

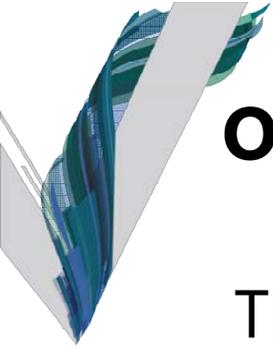
VENABLE

Mandatory Disclosures:
Best Practices for Protecting Your
Company's Interests in the Current
Compliance Environment

Wednesday, May 17, 2017
12:00pm – 1:30pm ET

MODERATOR:
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SPEAKERS:
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Objectives

The goal of this presentation is to provide:

- A working knowledge of the fundamental principles of the FAR Mandatory Disclosure Rule;
- An understanding of the federal government's expectations for contractor cooperation; and
- Takeaways for avoiding suspension and debarment for failing to disclose fraud, conflicts of interest, bribery, or gratuity violations.



What Is the Mandatory Disclosure Rule?

- Requires the Mandatory Disclosure of
 - Criminal violations involving fraud, conflicts of interest, bribery, or gratuities under Title 18 U.S.C.;
 - Civil False Claims Act violations; and
 - Significant overpayments.
- Other requirements:
 - Contractor Code of Business Ethics and Conduct requirement (FAR 52.203-13(b)) requiring contractors to have a written Code of Ethics and develop internal procedures to detect, process, investigate, and assess potential violations to determine whether there is credible evidence triggering a reporting obligation.
 - Established requirement for a Business Ethics Awareness and Compliance Program and Internal Control System (FAR 52.203-13(c)) to be in place within 90 days of contract award.



What Is the Risk of Not Disclosing?

- A contractor may be suspended or debarred for a knowing failure by a **principal** to timely disclose to the government, in connection with the award, performance, or closeout of a government contract performed by the contractor or a subcontract awarded thereunder, **credible evidence** of
 - Violation of federal criminal law involving fraud, conflict of interest, bribery, or gratuity violations found in Title 18 of the United States Code;
 - Violation of the civil False Claims Act; or
 - **Significant overpayment(s)** on the contract, other than overpayments resulting from contract financing payments.
- **Principal** means an officer, director, owner, partner, or a person having primary management or supervisory responsibilities within a business entity. This definition should be interpreted broadly, and could include compliance officers or directors of internal audit, as well as other positions of responsibility. (FAR 2.101)



When Does Your Company Have to Disclose? Can We Conduct an Internal Investigation before We Disclose?

- Timely disclosure:
 - The Mandatory Disclosure Rule allows contractors the opportunity to do some preliminary examination of the evidence to determine its credibility before deciding whether to disclose to the government.
 - No set time frame defines “timely.”
 - The “timely” requirement should be read in the context of the “credible evidence” standard, which provides for a period of internal investigation to determine whether evidence is credible before it is disclosed.
 - Contractors should take reasonable steps to determine evidence is credible, not launch a complex investigation.
 - No time frame for what constitutes a “reasonable investigation.”
 - Measured from contract award or discovery of credible evidence, whichever is later.
 - Disclosure requirements under the clause apply prospectively from December 12, 2008; however, examination of past conduct on contracts open to exposure is still required.





What Must Companies Do?

- Must fully cooperate with all government agencies responsible for audits, investigations, or corrective actions.
- Rule does not require:
 - Contractor to waive its attorney-client privilege or attorney work product protections.
 - An officer, director, or employee to waive his or her attorney client privilege or Fifth Amendment rights.
 - A contractor to refrain from conducting an internal investigation or defending a proceeding or dispute arising under the contract or related to a potential or disclosed violation.
- Comply with the requirements in QPR 1.2-007, Responding to Government Investigations Procedure, by contacting the General Counsel's office when notified of a government audit, investigation, or corrective action or if you are aware of a matter that may be considered reportable under the Mandatory Disclosure Rule.



Other Contractual Obligations Required – A Code, Compliance Program, and Internal Controls

- Code of Business Ethics and Conduct (FAR 52.203-13 (b))
 - Required to have written Code. ✓
 - Make available to each employee engaged in performance of the contract (electronic access included). ✓
 - Exercise due diligence to prevent and detect criminal conduct. ✓
 - Otherwise promote an organizational culture that encourages ethical conduct and a commitment to compliance with the law. ✓



Other Contractual Obligations Required – A Code, Compliance Program, and Internal Controls

- Compliance Program & Internal Control System (FAR 52.203-13(c))
 - Within 90 days after being awarded a covered contract, ongoing business ethics awareness and compliance program must be in place. ✓
 - Required to have steps in place to communicate periodically and in a practical manner the aspects of the compliance program and internal control system, by conducting effective training programs and otherwise disseminating information. ✓
 - Establish standards/procedures to facilitate the timely discovery of improper conduct in connection with government contracts (e.g., hotline). ✓
 - Ensure corrective measures are promptly instituted and carried out. ✓
 - Assigns high level of responsibility to individual for compliance with adequate resources. ✓
 - Includes periodic audits and reviews of business practices and internal controls (both operational functions and the Code of Ethics and Conduct program). ✓
 - Disciplinary action for improper conduct for failing to take reasonable steps to prevent or detect improper conduct. ✓
 - Include reasonable efforts not to employ individuals as principals who have engaged in conduct that conflicts with the Code of Ethics and Conduct (vetting of promotions with Compliance & Ethics/General Counsel's office and background checks on new candidates).
 - Timely disclosure, in writing, to agency OIG (copy CO) re credible evidence of wrongdoing under Mandatory Disclosure Rule.
 - Does not apply if the Contractor is a small business concern, or if contract is for the acquisition of a commercial item.



False Claims Act Defined

- The Civil False Claims Act (“FCA” or “Act”) imposes civil penalties and damages on parties that submit false or fraudulent claims to the federal government. A person can be found liable under the Act based on seven situations.
 - **Situation Number 1:** Any person who knowingly presents, or causes to be presented, a false or fraudulent claim for payment or approval.
 - **Situation Number 2:** Any person who knowingly makes, uses, or causes to be made or used, a false record or statement material to a false or fraudulent claim.
 - **Situation Number 3:** Any person who conspires to commit a violation of [this Act].
 - **Situation Number 4:** Any person who has possession, custody, or control of property used, or to be used, by the Government and knowingly delivers, or causes to be delivered, less than all of that money or property.
 - **Situation Number 5:** Any person who is authorized to make or delivers a document certifying receipt of property used, or to be used, by the Government, and, intending to defraud the Government, makes or delivers the receipt without completely knowing that the information on the receipt is true.
 - **Situation Number 6:** Any person who knowingly buys, or receives as a pledge of an obligation or debt, public property from an officer or employee of the Government, or a member of the Armed Forces, who lawfully may not sell or pledge the property.
 - **Situation Number 7:** Any person who knowingly makes, uses, or causes to be made or used, a false record or statement material to an obligation to pay or transmit money or property to the Government, or knowingly conceals or knowingly and improperly avoids or decreases an obligation to pay or transmit money or property to the Government.



What Constitutes a Claim Under the Civil False Claims Act?

- A “claim” is:
 - Any request or demand, whether under a contract or otherwise, for money or property and whether or not the United States has title to the money or property, that:
 - Is presented to an officer, employee, or agent of the United States; or
 - Is made to a contractor, grantee, or other recipient if the money or property is to be spent or used on the Government’s behalf or to advance a Government program or interest, and if the United States Government:
 - Provides or has provided any portion of the money or property requested or demanded; or
 - Will reimburse such contractor, grantee, or other recipient for any portion of the money or property which is requested or demanded; and
 - Does not include requests or demands for money or property that the Government has paid to an individual as compensation for federal employment or as an income subsidy with no restrictions on that individual’s use of the money or property.



“Knowingly” Presenting a Claim That Is False or Fraudulent

- The Act defines “knowing” and “knowingly” as:
 - [A] person with respect to information—
 - has actual knowledge of the information;
 - acts in deliberate ignorance of the truth or falsity of the information; or
 - acts in reckless disregard of the truth or falsity of the information,
 - and no proof of specific intent to defraud is required
- To establish “reckless disregard” the government must show:
 - “Aggravated gross negligence,” “gross negligence-plus,” or an “extreme version of ordinary negligence”



Implied Certification

- In *Universal Health Services v. Escobar*, the U.S. Supreme Court upheld the theory that “implied certification” would remain a viable theory of liability under the False Claims Act. The Court explained that when “a defendant makes representations in submitting a claim but omits its violations of statutory, regulatory, or contractual requirements, those omissions can be a basis for liability if they render the defendant’s representations misleading with respect to the goods or services provided.”



Implied Certification

- Specifically, the Supreme Court held that implied certification could be a basis for FCA liability when:
 - “the claim does not merely request payment, but also makes specific representations about the goods or services provided”; and
 - “the defendant’s failure to disclose noncompliance with material statutory, regulatory, or contractual requirements makes those representations misleading half-truths.”



Penalties and Damages for an FCA Violation

- Recovery of penalties up to three times the amount wrongfully charged to the government (treble damages), and
- Fines between \$5,500 and \$11,000 per fraudulent claim.
 - The Bipartisan Budget Act of 2015 allows for agencies to increase the fines, which many agencies have done (including the SBA and DOD) to \$10,781 to \$21,563.
- The government may also be able to recover interest.
- Penalties are limited to two times amount wrongfully charged if full disclosure is made to government within 30 days of knowledge of violation, there is full cooperation with the investigation, and no government investigation is pending at the time of disclosure.



Defenses to an FCA Claim

- Although the government's burden is fairly low for establishing an FCA violation, there are several potential defenses, including:
 - Government knowledge
 - Reasonable interpretation
 - Reliance on expert counsel
- Successful performance of a contract or achieving grant goals is NOT a defense.



False Claims Act

- Particular problem areas:
 - Sloppy time charging
 - Inflated equitable adjustment claims
 - Failure to distinguish funds from different projects at all times



Potential Indicators of Fraud

- Cost mischarging examples:
 - Unallowable costs (political contributions, certain entertainment costs, advertising)
 - Labor mischarging (transfer of labor costs, time sheet fraud, ceiling limitations)
 - Commercial vs. government contracts
 - Material mischarging and product substitution



Indicators of Fraud

- Product substitution examples:
 - Delivery of look-alike goods made from non-specification materials
 - Providing foreign-made products where domestic product is required
 - Failure to properly test materials
 - Falsification of test documents



Indicators of Fraud

- Other red flags:
 - Lapses in the enforcement of the Code of Conduct or similar policy
 - Transferring charges from one delivery order to another
 - Unexpected resignation or replacement of key management personnel
 - Managers retroactively assigning charge numbers
 - Weakening in the company's financial condition (e.g., recurring operating losses)
 - Actual results not meeting forecasts



Indicators of Fraud

- Other red flags (cont'd):
 - Unexpected year-end transactions that result in significant revenues
 - Unusual accounting practices for revenue recognition and cost deferral
 - Changes in accounting methods that are designed to enhance profit numbers
 - Changes in independent accountants that resulted from disagreements



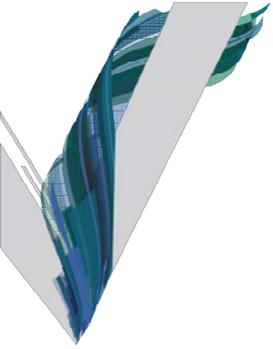
Practical Tips

- Know your company's compliance policies and ensure that your employees are familiar with them:
 - Proposal and grant application preparation
 - Cost accounting and billing
 - Government ethics and whistleblower policies (ideally, with some provision for anonymous reporting of complaints and potential violations)
- Review federal contract, subcontract, and grant opportunities carefully to identify all requirements and certifications, including:
 - Required express and implied certifications in proposal
 - Cost accounting and cost principle requirements
 - Invoicing instructions

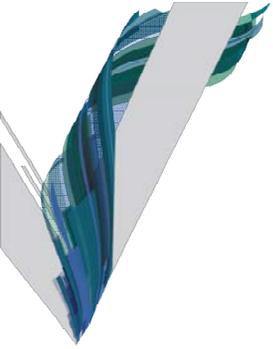


Practical Tips

- Educate employees about the FCA
- Talk to employees about potential problems and encourage them to err on the side of caution
- Ensure employees understand the terms of contracts they work under
- Document and justify costs
- Channel communications to the agency through a single (or a few) representative(s)
- Consider exit interviews for former employees



Key Takeaways



Questions?

Next Month's Government Contracts Webinar:

Escobar Update

Wednesday, June 21, 2017

12:00pm-1:30pm ET