

Government Contracts Team

To: Our Clients and Friends

June 22, 2011

Increased Scrutiny of Contractors' Code of Ethics, Compliance Program, and Internal Controls is Likely

A one-sentence addition to the Federal Acquisition Regulation ("FAR") that takes effect on June 30 should cause Federal contractors that have not reviewed their codes of conduct and business ethics recently to do so. Similarly, if they are required by their contracts to have a business ethics awareness and compliance program and an associated internal control system, they should also check that they will pass muster.

Over the past few years, the Federal government has added increasingly stringent requirements that contractors have codes of conduct and associated compliance programs and internal control systems. Most recently, in late 2008, a contract clause -- FAR 52.203-13, "Contractor Code of Business Ethics and Conduct" -- was promulgated that appears in all Federal prime contracts that exceed \$5 million and have a period of performance of 120 days or more and is required to be included in subcontracts of that dollar amount and period of performance. That clause requires contractors to have a code of conduct and business ethics and make it available to each employee working on the contract. As a practical matter, for most contractors, this resulted in them having to have such a code that covers everyone. Contractors also are required to make disclosures to the government when they have "credible evidence" of a violation of certain criminal laws or the civil False Claims Act. Unless the contractor is a small businesses or its contract is to provide a commercial item, the clause also requires the company to have a business ethics awareness and compliance program and an internal control system.^{1/}

Although contractors have had a contract requirement to have such a code of conduct and, as appropriate, compliance programs and internal control systems, no-one in the government was assigned the responsibility to verify that the contractor had actually done this. The Defense Contract Audit Agency ("DCAA") took it upon itself to include reviews of codes of conduct, compliance

^{1/} A more complete description of this contract clause is in our bulletin at:
<http://www.bryancave.com/bulletins/list.aspx?Services=678&year=2008>

programs, and internal controls as part of its Control Environmental and Overall Accounting System Control Audits, but these audits are not performed for all contractors and DCAA has a tremendous audit backlog.

The Government Accountability Office noted some of the gaps in oversight and concluded in 2009 that improvements could be made in the Department of Defense's oversight of contractor ethics programs. It recommended that the Department determine what guidance was needed to clarify the responsibilities of "contracting officials during contract administration for verifying the implementation of contractor ethics programs as required under the FAR ethics rules."^{2/}

The result of the GAO recommendation is a new rule, applicable to all executive branch agencies covered by the FAR, not just the Department of Defense. The FAR has been amended to add to the functions that are normally delegated to a government contract administration office (such as an Administrative Contracting Officer) having to "[e]nsure that the contractor has implemented the requirements of 52.203-13, Contractor Code of Business Ethics and Conduct." 54 Fed. Reg. 31416 (May 31, 2011)(to be codified at FAR 42.302(a)(71)). Thus, although some small contractors may still escape scrutiny, a far larger group of contractors can now expect to find the government taking steps to ensure that they have complied with the requirements of the contract clause.

Exactly what contracting officers will do to ensure compliance remains to be seen. Cryptically, the regulation writers noted in prefatory comments that "[c]ontracting officers may ask to see a contractor's code of ethics or a contractor's ethics program, but the contracting officer is not required to ask for a copy of any documents." *Id.*, at 31394. It seems likely, however, that contractors will soon start receiving requests for copies of their codes of conduct, compliance programs, and/or internal control systems in order that government contracting personnel can determine whether contractors are implementing the clause. It would be prudent for contractors to review those now to ensure that they are sufficient.

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^{2/} Government Accountability Office, GAO-09-591, Defense Contracting Integrity - Opportunities Exist to Improve DoD's Oversight of Contractor Ethics Programs 31 (2009).

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