

New FAR Requirements for Mandatory Disclosure Take Effect

Widespread Implications for Every Entity Holding a Federal Government Prime or Subcontract

By Robert M. Osier, Esq.



On December 12, 2008, a major revision to the Federal Acquisition Regulation (FAR) went into effect with far-reaching consequences for every entity that has a federal government prime or subcontract. The Federal Register

notice accurately describes this modification as a “sea change” in the fundamental approach to compliance followed by the Government.” (73 Fed. Reg. 67064.) With the anticipated increase in federal construction work due to stimulus legislation, the time to prepare for the new FAR provisions is right now.

MANDATORY DISCLOSURES BY CONTRACTORS

As a practical matter, the new FAR provisions will require every contractor (and major subcontractor) who does or plans to do business with the federal government to disclose to the government agency’s Office of Inspector General (“OIG”) all “credible evidence” related to a government contract of: (1) violations of criminal law involving fraud, conflict of interest, or bribery; (2) violations of the civil False Claims Act; or (3) significant overpayments. These FAR provisions not only apply to all contracts entered into with the Federal Government after December 12, 2008, but also to all open contracts, and all contracts closed out within the previous three years.

The mandatory disclosure requirement has two separate sources: (1) changes to FAR Part 9 making the failure to disclose violations a basis for suspension and debarment; and (2) a new contract clause at FAR 52.203-13, which applies to all contracts in excess of \$5 million and with a duration of at least 120 days, imposing a duty to disclose and an elevated obligation to use due diligence to discover violations that must be disclosed. Thus, failure to disclose is now grounds for suspension and debarment for anyone selling to the government directly or indirectly. Further, for

contracts exceeding \$5 million and 120 days, failure to disclose is also a breach of a specific contract provision mandating disclosure.

A. What Is To Be Disclosed: Credible Evidence of Violations or Overpayments

The mandatory disclosure is required if the contractor’s principals have knowledge of “credible evidence” of a violation of criminal law involving fraud, conflict of interest, bribery, or a violation of the False Claims Act, or receipt of significant overpayments from the Federal Government. In addition to reporting evidence of its own violations and overpayments, the contractor is required to disclose credible evidence of known violations and overpayments by subcontractors under its federal contracts. Although “credible evidence” is not defined in the new regulations, the contractor takes a significant risk if it decides that a disclosure was not required because of a legal theory that is subject to challenge by the Justice Department.

B. Mandatory Disclosures by Subcontractors

A prime contractor must also include the FAR 52.203-13 clause in all subcontracts with a value in excess of \$5 million and performance period of at least 120 days. Thus, through the new clause, many major subcontractors on federal projects will have an independent mandatory disclosure requirement, even if they have no direct contract with the Federal Government.

C. When and How To Make the Disclosures

The FAR rules require the “timely” disclosure but do not set any specific boundaries on what would be considered a timely disclosure. The government, however, does acknowledge that the contractor will need a reasonable time to conduct its own investigation into the issues. But government inspector generals have already taken the position that once a contractor discovers credible evidence of a

violation, it should promptly make disclosure to the relevant agency OIG, with a copy to the contracting officer responsible for the contract, without waiting for completion of the contractor’s investigations.

INTERNAL CONTROL SYSTEM AND TRAINING REQUIREMENTS


All new contracts that meet the \$5 million/120 day threshold must adopt “an ongoing business ethics awareness and compliance program.” FAR 52.203-13(c)(1). Under the clause, a contractor has 90 days after receiving its first contract including the new FAR contract clause to establish an enhanced internal control system, unless it can convince the contracting officer that more time is needed.

The internal control system requires the following elements: (1) mandatory disclosure; (2) periodic reviews of company practices, procedures, policies and internal controls; (3) reporting mechanism that offers anonymity; (4) disciplinary action for improper conduct; (5) assignment of responsibility at a sufficiently high level of the organization; (6) devotion of adequate resources to ensure effectiveness of the ethics awareness and compliance program; (7) reasonable efforts to exclude individuals who have been engaged in illegal or unethical conduct from the contractor’s senior management; and (8) periodic assessments of risk of criminal conduct. FAR 52.203-13(c)(2)(ii). These detailed requirements apply to all contractors unless they qualify as small businesses or receive exclusively commercial contracts.

The FAR provision also requires the contractor to provide training to its personnel to communicate the standards and procedures and other aspects of the contractor’s business ethics awareness and compliance program and the newly required internal control system.

WHAT TO DO NOW

At a minimum, contractors should begin by taking inventory of their principals' knowledge of prior misconduct. Additionally, as described above, to ensure compliance with the new FAR provisions requiring an internal control system to actively uncover violations and overpayments, contractors should review their existing systems and promptly make the necessary changes.

If a contractor discovers evidence of possible violations or overpayments requiring disclosure, the contractor should initiate, through counsel, an internal investigation right away to ensure a "timely" disclosure, if one is needed. An effective and thorough internal investigation by counsel before disclosure will not only provide an assessment of the contractor's potential criminal exposure but produce materials which, if disclosed to the government, may be helpful in convincing it that the contractor is presently responsible to obtain government contracts. 

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