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YOU THOUGHT EXECUTIVE COMPENSATION IN PRIVATE COMPANIES WAS ACTUALLY PRIVATE?!? NOT SO FOR MANY FEDERAL CONTRACTORS

By Cara Crotty
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In the Obama Administration's continuing quest for transparency, the federal government issued an **Interim Rule** on July 8, 2010, that requires many federal contractors and subcontractors *to report and make publicly available the total compensation of their top five executives*. The Interim Rule implements the Federal Funding Accountability and Transparency Act of 2006, as amended by the Government Funding Transparency Act of 2008, which requires covered contractors to report information on first-tier subcontracts and the total compensation of the top five executives for both direct contractors and first-tier subcontractors.

The Interim Rule notes that the "reporting requirements of the [Act] are sweeping in their breadth, and are intended to empower the American taxpayer with information that may be used to demand greater fiscal discipline from both executive and legislative branches of Government." Although the sponsors of the legislation stated that "Government officials will be less likely to earmark funds for special projects if they know the public could identify how much money was awarded to which organizations and for which purposes," the Interim Rule does not explain how reporting of executive compensation furthers this objective in any way.

What is an Interim Rule, and when will this be a Final Rule?

Typically, the federal government issues a Notice of Proposed Rulemaking before regulations become effective. This provides the public with an opportunity to comment on the proposed regulations before they become law. In certain situations, however, the government may issue an Interim Rule -- which is effective immediately -- while it solicits comments and prepares the Final Rule. In this case, the government determined "that urgent and compelling reasons exist to promulgate this interim rule without prior opportunity for public comment." The government is **accepting comments** on the Interim Rule through September 7, 2010, after which it may make changes and issue a Final Rule.

To what companies does the Interim Rule apply?

Subject to the implementation phase-in schedule **described below**, contractors are required to report all first-tier subcontracts worth \$25,000 if they have a contract that (1) was awarded based on a solicitation issued on or after July 8, 2010; (2) includes

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the “Reporting Executive Compensation and First-Tier Subcontract Awards” clause (FAR 52.204-10); and (3) is worth \$25,000 or more. Government contracting officers have been instructed to modify existing indefinite contracts to include this requirement where appropriate.

What are the reporting requirements of the Interim Rule?

By the end of the month following the month of award of a contract, and annually thereafter, **prime contractors** must report the names and total compensation of each of the five most highly compensated executives for the contractor’s preceding completed fiscal year. In addition, unless otherwise directed by the government contracting official, contractors must report (by the end of the month following the month of award of a first-tier subcontract and annually thereafter) the names and total compensation of the five most highly compensated executives for the **first-tier subcontractors’** preceding completed fiscal year. (Subcontractors are required to provide this information to the prime contractor for reporting purposes).

Covered contractors must also report a variety of information regarding all first-tier subcontracts awarded. This information includes the following: Dun & Bradstreet DUNS number for the subcontractor and its parent company; name of subcontractor; amount of subcontract award; date of subcontract award; description of products or services being provided, including overall purpose and expected outcome; subcontractor’s address, including congressional district; and subcontractor’s primary performance location, including congressional district.

How do you determine “total compensation” of top executives?

“Total compensation” means the cash and non-cash dollar value earned during the preceding fiscal year, and includes salary; bonus; awards of stock, stock options and stock appreciation rights; earnings for services under non-equity incentive plans; change in pension value; above-market earnings on deferred compensation that is not tax-qualified; and other compensation if the aggregate value exceeds \$10,000.

What is the effective date of the Interim Rule?

The Interim Rule was effective immediately upon issuance on July 8, 2010, but the government is phasing in the requirements relating to reporting of subcontracts:

- From July 8, 2010 through September 30, 2010, any newly awarded subcontract must be reported if the prime contract amount was \$20 million or more.
- From October 1, 2010 through February 28, 2011, any newly awarded subcontract must be reported if the prime contract amount was \$550,000 or more.
- Starting March 1, 2011, any newly awarded subcontract must be reported if the prime contract amount was \$25,000 or more.

How do contractors report the required information?

Contractors are required to provide the subcontract award information to the Federal Funding Accountability and Transparency Act Sub-award Reporting System at <http://www.fsrs.gov>. Contractors must report the names and total compensation of the contractors’ top five most highly compensated executives to <http://www.ccr.gov> and must report the same information for its first-tier subcontractors at <http://www.fsrs.gov>. The government then makes

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this information publicly available at <http://www.usaspending.gov>.

Are there any exceptions or exemptions to these reporting requirements?

Yes:

- They do not apply to contractors below the first-tier level.
- Contractors and subcontractors with less than \$300,000 in gross income in the previous tax year are exempt.
- The reporting requirement is not required to be included in classified solicitations and contracts or in contracts with individuals.
- Contractors and first-tier subcontractors are not required to comply with the compensation reporting requirement unless
 - (1) in the contractor or subcontractor's preceding fiscal year, the contractor or subcontractor received
 - (a) 80 percent or more of its annual gross revenue in Federal contracts (including all subcontracts), loans, grants, and cooperative agreements; and
 - (b) \$25 million or more in annual gross revenue in Federal contracts (including all subcontracts), loans, grants, and cooperative agreements; and
 - (2) the public does not have access to the information about the compensation of the senior executives through periodic filings with the Securities and Exchange Commission or the Internal Revenue Service.

Larger private companies are not likely to satisfy this exception, as compensation information is not generally reported to the SEC. Smaller private companies would be exempt from the compensation reporting requirements if they do not satisfy the revenue thresholds.

Deciding that it was in the "best interests of the Federal Government" and without further explanation, the government specifically declined to exempt contracts below the simplified acquisition threshold of \$100,000 (except for contracts less than \$25,000), commercial items contracts, and commercially available off-the-shelf items contracts.

How can I submit comments on the Interim Rule?

Comments must be submitted by September 7, 2010 to www.regulations.gov, referencing "FAC 2005-44, FAR case 2008-039." All comments submitted will be posted publicly.

If you have any questions regarding this Interim Rule, please contact any member of Constangy's **Strategic Affirmative Action Practice Group**, or the Constangy attorney of your choice.

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