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January 14, 2008

VIA FACSIMILE (202) 501-4067 AND FIRST-CLASS MAIL

General Services Administration
Regulatory Secretariat (VIR)
1800 F Street, NW
Room 4035
ATTN: Laurieann Duarte
Washington, DC 20405

Re: FAR Case 2007-006, Contractor Compliance Program and Integrity Reporting

Dear Ms. Duarte:

Holland & Knight LLP appreciates the opportunity to provide comments on the proposed rule published on November 14, 2007, in the Federal Register.[1] Holland & Knight is an international law firm that performs significant work for government contractors. These comments have been prepared jointly by members of Holland & Knight's Government Contracts National Practice Group and our Global Compliance and Governance Team.

Holland & Knight's Government Contracts Group represents and counsels businesses that sell services and supplies to the Federal government. We help government contractors and subcontractors minimize risk and maximize value from the beginning of the procurement process through contract close-out. Our counseling services include such issues as cost and pricing data, cost accounting, intellectual property, small business and other socioeconomic programs, labor and employment, domestic buying preferences, export control, teaming and subcontracting, and internal compliance programs. We represent clients in bid protests, contract claims, requests for equitable adjustment, government audits and investigations, and "qui tam" actions under the False Claims Act.

Holland & Knight's Global Compliance and Governance Team guides companies in proactive compliance and governance planning. We offer a broad range of services to help

[1] FAR Case 2007-006, Contractor Compliance Program and Integrity Reporting, 72 Fed. Reg. 64019 (Nov. 14, 2007) (the "Proposed Rule").

implement or upgrade compliance and ethics programs, including risk assessments, due diligence, compliance investigations, independent monitoring, training, and records management assistance. We conduct internal investigations and assist companies in both formal and informal voluntary disclosures. We represent companies that come under investigation by a variety of government agencies and law enforcement authorities.

Introduction

Holland & Knight understands and supports the Proposed Rule's stated goal of conformity with the elements of an effective compliance and ethics program as they are set forth in the United States Sentencing Commission Guidelines Manual, §8B2.1 (the "Sentencing Guidelines"). Such conformity will serve to reduce confusion and avoid what could otherwise be a false sense of security among contractors who comply with the requirements of the FAR's recently adopted Code of Ethics Rule[2] yet unknowingly fail to comply with all of the requirements of the Sentencing Guidelines. For most contractors, the "ongoing business ethics and business conduct awareness program" and the "internal control system" required by the Code of Ethics Rule will involve implementation of most, if not all, of the elements of a Sentencing Guidelines compliance and ethics program. The Sentencing Guidelines criteria are more clearly stated, however, and we believe contractors will be better able to develop, implement, and monitor their programs using the Sentencing Guidelines, rather than the more amorphous guidance of the Code of Ethics Rule. Formal adoption of the Sentencing Guidelines as the standard for contractor programs will also have the benefit of creating a uniform set of criteria to apply across multiple government agencies and law enforcement authorities, no matter whether the contractor program is being evaluated by contracting agencies, offices of inspector general, Federal prosecutors or sentencing judges.

Holland & Knight does have serious concerns, however, regarding certain components of the Proposed Rule. As currently drafted, the Proposed Rule requires more than the Sentencing Guidelines do. It may negate numerous and long-standing agency "voluntary" disclosure programs, and it could be read as unlawfully interfering with the necessary and well-established protections of the attorney-client privilege.

Specifically, this comment addresses concerns about the following provisions of the Proposed Rule:

(1) the requirement to "notify, in writing, the agency Office of Inspector General with a copy to the Contracting Officer, whenever the Contractor has reasonable grounds to believe that a principal, agent or subcontractor of the Contractor has committed a violation of Federal criminal law in connection with the award or performance of this contract or any subcontract thereunder";[3] and

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[2] FAR Case 2006-007, Contractor Code of Business Ethics and Conduct, 72 Fed. Reg. 65873 (Nov. 23, 2007) (the "Code of Ethics Rule").

[3] 72 Fed. Reg. at 64023 (citing 52.203-XX(b)(3)).

(2) the requirement that contractors make "[f]ull cooperation with any Government agencies responsible for audit, investigation, or corrective actions."[4]

Mandatory Disclosure to the OIG

The Proposed Rule requires a contractor to notify the Office of Inspector General (OIG) whenever it has "reasonable grounds to believe" a criminal violation has occurred in the performance or award of the contract. The penalties for a failure to make such a disclosure are severe: suspension and possible debarment. Specifically, the Proposed Rule would amend the suspension and debarment provisions to add two new types of contractor misconduct to the lists of causes for suspension or debarment under FAR 9.407-2 and 9.406-2, so long as the existence of the misconduct is based upon "a preponderance of the evidence":

(1) a "knowing failure" to "timely" disclose an "overpayment" on a government contract; and

(2) a "knowing failure" to "timely" disclose a "violation of Federal criminal law in connection with the award or performance of any Government contract or subcontract."

The Proposed Rule fails to include definitions of "reasonable grounds to believe," "knowing," or "timely," which raises multiple questions:

(1) What is the standard to be used for determining what might be "reasonable grounds" for a contractor's belief that a violation has occurred? For example, is the contractor to read this as the functional opposite of the standard of "reasonable doubt" as used in criminal prosecutions? Thus, as long as the contractor does not have a reasonable doubt whether a crime has been committed, must it disclose a suspected crime? Or is "reasonable grounds to believe" merely a disclosure-triggering epiphany whose occurrence is intended to remain subjectively viewed, and thus to expose the contractor to the strong possibility that government agencies will second-guess the contractor on whether reasonable grounds for notification or reporting duties had arisen?

(2) When does a necessary disclosure become late rather than "timely"? Is the contractor entitled to consult first with its legal counsel, its cost accounting expert and others, and to conduct a thorough self-investigation of the situation before it concludes that there has been an "overpayment" or a violation of Federal criminal law? And if the contractor does not have such professionals on its corporate staff or an outside firm with a good understanding of the company, how much time would be afforded the contractor to seek such professional assistance?

[4] Id. (citing 52.203-XX(c)(2)(ii)(G)).

(3) When is a failure to disclose "knowing," and who makes that determination? What if there are reasonable disagreements over whether there has been a violation?

There is, similarly, no definition of "overpayment." Federal contracts have many pricing methods and systems for interim or provisional payments. This raises further questions:

(1) Does an "overpayment" occur when a provisional payment such as a cost-reimbursement voucher is paid, even though the final amount for that voucher as determined at the end of the contract might be higher or lower than what the contractor had claimed for that voucher?

(2) Has an "overpayment" occurred when payment dollars pertaining to one line item appear to be excessive, but another line item was shortchanged by the government disbursing office in the exact same amount?

(3) Does the Proposed Rule's requirement to report "overpayments" to the OIG mean that existing processes for informal disclosures/discussions of potential accounting and other regulatory interpretation errors with the contracting officer are to be abandoned in favor of formal reporting to the OIG?

These questions are not answered by the plain language of the Proposed Rule and are subject to a broad range of interpretations.

We propose that the concept of "timely" reporting or notification of suspected criminal violations be modified to make it clear that any disclosure duty (whether mandatory, or preferably, voluntary) should allow for a reasonable period of self-inquiry, including seeking the unfettered assistance of legal counsel, aided as necessary by competent accountants, engineers or other professionals, giving the company enough time to make inquiry of its own employees, subcontractors, vendors, and others with potentially pertinent information.

More critically, irrespective of the specific words and phrases used in this Proposed Rule, the entire notion of mandatory disclosure runs counter to many established government processes. For example, unlike most of the compliance program elements required by the Proposed Rule, mandatory self-disclosure is not an element of an effective compliance program under the Sentencing Guidelines. Rather, voluntary self-disclosure is one factor in the mitigation of a company's culpability under the Sentencing Guidelines.

Mandatory self-disclosure is also at odds with the Department of Justice's own corporate-charging guidelines for Federal prosecutors. The "McNulty Memorandum," issued December 12, 2006 by then-Deputy U.S. Attorney General Paul McNulty, specifically states that

"prosecutors must consider" in their charging decision "the corporation's timely and voluntary disclosure of wrongdoing and its willingness to cooperate in the investigation of its agents."[5]

Nor does the Defense Federal Acquisition Regulation Supplement (DFARS) require reporting suspected violations directly to the OIG. Rather, the DFARS states that a "contractor's system of management controls should provide for ... [t]imely reporting to appropriate Government officials of any suspected or possible violation of law in connection with Government contracts."[6] Thus, where appropriate, contractors may make a voluntary disclosure to the contracting officer, the program manager, the contract administrator or some combination thereof. The OIG may be notified, certainly, but need not be notified unless appropriate.

More broadly, requiring disclosures to the agency OIG would defeat the concept of internal audits and correction of possible irregularities. It frequently happens that contractors' internal or external auditors, accounting personnel, compliance officers and others discover mistakes or misunderstandings that cause improper or inaccurate billings to government agencies. These typically honest mistakes often result in "overpayments" to the contractor. Under current practice, the contractor's personnel will notify the contracting officer or some other government official of the mistake and repay the "overpayment." This informal and productive process is threatened by the Proposed Rule.

Once a mandatory report is made to the OIG, both the contracting officer and the contractor or subcontractor may lose control of the investigation and resolution of contracting issues. We submit that it would not be good policy to require immediate reporting to an OIG office at the outset of the contractor's developing the threshold "reasonable grounds to believe" – a phrase that, as noted above, is undefined and subject to varying interpretations and misinterpretations. "Reasonable grounds to believe" could be viewed as a lower standard even than "probable cause." It could be based upon completely unevaluated or uninvestigated allegations, rumors and suspicions. It is likely to cause substantial over-reporting by companies trying to make sure they do not fall on the wrong side of the "reasonable grounds to believe" and "timely" reporting lines, as interpreted by government agents.

The existing voluntary disclosure protocols, in contrast, allow for internal investigation by the reporting parties before a disclosure is made. Many federal agencies currently have provisions encouraging voluntary self-disclosure. For example, the HHS-OIG's Provider Self-Disclosure Protocol[7] was implemented in October 1998 to assist health care providers in investigating and reporting potential violations of Federal health care laws. The program presents providers with an opportunity to police themselves, correct underlying problems and work cooperatively with the government to resolve any matters of concern. This and other voluntary disclosure programs provide the incentive of fair and appropriately lenient treatment as encouragement for contractors to self-audit, investigate and report actual wrongdoing and administrative violations. In fact, the HHS-OIG specifically discourages health care entities

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[5] Memorandum from Paul J. McNulty, Deputy Attorney General, to Heads of Department Components, United States Attorneys at 4 (Dec. 12, 2006) [hereinafter McNulty Memorandum] (emphasis added).
[6] DFARS § 203.7001(a)(6) (emphasis added).
[7] 63 Fed. Reg. 58399 (Oct. 30, 1998), *available at* http://oig.hhs.gov/authorities/docs/selfdisclosure.pdf.

from using the Self-Disclosure Protocol for mere "overpayments" unless they result from violations of criminal or administrative law.[8] The Proposed Rule, with its mandatory reporting requirement, may eliminate both existing informal processes for resolving possible overpayments, as well as the more formal voluntary self-policing and disclosure programs.

One of the larger concerns about mandatory disclosure – with looming penalties of suspension and debarment – is that it will inhibit "good" companies from entering or remaining in the Federal market, while likely leading to only marginally more useful reporting, if any. With the existing voluntary disclosure systems that reward self-reporting, "good" companies will naturally disclose concerns to authorities, whereas "bad" companies will not. With mandatory disclosure, however, "good" companies will still disclose – because it is required – yet "bad" companies still will not disclose. Plus, the threat of suspension and debarment and the potentially massive costs of responding to an OIG investigation, rather than the current system of more informally working out most issues with the contracting officer, will keep some "good" companies from bidding on government contracts in the first place.

Those "good," or ethical, companies that enter or remain in the Federal market are likely to substantially over-report potential problems. The vagueness and uncertainty surrounding the mandatory reporting standards in the Proposed Rule will lead to decisions to report anything that could even remotely be considered a criminal violation or overpayment. Because of the complexity of many government contracting regulations, ethical contractors will want to avoid even approaching the line. These companies will almost certainly follow the maxim, "When in doubt, report." This, in turn, may result in inundation of OIGs with cases based on nonexistent or minor violations and drain limited resources from more substantive matters.

Voluntary disclosures, internal audits and inquiries should be encouraged for a broader range of events, not just potential fraud or crime. They should be encouraged, either in the current formal voluntary disclosure format, or as much more informal requests to contracting officers, auditors and program officials for guidance on the whole range of issues that might be irregular, or unorthodox, or mistaken for whatever reasons. Such inquiries by contractors would permit the prompt correction of noncompliant practices, and restitution if necessary, but not prosecution, or investigations by OIGs which typically take the form of enforcement actions. Contractors should be rewarded for bringing questionable practices to the attention of the authorities rather than being bullied by mandatory disclosures and accused of not following ethics rules.

Thus, in order to maintain consistency with other federal agencies and the Sentencing Guidelines' widely known compliance program elements, and to keep ethical companies from

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[8] "The Provider Self-Disclosure Protocol is intended to facilitate the resolution of only matters that, in the provider's reasonable assessment, are potentially violative of Federal criminal, civil or administrative laws. Matters exclusively involving overpayments or errors that do not suggest that violations of law have occurred should be brought directly to the attention of the entity (e.g., a contractor such as a carrier or an intermediary) that processes claims and issues payment on behalf of the Government agency responsible for the particular Federal health care program (e.g., HCFA for matters involving Medicare)." 63 Fed. Reg. at 58400.

being scared away by business-killing penalties and costs, the Councils should consider a broad, voluntary disclosure program instead.

Mandatory "Full Cooperation"

The Proposed Rule also requires "[f]ull cooperation with any Government agencies responsible for audit, investigation, or corrective actions." This statement lacks further explanation or clarification, however, and raises additional questions:

(1) What is "full cooperation," as opposed to mere "cooperation"?

(2) Does "full cooperation" require waiver of the attorney-client privilege and work product protections?

(3) Does "full cooperation" restrict the right of corporations to provide legal counsel for their employees in an effort to increase communication and the flow of information?

If "full cooperation" does indeed mean a complete waiver of the attorney-client privilege and work product protections, this Proposed Rule would run counter to Supreme Court case law, as well as DOJ's guidance to its own prosecutors.

As the Supreme Court has explained, the purpose of the attorney-client privilege is to "encourage full and frank communication between attorneys and their clients and thereby promote broader public interests in the observance of law and administration of justice."[9] Restraints on the privilege "limit the valuable efforts of corporate counsel to ensure their client's compliance with the law."[10] In the context of potential legal or regulatory violations, the privilege is a critical piece of a complete and thorough internal investigation, fostering open communication and the disclosure of pertinent facts.

More recently, Federal judges are reemphasizing the necessity for the privilege and the full breadth of its protections. For example, in a highly publicized decision involving the accounting firm KPMG, the Southern District of New York found that Federal prosecutors had violated the constitutional rights of former KPMG employees by pressuring the company not to pay their legal bills.[11] The "full cooperation" requirement of the Proposed Rule could easily be read to discourage or even prohibit contractors from providing attorneys to employees, chilling the entire investigation process and hindering any fact-finding mission.

Also, the McNulty Memorandum, referenced above, notes that a company's "willingness to cooperate" should be a factor in a prosecutor's charging decision. The McNulty Memorandum further states that "[t]he attorney-client and work product protections serve an extremely important function in the U.S. legal system" and that "[w]aiver of attorney-client and work

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[9] *Upjohn Co. v. United States*, 449 U.S. 383, 389 (1981).
[10] *Id.* at 392.
[11] *United States v. Stein*, 435 F. Supp. 2d 330, 364-67 (S.D.N.Y. 2006).

product protections is not a prerequisite to a finding that a company has cooperated in the government's investigation."[12] The absence of a clear acknowledgement in the FAR that the privilege is sacrosanct, and waiver is not a requirement of "cooperation" by a contractor, will also have the effect of deterring a contractor's employees from reporting any potential or suspected wrongdoing in the first place, or from hiring competent counsel to conduct internal investigations. Thus, the requirement of such "full cooperation" may lead to fewer reports in the end.

Legal counsel advising contractors need to be confident that their clients will provide them with all pertinent information on matters under internal review or investigation. If anything impedes the candid exchange of views between the client and the attorney, the quality and accuracy of the resulting legal advice will be dangerously degraded. Maintaining the attorney-client privilege is vital to full and productive analysis, to preventing violations, and to assisting the client in remediation measures and in considering voluntary disclosures.

For example, in the experience of many attorneys practicing in the confluence of government contracts and Federal investigations, it is not uncommon for counsel to recommend that companies cooperate in the sense that: (a) all appropriate records are made available to auditors within the scope of pertinent audit clauses or other requirements and nothing of potential significance is destroyed; (b) subpoenas are forthrightly obeyed; (c) the corporate clients are advised not to make any attempt to direct employees not to speak with investigators, or to dictate the content of their discussions with investigators; (d) conversely, employees likely to be approached by investigators are reminded that they also have the right not to speak to investigators, and that the choice is theirs, not that of their employer; (e) employees are told that if they wish to speak with investigators, they may request that counsel be made available to them and accompany them in the interview if they wish; (f) companies and employees are advised that when employees confer with corporate counsel on legal matters involving the company, those discussions are privileged, and yet it is the client (the company) that owns the privilege and can choose to relinquish it voluntarily such as by a report or a voluntary disclosure; (g) that if the employee wishes, the company will assist in arranging a suitable location for an interview; and so on. Counsel also will typically advise companies and their employees that if they do agree to be interviewed by enforcement agents, they must tell the truth. Many government investigators are routinely able to conduct useful, courteous inquiries under such circumstances, and these measures should qualify as cooperation without necessitating waiver of long-standing privileges and protections attendant to the provision of legal advice and assistance to a contractor client.

Given the above, we surmise that the Councils do not intend to require waiver of the attorney-client privilege and work product protections through the use of the phrase "full cooperation." However, absent any clarifying language, the requirement is too easily broadened and can be used to justify unreasonable demands for waiver of privilege. Accordingly, the "full cooperation" language in 52.203-XX(c)(2)(ii)(G) should be modified to state that the contractor is expected to cooperate procedurally with audits, investigations and corrective actions, and it should also be made explicitly clear that nothing in this context should be taken to imply that the

[12] McNulty Memorandum at 8.

protections of attorney-client privilege and the attorney work product doctrine must be surrendered. As with the mandatory disclosure provision, the government should continue its history of encouraging voluntary cooperation and taking such cooperation into account in suspension and debarment decisions. Mandatory and "full" cooperation, however, would be counterproductive and contrary to the government's stated goals.

Conclusion

The government's goals of conformity with existing compliance and ethics guidelines and, ultimately, the attendant reduction of fraud in the Federal marketplace are laudable and necessary objectives. However, in the process of achieving those objectives, surely the Councils do not intend to break with established legal protections. Thus, the Councils should carefully reexamine the Proposed Rule's requirements of mandatory disclosure to the OIG and mandatory "full cooperation" in light of Federal case law, the Sentencing Guidelines, the DOJ's guidance to prosecutors, and the daily workings of the government contracts marketplace.

Holland & Knight appreciates being given this opportunity to submit our comments. If you have questions or need additional information, please contact either Christopher Myers at chris.myers@hklaw.com or Alan Dickson at alan.dickson@hklaw.com, or telephone us toll-free at 1-888-688-8500.

Respectfully Submitted,

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