. 1, 2017-Mar. 31, 2018
 - Most related to personnel misconduct, personnel-related matters, reprisal complaints, and improper procurement or contract administration matters
- 940 whistleblower reprisal complaints to DOD IG or Component IG
 - 84 concerned defense contractor reprisal
- 113 contractor disclosures, as required by FAR 52.203-13
 - Largest percentage of disclosures related to labor mischarging (68%)
 - **Fewer than half the reports than from one year ago** (274 in Oct. 2016-Mar. 31, 2017)

■ GSA IG

- 5 contractor disclosures received Oct. 1, 2017-Mar. 31, 2018
 - Also less than year ago (7 for period Oct. 2016-Mar. 31, 2017)
- Concluded evaluation of 8 disclosures, recovering over \$1.4 million (M)

Statistics

- Dec. 21, 2017: [Department of Justice \(DOJ\) reports](#) False Claims Act recoveries for Fiscal Year (FY) 2017
 - \$3.7 billion (B) (one billion less than FY2016)
 - \$2.4B from health care industry, including drug companies, medical device companies, hospitals, nursing homes, labs, and physicians
 - \$543M from financial industry re housing and mortgage fraud
 - Procurement fraud recoveries ran the gamut:
 - \$95M (plus foregoing \$249M in claims) to resolve allegations of overcharging for local produce provided to soldiers in Iraq/Kuwait
 - \$125M to resolve allegations that charged DOE for deficient nuclear quality materials
 - \$45M to resolve allegations that made false statements and claims to GSA in negotiation of software licenses
 - \$29.5M to resolve ARRA overcharging allegations
 - \$16M to resolve allegations involving small business program eligibility

Statistics

- DOJ (cont'd)
 - Whistleblowers filed 669 *qui tam* suits in FY2017 – “an average of more than 12 new cases every week”
 - Of the \$3.7B recovered, \$3.4B related to *qui tam* suits
 - Even though FCA recoveries overall declined, *qui tam* suit recoveries **increased** (\$3.4B in FY2017 vs. \$2.9B in FY2016)
 - DOJ paid out \$392M to whistleblowers
- ISDC
 - Agency suspensions and debarments decreased 14% in FY2017 over FY2016 (604 suspensions, 1613 proposed debarments, and 1423 debarments in FY2017)
 - Even decreased numbers represent nearly double the activity reported in FY2009, when the ISDC began tracking this data
 - Proactive outreaches by contractors before a debarring official raises concerns also decreased from 76 to 53 between FY2016 and FY2017
 - Pre-notice letters (e.g., show cause) increased 21%

FAR Mandatory Disclosure

- FAR 52.203-13, Contractor Code of Business Ethics and Conduct
 - Business ethics awareness and compliance program, generally tracks Federal Sentencing Guidelines requirements for effective compliance and ethics program
 - Internal control system that allows the company to timely discover improper conduct
- Mandatory Disclosure Requirements in FAR 52.203-13:
 - Must “timely” disclose “credible evidence” of certain procurement-related federal criminal violations and violations of civil False Claims Act to Agency Office of Inspector General (OIG)

FAR Mandatory Disclosure

- Mandatory Disclosure Requirements in FAR 52.203-13 (cont'd):
 - Applies to all covered contracts (>\$5.5M and 120 days), and must be flowed down to covered subcontractors
 - Although small businesses and commercial item contracts exempt from 52.203-13(c) compliance program and internal controls requirements, not exempt from mandatory disclosure obligations. *See* FAR 52.203-13(b)
 - Noncompliance with disclosure obligation is ground for suspension/debarment under FAR 9.4 (knowing failure of “principal” to “timely” disclose “credible evidence” of enumerated procurement-related and significant overpayments)

How Do You Know What To Disclose?

- Guiding Principles:
 - Policy and practice must encourage reporting. If you see something, say something
 - The goal is to be proactive, not reactive
 - How would you explain to a neutral third party a decision NOT to disclose?
 - Bad news does not get better with age
 - The “cover-up” is worse than the crime

FAR Mandatory Disclosure: Managing the Investigation

- Overview of structure of corporate/internal investigations at BAE Systems
 - Chain of command
- Initiation of investigation: the intake process
- Who investigates?
- How are investigations tracked?
 - “Timely” not defined in rule or preamble (73 Fed. Reg. 67064 (Nov. 12, 2008))
 - Rule contemplates sufficient time to conduct investigation to determine whether “credible evidence” exists
 - “Reasonable steps that the contractor considers sufficient to determine that the evidence is credible”

FAR Mandatory Disclosure: Managing the Investigation

- Use of templates, scripts
- How to handle employees who are reluctant to talk to internal/external investigators or who might be involved in wrongdoing?
- How are investigations findings and results documented?
- When to hire outside counsel
- When to hire other outside professionals (computer forensics, accountants)

FAR Mandatory Disclosure: Managing the Disclosure

- What is the process for determining whether a disclosure is required?
 - Internal coordination of decision-making
 - Obligation rests with the “principals” of the company. What is a “principal”? Net is cast both broadly and ambiguously
 - “Officer, director, owner, partner, or a person having primary management or supervisory responsibilities within a business entity (e.g., general manager; plant manager; head of a division or business segment; *and similar positions*)
- Drafting the disclosure
 - Use and views on “batch” disclosures
 - Standard letter format?
 - Remedial measures in disclosures?
 - Discipline discussed in disclosures?

FAR Mandatory Disclosure Insights

- Disclosures to DOD IG are sent to DOJ and Agency SDO as matter of course
 - DCIS and DCAA may also become involved
 - DOD IG practice to promptly send letter that their office is “coordinating with the Department of Justice and Defense agencies with equities or interest in the disclosure”
 - Routine to route disclosures to civil/criminal DOJ
 - Does not necessarily mean a DOJ judgment has been made

FAR Mandatory Disclosure Insights

- All mandatory disclosures are reviewed in the Criminal Division by the Fraud Section in Washington
- Very few disclosures result in cases being opened by criminal prosecutors. Many more are acted on by DOJ Civil
- Vast majority of disclosures are time charging violations, many very minor. Vast majority of them indicate discipline had been handed out
- Cases that are further criminally investigated are brought to DOJ attention by OIG or picked up from a *qui tam*, not on basis of mandatory disclosures

FAR Mandatory Disclosure Insights

- Characteristics of a criminal case:
 - Loss (greater flexibility when conduct threatens a government mission)
 - Pervasiveness of misconduct
 - Clarity of contractual or regulatory “ground rules”
 - Presence or absence of certifications
 - Internal communications (emails, recorded calls, etc.)
 - Evidence of concealment

FAR Mandatory Disclosure Insights

- DOD IG requires information on individuals involved in disclosed conduct
 - Often leads to inquiry from SDO regarding present responsibility of individuals
 - May affect security clearance
- Discipline is two-edged sword
 - Discipline expected by some regulators; others may not think it is enough (i.e., scapegoat or larger organizational issue?)

FAR Mandatory Disclosure Insights

- Remedial measures?
 - If you make a disclosure, behooves you to address consideration/remediation
 - Prevent retention of an overpayment
 - Address the matter “timely”
 - Get ahead of the SDO
- Close Out Notice?: DOD IG and GSA IG state that they generally provide written notice to contractor if agency decides to close a disclosure

FAR Mandatory Disclosure Insights

- Regulator position: *no de minimis* amount
 - Some regulators bemoan the quantity of disclosures vs. quality of disclosures
 - Some regulators question whether “all” misconduct reported
- Your idea of “credible evidence” may not be the same as the regulator’s view
 - Overly legalistic analysis?
 - How will you explain the failure/absence of a disclosure to a regulator?
- Subcontractor disclosures
 - Upstream FCA implications for prime
 - Advance notice to the subcontractor?

Other Sources of Disclosure Obligations

- **Grants, 2 C.F.R. 200.113**
 - Requires organization to disclose “in a timely manner” to the awarding agency or pass-through entity “all violations of federal criminal law involving fraud, bribery, or gratuity violations potentially affecting the federal award”
- **DFARS rule promoting “voluntary post-award disclosure of defective pricing,” finalized May 4, 2018, DFARS 215.407-1(c)(i)**
 - Relates to findings of defective pricing when contractor provided certified cost or pricing data
 - To promote voluntary contractor disclosures of defective pricing, gives DOD contracting officers discretion to discuss disclosure with DCAA and, as necessary, request a limited-scope or full-scope audit
- Disclosure to CO

Other Sources of Disclosure Obligations

- **Overpayments, FAR 52.232-25(d)**
 - If Contractor becomes aware of a duplicate contract financing/ invoice payment or that Government has otherwise overpaid, Contractor must remit overpayment with a description of the circumstances of the overpayment, affected contract/deliver order and line items along with supporting documents
 - Disclosure to CO
- **Reps and Certs in SAM and FAPIIS, e.g., FAR 52.209-5 and 52.209-7 (Responsibility Matters)**

Other Sources of Disclosure Obligations

- **Anti-Kickback Act, 41 U.S.C. §§ 8701-8707, implemented in FAR 3.502, Subcontractor Kickbacks, and FAR 52.203-7**
 - Disclosure obligations similar, but not identical, to mandatory disclosure. *See* 41 U.S.C. § 8703; FAR 3.502-2(g) and FAR 52.203-7(c) (2)
 - “reasonable grounds to believe” standard
 - Criminal, civil, and administrative penalties
- **Combating Trafficking in Persons, FAR Subpart 22.17 and FAR 52.222-50**
 - FAR 52.222-50(d) requires contractor to: (1) “notify” CO and Agency OIG of any credible information that a contractor employee, subcontractor employee or agent has engaged in conduct that violates 52.222-50(b) (policy and list of prohibited conduct); and (2) any actions taken against a contractor employee, subcontractor employee or agent pursuant to clause

Other Sources of Disclosure Obligations

■ SEC Disclosure Obligations

- Do you have to disclose allegation of fraud, a CID, or an SEC subpoena?
 - It depends, but generally no automatic duty to disclose
 - *Richman v. Goldman Sachs Group, Inc.*, 868 F. Supp. 2d 261 (S.D.N.Y. 2012) (no duty to disclose receipt of SEC Wells notice)
- Have to disclose if there is a Rule, such as “material” legal proceedings in SEC Regulation S-K, Rule 103
- Have to disclose if failing to do so would render another disclosure misleading
- Investigation could reveal internal control failings requiring disclosure

Disclosures in a Whistleblower World

- [SEC](#) Whistleblower Program
 - Over 4,400 whistleblower tips in FY2017
 - Number of tips has increased every year since FY2011
 - 50% more than first year with full program data (FY2012)
 - In FY2017, Corporate Disclosures and Financials accounted for highest percentage (19%) of complaint type; Offering Fraud was second most common complaint (18%); Manipulation was third (12%)
 - In FY2017, SEC awarded \$50M to 12 individual whistleblowers
 - Three of the ten largest awards were in FY2017
 - \$322M awarded to 58 whistleblowers since program inception

DOJ Corporate Enforcement Policy

- Corporate criminal liability is resolved through either indictment, guilty plea, deferred prosecution agreement, non-prosecution agreement, or declination
- Outcome depends on “Filip Factors” listed in USAM 9-28.300
 - Nature and seriousness of offense
 - Pervasiveness of wrongdoing and managerial involvement
 - History of misconduct
 - Cooperation
 - Existence of effective compliance program
 - Timely and voluntary disclosure
 - Remedial actions
 - Collateral consequences to public and shareholders
 - Adequacy of other remedies, such as civil enforcement or debarment
 - Adequacy of prosecution of individuals

Factor Four: Cooperation

- Cooperation is connected to the adequacy of criminal prosecution (“Yates Memo”)
- Cooperation generally involves:
 - Revealing results of internal investigation (without waiver of privilege)
 - Review and disclosure of emails; documents; and audio files (litigation holds are essential)
 - Making current employees available for interview
 - Coordination of interviews with DOJ (tip: adverse employment actions and public filings may impact investigation)
 - Assessment of loss
 - Cooperation in court processes
- Continued cooperation through DPA or NPA agreements

Factors Five and Seven: Compliance Policies

- Fraud Section Guidance on “Evaluation of Corporate Compliance Programs” (available online) issued in February 2017
- Includes 11 key compliance metrics and a set of “common questions” that DOJ considers in assessing compliance programs; DOJ prosecutors and consultants will test these 11 factors:
 - Analysis and Remediation of Underlying Misconduct (“how did this slip through?”)
 - Involvement of Senior and Middle Management in the compliance program.
 - Autonomy and Resources of compliance program (independence and resources)
 - Policies and procedures (including identification of who at the company was responsible for integrating policies into the compliance program)
 - Risk assessment (e.g., identifying problem areas by geography or industry)
 - Training and Communication
 - Confidential Reporting and Investigation (avenues to report misconduct)
 - Incentives and disciplinary measures (bonuses, promotions, termination)
 - Periodic testing and review
 - Third party management (watching the subs)
 - Mergers and Acquisitions

How Do You Manage/Mitigate The Risks?

- Careful preparation of disclosures given wide audience
 - Just the facts
 - Facts are not privileged
 - Avoid admissions and waiver of privilege
 - Truthfulness
 - Completeness
 - Remedial/corrective actions
 - Ducks in a row BEFORE disclosure
 - Balance “timely” with sufficient understanding of facts
 - Consider preliminary disclosure for complex/lengthy investigations

How Do You Manage/Mitigate The Risks?

- Understand and anticipate that employees identified in disclosure may find themselves contacted by regulators
 - Effective internal investigation before disclosure
 - Be prepared for “target” to claim status as “whistleblower” and have in place anti-retaliation policies
 - Is the misconduct of a single employee a broader indicator of misconduct within the organization?
 - If that employee is the target of enforcement actions (e.g., suspension/debarment), what is the company’s policy and response?

How Do You Manage/Mitigate The Risks?

- Disclosures include more than just FAR mandatory disclosure obligation
 - E.g., various SAM/FAPIIS and other reps and certs are numerous and can be complicated. Include update requirements as well
- Be on the lookout for other disclosure “opportunities”
 - Pre-acquisition due diligence may uncover corrupt payments where disclosure could result in DOJ/SEC declination
 - Pair disclosure decision with compliance review and remediation