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FEDERAL GOVERNMENT CONTRACTS AND COMMERCIAL CONTRACTS: A BRIEF COMPARISON

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I. GOVERNMENT CONSTRUCTION CONTRACTING PROCESS: AN OVERVIEW

A. Introduction

Unlike commercial construction contracts, a government construction contract combines the expected statement of the scope of the work to be executed with terms and conditions that reflect the government's policies regarding contractual risk allocation, project management, and various social and economic objectives. While a description of the scope of the work, risk allocation terms, and project management requirements are common on all private and public construction projects, contractors need to recognize the significance of the various social and economic policies and their effect on all aspects of the project from contract award through execution of the work.

In addition to recognizing the multiple objectives related to the award and execution of a government construction project, potential government contractors need to appreciate that the federal government's departments and agencies awarding and administering contracts can have very different styles of management and organization. Understanding the federal government as a client and customer requires an investment of time to gain an appreciation of the differences between the various departments and even among the various offices within the same department that award and administer construction projects. Although extremely large in size, the federal government is not monolithic when it contracts for construction services.

Understanding the government's contracting process also requires an appreciation of the terminology or jargon commonly used by government contractors and agency

personnel. Every business has its jargon, and federal construction contracting is no different. Finally, contractors must appreciate that the Internet is a major tool in government contracting from the initial steps in seeking to compete for an award to the final evaluation of the contractor's performance. Understanding and managing these tools is an essential step in becoming a successful government contractor.

B. Organization of This Book

With limited exceptions, the organization of this book follows the sequential steps of the government construction contracting process. **Chapter 1** provides an overview of the organization of several of the major federal agencies that award and administer construction contracts, the jargon or terminology used in the process, and a survey of many of the Internet sites involved in the contracting process. In addition, this chapter provides a brief comparison of commercial and government contract law, the sources of federal law affecting contractors and the performance of the contract work, and, last but not least, the federal government's comprehensive legal and regulatory scheme to promote the highest standards of business ethics and conduct.

Government contracts, whether for supply, service, or construction, illustrate the use of the procurement process to fill a perceived need. The initial steps in the contracting process are the authorization of funds, financing, and the delegation of authority to procure the work and administer the contract. (See **Chapter 2.**)

Once funding is in place, the procuring agency selects the project delivery method and contract type,[1] undertakes to solicit bids or proposals, and thereafter awards a contract for the work. This involves basic principles of contract law (offer, acceptance, authority to bind the government) and the selection of the actual procurement method (sealed bids or negotiated proposals) as well as the appropriate contract type and project delivery vehicle. **Chapter 3** discusses the contract formation process, relief for bid or proposal mistakes, and the resolution of bid protests. **Chapter 4** reviews various project delivery methods and contract types that the government may utilize in the procurement process.

For the past several decades, government contracts have been used to achieve social policies. These policies affect contractor selection (small business firms, service-disabled veteran-owned contractors, etc.) as well as performance of the work (labor laws, environmental laws, safety, etc.) and a preference for domestic (U.S.) products. These topics are addressed in **Chapter 5.**

Issues arising during performance of the work may include issues of contract interpretation, differing site conditions, delays, changes, inspection and acceptance, payment, bonding, and contract termination. These contract administration issues reflect the large majority of potential problems that a contractor may face during or after performance, and they are covered in **Chapters 6 to 13.**

Project documentation is important throughout contract performance and can affect the parties' rights and obligations under the various clauses. Consequently,

[1]*See* **Chapter 4** for an overview of the organization and contents of a typical government construction contract.

notice and documentation practices are addressed in **Chapter 14**. Regarding notice, government contractors need to consider that subcontracts and purchase orders are actually commercial (private) contracts being performed to satisfy the requirements of the prime contract with the government, and they should remember to flow down many of the federal government's terms and conditions into their subcontracts *and* purchase orders. These topics, which relate to the management of subcontracts, are beyond the scope of this book.[2]

Given the complexity of government projects and contracts, it is highly unlikely that all claims and disputes can be avoided. Even if a contractor is claim adverse, it needs to have an appreciation of the disputes process in the event a claim develops or appears likely. This topic is addressed in **Chapter 15**.

While not technically government contracts, projects funded by federal grants may have attributes similar to federal government contracts. Consequently, the role of the federal government and the effect of federal procurement principles on federally funded grant contracts are addressed in **Chapter 16**.

Finally, with the passage of the American Recovery and Reinvestment Act of 2009[3] (commonly called ARRA or the Recovery Act), Congress imposed several new requirements on contractors receiving Recovery Act funds in both a federal government contract and a grant-funded state/local construction project. Since these topics apply to a subset of federally funded projects, these requirements are addressed collectively in **Chapter 17.**

In an effort to provide a more practical perspective on the various topics addressed in this book, numerous **Checklists** are set forth throughout the book. These checklists are provided as a means to assist the user of this book in applying the concepts and principles in a practical manner. In addition, copies of these checklists are also included on the support Web site at www.wiley.com/go/federalconstructionlaw in a Word format to permit the user to copy and adapt them as needed for a particular contractor's project and organization.

C. Federal Agency Organization, Terminology, and Resources

The federal government procures construction services through multiple agencies. Screening the Federal Business Opportunities (FedBizOpps) Web site (*www.fbo.gov*) for notice of solicitations and awards posted in a 30-day period[4] reflects more than 3700 construction actions (solicitations and awards) involving 24 separate agencies of the federal government ranging from the Department of the Army—Corps of

[2]*See generally Common Sense Construction Law* (fourth edition) (ed. Thomas J. Kelleher, Jr. and G. Scott Walters [John Wiley & Sons 2009]) for a review of these issues and others (subcontract bidding, insurance, bankruptcy, purchase of goods under the UCC, etc.).

[3]Pub. L. 111-5.

[4]Search performed under the North American Industry Classification (NAICS) code "y"—Construction of Structures and Facilities (accessed August 21, 2009). Although it seems complex, this Web site is relatively easy to use.

Engineers (COE) with several hundred postings to the Architect of the Capitol and International Boundary and Water Commission with only a few postings each.

Regardless of the size of the project, nearly all contractors seek to gain an understanding of the client (owner) as part of the decision process on whether to compete for that contract. In the private sector, some call this activity "qualifying the owner." In reality, it is an effort by the contractor to understand the potential client and the anticipated project, and to conduct a self-evaluation of its capabilities for successful performance. In that context, the following questions or topics should be considered:

PROJECT QUALIFICATION CHECKLIST

- Has the contractor or its key project management personnel worked for that agency before? If so, what were the results and why?
- If the agency has multiple offices, what experience does the contractor have with the office that will administer the contract?
- Do the agency personnel that evaluate the proposal or bid remain responsible for the administration of the contract during performance?
- Has the agency or particular office previously built a project of similar type and complexity? If so, were there any problems? Potential subcontractors can be a useful source of information.
- Does the agency routinely change its project management staff as construction nears the punch list stage?
- Is the contracting officer located at the project site or in a relatively distant agency office? If so, does any government employee at the project site have contracting officer authority?
- Is the agency awarding and administering the contract also the eventual "owner" of the project, e.g., the Department of Veterans Affairs (VA) constructing a VA medical center, or is that agency essentially functioning as a construction manager? An example of the latter would be the Corps of Engineers constructing a project for use by the U.S. Air Force.
- What information is available regarding the experience and so on of the people the agency will place on the project site during the actual construction? (Again, potential subcontractors can be a useful source of information.)
- Does the agency routinely require project management, scheduling, or design coordination programs that require a significant new investment of contractor resources?

As a potential contractor evaluates these and similar questions, the contractor should recognize that federal agencies awarding and administering construction contracts are not organized uniformly. These structural differences may reflect differences in the agency's mission and, to some extent, historical practices. The next list illustrates some of the variety in agency organizational structure.

- **U.S. Army Corps of Engineers**. In 2009 the Corps (USACE) is geographically organized with one headquarters in Washington, D.C., and nine regional divisions including one in the Gulf Region of Southwest Asia overseeing 45 subordinate district offices in the United States and overseas and six specialized centers and laboratory facilities throughout the world.[5] In the United States, the Corps' District Offices are responsible for either civil works and/or military missions. USACE Civil Works District boundaries are set on the basis of watersheds. Military Districts are generally set within designated state boundaries. Given this organization and the fact that the Corps administers contracts for other agencies, the contracting officer may not be located near the project site. For example, it is not unusual to see a contract involving the location and disposal of munitions on former military training facilities awarded and administered by a contracting officer in Huntsville's Center of Expertise (CX) but performed in the Hawaiian Islands. Contractors need to consider whether there are potential issues created by the geographic remoteness of a project from the contracting officer.
- **Naval Facilities Engineering Command.** While not as complex as the USACE organization, NAVFAC has 10 Facilities Engineering Commands that report to two NAVFAC commands: NAVFAC Atlantic in Norfolk, Virginia, and NAVFAC Pacific in Pearl Harbor, Hawaii.[6] Similar to the COE, the Navy awards and administers projects for other Department of Defense branches, such as the U.S. Air Force, as well as for the Navy and Marine Corps. Consequently, there may be potential issues related to the distance between the project and that agency's contracting officer.
- **Department of Veterans Affairs.** The VA reflects a more centralized approach as it manages construction for the VA's health facilities (Veterans Health Administration) and approximately 80 national cemeteries in the National Cemetery Administration (NCA). The contracting officer for major VA projects is often located in that agency's Office of Construction and Facilities Management in the Washington, D.C., area.[7] Resident Engineers (RE) and Senior Resident Engineers (SRE) usually located at the project site are the primary point of contact with the contractor once a contract is awarded. These individuals may have limited contracting officer authority, as discussed in **Chapter 2.** Smaller construction projects (often minor renovations) may be awarded and administered by the staff at an individual VA facility.

With two dozen or more different agencies of the federal government awarding and administering contracts, contractors should anticipate that there will be differences in the administration of contracts among the agencies and even within the

[5]*www.usace.army.mil/about/Pages/Locations.aspx* (accessed November 3, 2009).
[6]*https://portal.navfac.navy.mil/portal/page/portal/navfac/* (accessed November 3, 2009).
[7]*www.cfm.va.gov/about/history.asp* (accessed November 3, 2009).

agencies. Just as a contractor typically performs a site investigation as part of its estimating process, a contractor should obtain as much information as possible regarding the agency's organization as it affects contract administration and the key agency personnel who will administer the contract on a day-to-day basis. Construction is very much a people business. Neither the federal government nor the various agencies are truly monolithic.

In addition to obtaining an appreciation of a particular agency's organization as it affects construction contract awards and project administration, a contractor should consider that government construction contracts often reference standards, design guides, and other technical publications used by various agencies (e.g., the Corps of Engineers, NAVFAC, the General Services Administration's Public Buildings Service, the VA, etc.). These standards or publications can provide critical information on the agency's expectations. For example, the expected level of detailed design development on a design-build project can vary substantially from agency to agency and from project to project. Acceptable practice on a private, commercial project may not be acceptable to a federal agency. If the agency's solicitation references a design guide or standard, a contractor's review of that document is an essential step in estimating the time and cost of performance.

Many agencies maintain virtual libraries on the Internet on which a contractor can access technical publications. For example, the VA's Technical Information Library at *www.cfm.va.gov/til/* contains materials on master specifications, design guides, and manuals. **Appendix A** to this book contains a listing of government contract–related Internet Web sites, including the reference libraries of the Corps of Engineers, NAVFAC, General Services Administration's Public Building Service, and the VA. This Web site data is also included on the support Web site at www.wiley.com/go/federalconstructionlaw.

D. Terminology and Jargon

Every industry and business uses jargon and acronyms, such as ERA (earned run average) in baseball. Federal government construction contracting is replete with both. For example, FAR is the acronym for the Federal Acquisition Regulation. In addition to providing information in the text of this book on acronyms and jargon commonly associated with government construction contracting, **Appendix B** to this book is a glossary of terms and acronyms often referenced or used in the award and administration of government construction contracts. A copy of this glossary is also found on the support Web site at www.wiley.com/go/federalconstructionlaw.

E. Internet-Based Resources

This book is intended to provide a construction professional with a reasonably comprehensive, basic resource and overview of the topics and issues that a government construction contractor may be required to address and needs to appreciate. To provide a single point of reference for all procurement-related information (potential contracting opportunities) and to reduce costs associated with the management of the

procurement process, the government has created a number of Web sites that pertain to the construction contracting process, ranging from contractor registration, to access to technical manuals and standards. Attached to this book at **Appendix A** and included on the support Web site at www.wiley.com/go/federalconstructionlaw is a summary of the primary government contract–related Web sites along with a brief description of the purpose of each and the information that is available on each Web site.

II. RELATIONSHIP OF COMMERCIAL AND GOVERNMENT CONTRACT LAW

Since World War II, the federal government has consistently purchased or funded, directly or indirectly, a larger volume of construction services or work than any other single entity. While some agencies of the federal government, especially within the Department of Defense (DOD), have some capability to perform construction services with internal or agency resources, that capability is limited and often is used to support the military forces in their field operations rather than build substantial projects in the United States. Consequently, the government obtains nearly all of its needed construction work and services by contracting with private entities.

Basically, any reference to a *government construction contract* in this book means a contract directly with an agency of the federal government and does not include a contract awarded by a state or local public body or other entities using federal funds or financing.

The basic principles governing government construction contracts reflect the American common law of contracts, which evolved from the English common law. First, the parties to a contract must have the capacity to enter into that contract. Second, parties with capacity to contract generally may agree to whatever they wish, as long as their agreement does not run afoul of some legal authority or public policy. Thus, in private commercial contracts, an owner and a contractor may agree to a very risky undertaking in the context of a construction project, but they may not agree to do something illegal (e.g., gamble on the project's outcome). The former agreement reflects a policy of freedom of contract; the latter could violate a prohibition on gambling transactions. The law has long recognized that the government has the capacity to enter contracts.[8] Of greater importance is the issue of the contents of the contract and the parties' obligations under it.

A contract is traditionally defined as "a promise or set of promises, for the breach of which the law gives a remedy, or the performance of which the law in some way recognizes as a duty."[9] Thus, a contract is basically a set of promises made by one party to another party, and vice versa. In the United States, contract law reflects both the common law of contracts, as set forth in court decisions, and statutory law governing the terms of certain transactions.

[8]*United States v. Tingey,* 30 U.S. 115 (1831).
[9]Samuel Williston and Richard Lord, *Williston on Contracts* § 1:1 (Thomson/West 4th ed. 2007).

Similar to private contracts, government construction contracts contain or reflect both express and implied obligations or promises. Express contract obligations are those that are spelled out in the agreement or contract. Less obvious than the express duties under a contract, but just as important, are those obligations that are implied in every contract. Examples of these duties include the obligations of good faith and cooperation.

In the context of a construction project, one of the most important of these implied duties is the obligation that each contracting party cooperates regarding the other party's performance.[10] The fact that this obligation is implied rather than express is not reflective either of its importance or of the frequency with which it forms the basis for claims for compensation. Rather, the obligation to cooperate forms the very basis of the agreement between the parties.

The obligations to coordinate and cooperate are reciprocal and apply equally to all contracting parties. By way of illustration, an owner (public or private) owes a contractor an obligation to allow the contractor access to the site in order to perform its work; a prime contractor has a similar duty not to hinder or delay the work of its own subcontractors; and one prime contractor is obligated not to delay or disrupt the activities of other parallel prime contractors to the detriment of the government. Each example demonstrates that a contracting party owes an obligation of cooperation to the parties with which it has contracted. In addition, under certain circumstances, the duty to cooperate may extend to third parties with whom there is no direct contractual relationship.

In addition to the obligation of cooperation, the government, as the owner, and the contractor have other implied obligations, such as warranty responsibilities. The government's implied warranty of the adequacy of government-provided plans and specifications is of great importance to the contractor, and the breach of this warranty forms the basis of a large portion of contractor claims. The existence of an implied warranty in connection with government-furnished plans and specifications was recognized in *United States v. Spearin.*[11] The so-called *Spearin* doctrine has become well established in virtually every American jurisdiction that has considered the question of who must bear responsibility for the results of defective, inaccurate, or incomplete plans and specifications. In layman's language, the doctrine states that when an owner supplies the plans and specifications for the construction project, the contractor cannot be held liable for an unsatisfactory final result attributable solely to defects or inadequacies in the owner's plans and specifications. The key in this situation is the allocation of the risk of the inadequacies of the design to the contracting party that furnished the design or controlled the development of the design. Thus, in a design-build project, the design-build contractor, not the government, typically would bear the risk for a design error or deficiency.[12]

[10]*See* 13 Samuel Williston and Richard Lord, *Williston on Contracts* § 39:6 (Thomson/West 4th ed. 2000).
[11]248 U.S. 132 (1918).
[12]This risk allocation may be altered by the actions of the government. For example, in *M.A. Mortenson Co.,* ASBCA No. 39978, 93-3 BCA ¶ 26,189, the government furnished a conceptual structural design to the design-builder for estimating (bidding purposes). When it was determined that the conceptual structural design was inadequate, the government bore the risk of the cost of the additional steel and concrete to remedy the design problems, even though the contract was labeled as a "design-build" contract.

Similar to private contracts governed by the common law, the basic concept of breach of contract applies to government contracts. In private contractual relationships, a *breach of contract* results when one party fails in some respect to do what that party has agreed to do, without excuse or justification.[13] For example, a contractor's failure to use the specified trim paint color, or its failure to complete the work on time, constitutes a breach of contract. Public or private owners may likewise breach their contract obligations. Many contracts expressly provide, for example, that the owner will make periodic payments to the contractor as portions of the work are completed. If the owner unjustifiably fails to make these payments, this failure constitutes a breach of contract. Similarly, an owner may be held in breach for failing to meet other nonfinancial contractual obligations, such as the duty to timely review and return shop drawings and submittals. In short, any failure to live up to the promises that comprise the contract is a breach.

Whenever there is a breach of contract, the injured party has a legal right to seek and recover damages. In addition, if there has been a serious and *material* breach—that is, a breach that, in essence, destroys the basis of the parties' agreement—the injured party is justified in treating the contract as ended.[14]

Breach of contract actions are relatively rare in government contracting due to the fact that these contracts include remedy-granting clauses, such as the Changes clause,[15] the Default clause,[16] and the Suspension of Work clause.[17] These remedy-granting clauses, when combined with a very comprehensive disputes procedure that generally requires a contractor's continued performance pending claim resolution (see **Chapter 15**), effectively limit the application of traditional breach of contact theories and damages claims in government contracts. However, the concept of contractual terms limiting the scope of breach of contact liabilities and damages is not unique to government contracts, as illustrated by the provisions of the Uniform Commercial Code (UCC)[18] that provide for limitations on liabilities[19] and remedies.[20] All of these basic principles and concepts of contracting are reflected in both government contracting and private commercial contracts.

III. SOURCES OF FEDERAL LAWS AFFECTING GOVERNMENT CONSTRUCTION CONTRACTS

A. Contracts Awarded by Federal Agencies

The procurement and administration of government construction contracts, as well as the resolution of disputes on these projects, are governed by multiple statutes

[13]*See Restatement (Second) of Contracts* §§ 235, 236.
[14]*See generally* 17A Am. Jur. 2d *Contracts* § 528 (2007).
[15]FAR § 52.243-4.
[16]FAR § 52.249-10.
[17]FAR § 52.242-14.
[18]The UCC, which applies to the sale of goods and other commercial transactions, has been adopted in 49 states (Louisiana is the exception), the District of Columbia, and the Virgin Islands.
[19]UCC § 2-316.
[20]UCC §§ 2-718, 2-719.

and extensive regulations. Administrative boards of contract appeals and special courts have operated for decades for the sole purpose of resolving disputes on federal contracts.[21] Each year the boards and courts generate hundreds of decisions that collectively provide the single largest body of law in the area of construction disputes. Numerous fundamental principles of construction law have their genesis in the law of government construction contracts. It is impractical to speak of modern American construction law without the consideration of federal procurement law.

1. The Federal Acquisition Regulation and Its Supplements

Most government construction contracts reflect policies contained in statutes and in the Federal Acquisition Regulation.[22] Besides containing standard contract clauses, the FAR also sets forth extensive guidance to the federal agencies and their personnel regarding the award and administration of government construction contracts. In addition to the basic FAR, many of the federal agencies have their own supplements to the FAR. For example, the DFARS is the Defense Federal Acquisition Regulation Supplement. These supplements can substantially alter a contractor's rights, obligations, and remedies on a government contract with that agency. While possibly not as complex as the federal income tax regulations, the collective volume of these procurement regulations is extensive.[23]

Since the FAR contains in excess of 1,800 pages of materials, understanding its basic organization helps the user to navigate this procurement regulation. The FAR is subdivided into eight major subchapters containing 53 parts. Parts 1 to 51 contain substantive guidance and policy statements. Part 52 contains the clauses used in government contracts, and Part 53 contains examples of many of the standard forms used in contracting.

Each of these parts addresses a separate aspect of the acquisition process and contains policy guidance or direction, instructions on the use of contract provisions, and the text of the actual contract clauses. The eight major subchapters are:

[21] *See* **Chapter 15**.

[22] The United States Postal Service contracts under authority of the Postal Services Reorganization Act, 39 U.S.C. § 410(a), which exempts the Postal Service from the federal procurement laws and regulations governing traditional federal agencies. The Postal Service has its own regulations and policies contained in its Purchasing Manual. The Federal Aviation Administration is exempt from several procurement statutes pursuant to Pub. L. No. 104-50. Both agencies have boards and procedures to address claims and disputes.

[23] As published by the Government Printing Office, the FAR and its supplements are found in 48 C.F.R. (Web site: *http://ecfr.gpoaccess.gov*). Collectively, the FAR and its supplements total in excess of 4,100 pages of material. While the FAR contains separate parts or sections for particular types of contracts, those designations may be misleading. For example, FAR Part 36 is entitled "Construction and Architect-Engineer Contracts," but that part does not contain all of the provisions and regulatory guidance applicable to construction contracts. In addition, 41 C.F.R. Chapters 50, 51, 60 and 61 contain an additional 240 pages of regulations addressing wage and hour laws, affirmative action requirements, and other labor laws governing the performance of government contracts.

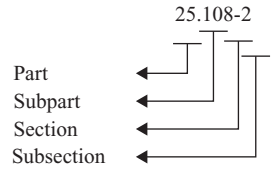


Figure 1.1 Makeup—FAR Number Citation

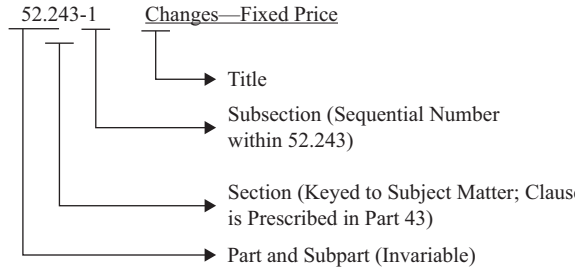
A. General (Parts 1-4)
B. Competition and Acquisition Planning (Parts 5-12)
C. Contracting Methods and Contract Types (Parts 13-18)
D. Socioeconomic Programs (Parts 19-26)
E. General Contracting Requirements (Parts 27-33)
F. Special Categories of Contracting (Parts 34-41)
G. Contract Management (Parts 42-51)
H. Clauses and Forms (Parts 52-53)

Within each of these parts are subparts, sections, and subsections. The FAR contains a numbering system that allows for discrete identification of every FAR paragraph. The digits to the left of the decimal point represent the part number. The numbers to the right of the decimal point and to the left of the dash represent, in order, the subpart (one or two digits), and the section (two digits). The number to the right of the dash represents the subsection. Subdivisions may be used at the section and subsection level to identify individual paragraphs. Figure 1.1 illustrates the structure of a typical FAR number citation (FAR 25.108-2).

Subdivisions in the text or a provision of the FAR below the section or subsection level consist of parenthetical alphanumerics using this sequence: (a)(1)(i)(A)(*1*)(*i*).

The various FAR contract clauses for all types of government contracts are found in Part 52. The numerical designation for each of these clauses contains a reference to the applicable substantive provision in the FAR, which provides guidance on its use. For example, Figure 1.2, the designation for the Changes clause for supply contracts (FAR 52.243-1), illustrates the makeup of the designation for a FAR clause.

Figure 1.2 Makeup—FAR Clause Citation



Although Part 36 of the FAR is entitled "Construction and Architect-Engineer Contracts," that part does not contain all of the provisions or policy guidance related to construction contracts. For example, the policy guidance for the Prompt Payment for Construction clause (FAR 52.232-27) is found in Part 32 of the FAR, which is entitled "Contract Financing." Many other key clauses similarly are found in various parts of the FAR; for example, the Suspension of Work clause (FAR 52.242-14), which obligates the government to compensate the contractor for certain government-caused delays, implements policy found in Part 42, "Contract Administration and Audit Services."

This organization can add some degree of potential confusion when determining whether a solicitation contains the correct FAR clause. Fortunately, FAR Subpart 52.3 contains a detailed matrix listing each of the clauses found in Part 52 together with a listing of principal types of contracts—for example, fixed-price construction contracts ("FP CON"). In the matrix column under FP CON are designations if a particular clause is generally authorized or required in that type of contract and a reference to the section of the FAR that prescribes the use of that clause. These designations are:

R = Required

A = Required when Applicable

O = Optional

By referring back to the substantive sections of the FAR (Parts 1-51), it is possible to review any policy guidance on the use of a particular clause or any variation of that clause.

Part 2 of the FAR contains definitions of many of the key words and terms used in the FAR. However, the listing of definitions is not comprehensive, as other definitions are found in other parts or subparts of the FAR. For example, very broad definitions of "subcontract" and "subcontractor" are set forth in FAR 44.101.[24]

In addition to the clauses required or authorized by the FAR, contractors also need to identify and review contract clauses that may be included in a contract pursuant to agency supplements to the FAR. As illustrated by the clauses in the Defense Federal Acquisition Regulation Supplement, DFARS 252.201-7000, Contracting Officer's Representative,[25] and the Department of Veterans Affairs Acquisition Regulation, VAAR 852.236-88, Contract changes—supplement,[26] these so-called supplements can substantially affect a contractor's obligations and limit its substantive rights.

[24]Those definitions are broader than the generally accepted understanding of these terms in the construction industry as they include vendors or materialmen providing supplies or equipment under purchase orders as well as firms performing work on the project site as subcontractors. This difference needs to be understood in the context of the administration of a government contract and the drafting of subcontracts and purchase orders for government contracts.

[25]*See* **Chapter 2.**

[26]*See* **Chapter 8.**

One major difference between most private commercial construction contracts and government contracts is the government's practice of *incorporating by reference* many key clauses from the FAR or the agency's FAR supplement into the construction contract. Upon reviewing a solicitation for a government project, a contractor may find a multipage listing of clauses with the FAR or the FAR supplement numerical designations. The significance of these clauses is not diminished by their listing on a multipage table of incorporated clauses. As part of its evaluation of the potential risks and obligations, a contractor should obtain and review each of those provisions. For a firm that is relatively new to government contracting, this review can be rather time intensive. Fortunately, most of the standard FAR clauses are revised on a relatively infrequent basis.[27] Once one becomes familiar with the FAR clauses and applicable agency supplements, the time needed to review subsequent solicitations from the same agency is substantially reduced.

Disputes arising out of or related to the performance of a government construction contract are governed by the Contract Disputes Act (CDA).[28] The CDA and its implementing regulations set forth a comprehensive approach to the resolution of contract claims by contractors and the government. (See **Chapter 15**.) The citations in this book are to the appropriate provisions of the CDA, other relevant statutes, and the applicable regulations, particularly the FAR, as well as to the various board and court decisions. The CDA and the other cited statutes are found in West Publishing Company's *United States Code Annotated*. Citations to the FAR and the agency supplements are found in Title 48 of the Code of Federal Regulations (CFR).

The current disputes procedure has its roots in practices that developed from the early part of the twentieth century. Over nearly 100 years, the process has evolved as efforts to remedy possible or actual procedural or substantive problems have been implemented. Understanding this history evolution provides a useful perspective on the current status of the disputes process. Consequently, **Appendix 1A** to this chapter provides an overview on the history and evolution.

2. Court, Board, and Bid Protest Decisions

Government contract case law is found in a variety of sources. Since 1921, selected bid protest decisions issued by the United States Government Accountability Office (GAO) have been published in the *Decisions of the Comptroller General of the United States.*[29] Beginning in 1974, Federal Publications, Inc., now part of the West Group, has published the *Comptroller General's Procurement Decisions* (*CPD*) service containing the full text of all of the GAO's bid protest decisions. Court decisions regarding bid protests have been issued by the federal district courts,[30] the

[27]For example, the standard Differing Site Conditions clause in government construction contracts, FAR 52.236-2, was last revised in April 1984.
[28]41 U.S.C. §§ 601 *et seq.*
[29]Formerly the General Accounting Office. Typically, about 10 percent of the GAO's decisions in a given year are published in that publication.
[30]The U.S. Federal District Courts' jurisdiction over bid protests ended as of January 2001.

various federal circuit courts of appeals, the United States Court of Federal Claims (and its predecessor courts), and the United States Court of Appeals for the Federal Circuit. The case law involving claims and disputes arising out of or related to the performance of a contract basically consists of the decisions of the various boards, United States Court of Claims, United States Claims Court, United States Court of Federal Claims (Court of Federal Claims), and the United States Court of Appeals for the Federal Circuit (Federal Circuit). On relatively rare occasions, the United States Supreme Court will consider and issue decisions directly addressing federal government contracts.[31]

The Court of Claims, which was abolished in 1982, had jurisdiction to entertain suits involving government contract claims, including claims under the CDA. When Congress abolished the Court of Claims, it created the Claims Court, now the Court of Federal Claims,[32] and granted to it all of the original jurisdiction of the Court of Claims.[33] At the same time, Congress also created a new United States Court of Appeals for the Federal Circuit.[34] The Federal Circuit reviews appeals of decisions from the boards and the Court of Federal Claims.[35] The Court of Federal Claims and the Federal Circuit view decisions of the old Court of Claims as binding precedent.[36]

B. Contracts Funded by Federal Grants

Although not considered to be *government construction contracts*, many federal agencies provide grants to state, county, and municipal agencies to partially fund construction projects. These grant agreements may provide for the inclusion of clauses or application of federally mandated policies in the actual construction contracts. These grant agreements are addressed in **Chapter 16** of this book.

C. Effect of Statutes and Regulations on Contractors

1. Possible Conflicting Themes

When contracting with the federal government, contractors need to appreciate that there are two fundamental and potentially conflicting policies that may affect the parties' rights and obligations. One policy addresses the status of the United States when it enters into a contract in the commercial marketplace. This was summarized in *McQuagge v. United States*[37]:

[31]*See, e.g., S&E Contractors, Inc. v. United States,* 406 U.S.1 (1972).
[32]28 U.S.C. § 171.
[33]28 U.S.C. § 1491(a)(2). The United States Court of Federal Claims has the same basic jurisdiction but broadened to include nonmonetary claims.
[34]28 U.S.C. § 41.
[35]41 U.S.C. § 607(g)(1)(A); 28 U.S.C. § 1295(a)(10), (a)(3).
[36]*South Corp. v. United States,* 690 F.2d 1368, 1369 (Fed. Cir. 1982) (en banc); United States Court of Federal Claims Gen. Order No. 33, 27 Fed. Cl. xyv (1992).
[37]197 F. Supp. 460 (W.D. La. 1961).

> In ordinary contractual relations with its citizens, the government enjoys the same privileges and assumes the same liabilities as does its citizens. This is distinguished from the situation where the sovereign is seeking to enforce a public right or protect a public interest, for example, eminent domain or an exercise of the taxing power. In the latter case the government is not bound by ordinary rules of private contract law or by doctrines of estoppel or waiver. When the government enters the market place, however, and puts itself in the position of one of its citizens seeking to enforce a contractual right (i.e., one which arises from express consent rather than sovereignty), it submits to the same rules which govern legal relations among its subjects.[38]

Many of the decisions that provide that the United States is bound by its contracts just as a private party involve questions of contract interpretation.[39] However, another theme in government contract cases reflects a statement by Justice Oliver Wendell Holmes, Jr., that "Men must turn square corners when they deal with the Government."[40] This statement would seem to imply that the government may have, in certain respects, a special status in its contractual relationships and that all of the rules governing contractual relationships may not apply in government contracts. While the standard contract provisions in a government construction generally reflect a balanced allocation of risks, there are many special requirements and legal principles, which every contractor must appreciate. These are the "square corners" of contracting with the government in the twenty-first century.

2. Authority and Public Policy Considerations

While the two themes just noted appear to conflict, the *McQuagge* decision referenced two conditions that are critical to understanding them. First, the government must be acting in a contractual capacity. Second, it must not be seeking to protect or enforce a public policy.

There is no question that the government has the capacity to enter into a contract.[41] However, a contract that is prohibited by statute or varies from mandatory procedures is not enforceable or binding on the government.[42] Similarly, the person or entity entering into a contract on behalf of the government must have the requisite authority to do so. If that person has the requisite authority to bind the government, the exercise of that authority usually involves a degree of discretion.[43] Consequently, if the contractual action by the government's representative reflects an error in judgment, the government usually is bound so long as the person was acting within the limits of that person's authority.[44]

[38]197 F. Supp. at 469; *see also Mann v. United States,* 3 Ct. Cl. 404, 411 (1867); *Hollerbach v. United States,* 233 U.S. 165 (1914).
[39]*See, e.g., Hollerbach v. United States,* 233 U.S. 165 (1914).
[40]*Rock Island, Ark. & La. R.R. v. United States,* 254 U.S. 141, 143 (1920).
[41]*United States v. Tingey,* 30 U.S. 115 (1831).
[42]*The Floyd Acceptances,* 74 U.S. 666 (1868).
[43]*Arizona v. California,* 373 U.S. 546 (1963); *United States v. MacDaniel,* 32 U.S. 1 (1833).
[44]*United States v. Winstar Corp.,* 518 U.S. 839 (1996); *Cooke v. United States,* 91 U.S. 389 (1875); *Liberty Coat Co.,* ASBCA No. 4119, 57-2 BCA ¶ 1576.

The key is ascertaining the limits of authority. This is one of those square corners for government contractors. The limits of authority question was addressed by the United States Supreme Court in *Federal Crop Insurance Corp. v. Merrill,*[45] which involved an issue of the ability of an unauthorized agent of a government agency to bind the United States. The Court rejected the application of the concept of apparent authority and ruled that the party dealing with the United States had the burden of ascertaining the *actual authority* of the government's representative. The Court, after reviewing the prior proceeding in the case, stated:

> That court [Supreme Court of Idaho] in effect adopted the theory of the trial judge, that since the knowledge of the agent of a private insurance company, under the circumstances of this case, would be attributed to, and thereby bind, a private insurance company, the Corporation [United States] is equally bound.
>
> The case no doubt presents phases of hardship. We take for granted that, on the basis of what they were told by the Corporation's local agent, the respondents reasonably believed that their entire crop was covered by petitioner's insurance. And so we assume that recovery could be had against a private insurance company. But the Corporation is not a private insurance company. It is too late in the day to urge that the Government is just another private litigant, for purposes of charging it with liability, whenever it takes over a business theretofore conducted by private enterprise or engages in competition with private ventures. Government is not partly public or partly private, depending upon the governmental pedigree of the type of a particular activity or the manner in which the Government conducts it. The Government may carry on its operations through conventional executive agencies or through corporate forms especially created for defined ends. *See Keifer & Keifer v. Reconstruction Finance Corp.*, 306 U.S. 381, 390. Whatever the form in which the Government functions, anyone entering into an arrangement with the Government takes the risk of having accurately ascertained that he who purports to act for the Government stays within the bounds of his authority. The scope of this authority may be explicitly defined by Congress or be limited by delegated legislation, properly exercised through the rule-making power. And this is so even though, as here, the agent himself may have been unaware of the limitations upon his authority.[46]

The *Federal Crop Insurance* decision reflects one of the two conditions expressed in *McQuagge.* The government must have entered into a valid contractual relationship. A valid contract can occur only if the government's representative is authorized to bind the United States. A similar condition applies to changes ordered by a representative of the government. Since the contractor bears the burden to ascertain the authority of the person with whom it is dealing, the often critical issue related to authority is addressed in several chapters of this book. (See **Chapters 2, 8, and 10.**)

[45]332 U.S. 380 (1947).
[46]332 U.S. at 383-384.

The second *McQuagge* exception to the general principle that the United States is bound to its contracts in the same manner as a private party referred to the enforcement of a *public right* or *public interest.* This exception is best illustrated by the decision of the United States Court of Claims in *G. L. Christian & Associates v. United States.*[47] The *Christian* decision involved a contractor's claim for its lost anticipated profits following the government's decision to terminate for convenience a large housing project. The contract did not contain a termination for convenience clause;[48] hence, there was no contractual preclusion on the recovery of lost anticipated profits. While acknowledging the basic principle that the government has the rights and ordinarily the liabilities of a private party when it enters into a contract, the Court of Claims held that the termination for convenience clause was incorporated into the contract by operation of law as it was a mandatory clause under the applicable procurement regulations.[49]

While the Christian doctrine appears to apply only to mandatory clauses that implement fundamental policy, a contractor generally is deemed to be on notice of these clauses. Contractual notice of the provisions to the contractor occurs following publication of the procurement regulation in the *Federal Register.*[50] If a regulation is not published in the *Federal Register,* the contractor still may be bound if it has actual notice or knowledge of it.[51] Given this doctrine, any government construction contractor needs to have a basic understanding of the key principles affecting the interpretation and enforcement of the standard mandatory clauses and the ability to obtain advice on these provisions. In addition, as the FAR provides guidance to the government's representatives on the award and administration of government contractors, a contractor should obtain or have access to the edition of the FAR and any agency supplements applicable to its contract.[52]

Another potential square corner for a government contractor follows from the principle that actions taken by a government official within the limits of that person's authority are presumed to be properly made unless contrary to law or regulation.[53] While this doctrine may operate to protect a contractor when the government's authorized representative makes what is later challenged as a bad business decision,[54] the same presumption that the contracting officer acted in good faith makes it very difficult to overturn actions such as termination for convenience on the basis that the action was an abuse of discretion, taken in bad faith, or motivated with malice toward the contractor.[55]

[47]312 F.2d 418 *rehearing denied* 320 F.2d 345 (Ct. Cl. 1965).
[48]*See* **Chapter 11** for a discussion of convenience terminations.
[49]312 F.2d at 427.
[50]41 U.S.C. § 4186.
[51]*Timber Access Indus. Co. v. United States,* 553 F.2d 1250 (Ct. Cl. 1977).
[52]Electronic versions of the FAR and its supplements can be accessed at the Government Printing Office's Web site, *http://ecfr.gpoaccess.gov.* (This Web site contains current versions of the FAR and its supplements and is updated on almost a daily basis.)
[53]*General Electric Co. v. United States,* 412 F.2d 1215 (Ct. Cl. 1969).
[54]*McQuagge v. United States,* 197 F. Supp. 460 (W.D. La. 1961); *Conrad Weihnacht Constr., Inc.,* ASBCA No. 20767, 76-2 BCA ¶ 11,963.
[55]*See Librach v. United States,* 147 Ct. Cl. 605, 612 (1959); *Kalvar Corp. v. United States,* 543 F.2d 1298 (Ct. Cl. 1976); *see also* **Chapters 2 and 11.**

IV. PROCUREMENT INTEGRITY AND STANDARDS OF CONDUCT

Government contractors are expected to conduct business with a high degree of integrity and ethics. The consequences for failing to meet these expectations of integrity when dealing with the federal government can be extremely serious. The remedies that the government may utilize include contract cancellation, debarment, fines, damages, forfeiture of claims as well as criminal sanctions. Consequently, these expectations, as well as the related laws and regulations, must be understood and appreciated by contractors and subcontractors performing work for the government. The most common way that the government asserts its expectations of honesty and integrity is through the application of various anti-fraud and false claims statutes. The government effort to prevent fraud and false claims may become more focused on the construction industry in the near future. Past efforts, which have resulted in substantial payments to the government, primarily focused on the healthcare industry. However, allegations of abuses in Iraq and elsewhere have placed government construction and service contractors in the spotlight. An initial tool that the government employs to alert its contractors to the expectations related to integrity and ethics involve a broad variety of contractor certifications related to its actions and contract performance. Complete treatment of the details of the various laws and regulations and their interpretation is beyond the scope of this book and would justify, if not require, an entire separate book. However, contractors need to appreciate they will be held to a high standard of business ethics and conduct.[56]

A. Importance of Certifications

Central to government contracting is the requirement that contractors and subcontractors must deal honestly with the government. This theme is reflected in the general standards of responsibility for a prospective contractor[57] and in the requirements for certification of cost or pricing data[58] and claims.[59]

Consistent with the expectation of a high standard of ethics and conduct, contractors are routinely required to provide certifications during all phases of the contracting process, from the initial solicitation to the resolution of claims. Often these certifications provide the initial foundation of the government's assertion of wrongdoing by a contractor. Consequently, no certification or affirmation of fact should be dismissed as just *another government form.*

[56]*See* FAR § 3.1002(a) (government contractors are expected to conduct themselves with the "highest degree of integrity and honesty").
[57]FAR § 9.104-1(d).
[58]FAR § 15.403.
[59]FAR § 33.207. *See also* **Chapter 15**.

While the subject matter and wording of contractor-provided certifications are subject to change, **Table 1.1** lists many of the certifications, affirmations, or representations currently required of a government construction contractor.[60]

While a few of these provisions reference potential liabilities associated with the various certifications, many are silent. In that regard, the FAR requires the inclusion of this clause in sealed bid procurements issued under FAR Part 14:

> **FAR § 52.214-4 FALSE STATEMENTS IN BIDS (APR 1984)**
>
> Bidders must provide full, accurate, and complete information as required by this solicitation and its attachments. The penalty for making false statements in bids is prescribed in 18 U.S.C. 1001.

This provision is not mandated for use in negotiated contracts awarded under FAR Part 15. However, 18 U.S.C. § 1001, the False Statements Act, which is referenced in the False Statements in Bids clause, is not limited in its application to sealed bid procurements.[61]

B. Overview of Federal Laws Related to Procurement Integrity/Standards of Conduct

Whether competing for or performing a government contract, every contractor needs to appreciate the broad scope of legislation intended to protect the government (the public) from a variety of prohibited activities. These laws prescribe a range of improper actions and the applicable civil and criminal sanctions. However, the government agencies perceive that the task of inspecting work and determining compliance with the contract requirements for billions of dollars in contracts every year is extremely difficult.

[60]Each contract, including those provisions incorporated by reference, should be screened to identify requirements for contractor certifications and representations, as the extent and scope of the requirements for certifications and representations are receiving extensive Congressional review and are becoming more detailed. For example, Section 872 of the Duncan Hunter National Defense Authorization Act of 2009 (Pub. L. 110-417) requires the Office of Management and Budget and the General Services Administration to establish, within one year of the effective date of that legislation (October 14, 2008), an information database on the integrity and performance of contractors that will be available to all federal agencies and grantees. That legislation also directs the adoption of regulations within one year of the effective date of the legislation requiring contractors with agency awards or grant contracts with a total value in excess of $10,000,000 to provide to the federal government detailed information similar to that currently found in FAR § 52.209-5 with certain critical differences. The new reporting requirements, representations, and database will cover a **five year** period, not three years, and will include disclosure of civil judgments "in connection with" the award or performance of a contract or grant with the federal government, default terminations, and the administrative resolution of suspension or debarment proceedings. The phrase "in connection with" is not defined in the Duncan Hunter Act.

[61]*See also* 15 U.S.C. § 645(d) (provides for criminal penalties for knowingly misrepresenting a firm's small business size status).

Table 1.1 Contractor Certifications and Representations

Title of Provision	FAR Reference	Basic Subject Matter
Certification of Independent Price Determination	FAR § 52.203-2	Price competition and actions to influence others in submitting offers in connection with a solicitation
Covenant Against Contingent Fees	FAR § 52.203-5	Agents engaged to solicit award
Taxpayer Identification	FAR § 52.204-3	Ownership and tax status of bidder/offeror
Certification Regarding Responsibility Matters	FAR § 52.209-5	Certification by offeror regarding whether it and/or any of its *principals* are or are not debarred, suspended, proposed for debarment, or declared ineligible for award of a federal agency contract; have or have not, within a three-year period preceding the offer on the contract, been convicted or had a civil judgment rendered against them for fraud or certain criminal offenses in connection any public contract or subcontract; are or are not presently indicted or civilly charged for fraud or certain criminal offenses in connection any public contract or subcontract; have or have not, within a three-year period preceding the offer on the contract, been notified of delinquent federal taxes in excess of $3,000 owed by the contractor or its *principals*
Small Business Program Representations	FAR § 52.219-1	Status of bidder/offeror under various SBA-related preference programs
Certificate of Current Cost or Pricing Data	FAR § 15.406-2	Applicable when contractor submits cost or pricing data for proposals or modifications (equitable adjustments)
Subcontractor Cost or Pricing Data—Modifications	FAR § 52.215-13	Applicable when subcontractor submits cost or pricing data for pricing of contract modifications (equitable adjustments)
Payrolls and Basic Records	FAR § 52.222-8	Certification that Davis Bacon wages fully paid and data on payroll records form (e.g., social security numbers) are accurate and complete

Affirmative Action Compliance	FAR § 52.222-25	Affirmative Action Program Status
Exemption from Application of Service Contract Act Provisions	FAR § 52.222-48	Contractor certification that services qualify as “commercial items” and priced based on catalog or market prices
Recovered Material Certification	FAR § 52.223-4	Applies if specifications required use of Environmental Protection Agency-designated products
NC State and Local Sales and Use Tax	FAR § 52.229-2	Certification and payment of North Carolina taxes
Disclosure Statement—Cost Accounting Practices And Certification	FAR § 52.230-1	Applicability of cost accounting standards to offeror
Payments under Fixed-Price Construction Contracts	FAR § 52.232-5	Amounts requested are only for performance in accordance with specifications, terms, and conditions of contract; payments to subcontractors have been made from previous payments; timely payments to subcontractors will be made; and payment request includes no amount that prime contractor intends to withhold (retain) from a subcontractor or supplier
Disputes	FAR § 52.233-1	Claims in excess of $100,000.00
Certification of Final Indirect Costs	FAR § 52.242-4	No unallowable costs are included in the costs used to establish indirect cost rates (Applies to cost reimbursement construction contracts)
Termination for Convenience Settlement Proposals (Total Cost Basis)	FAR § 53.301- SF 1436	Proposal reflects recognized commercial accounting practices and includes only those charges allocable to terminated contract and that are fair and reasonable
Termination for Convenience Schedule of Accounting Information	FAR § 53.301- SF 1439	Disclosure of contractor’s accounting practices

Three different approaches have been adopted to address this difficulty. One approach involves the broad use of contractor furnished certifications and representations. Many of these are identified in **Table 1.1** of this chapter. These certifications and representations can serve at least three possible purposes.

(1) Alert the contractor signing the certification or representation to the significance of its signature.
(2) Simplify the government's proof in establishing a violation of an underlying statute.
(3) Create the basis for an action based solely on the false nature of the certification.

The final two purposes involve multiple civil and criminal statutes addressing prohibited conduct and the provision of economic incentives to those who report wrongdoing. In that regard, federal law provides substantial economic incentives or bounties for individuals to disclose fraudulent conduct by government contractors. In 1986 Congress amended the Civil False Claims Act, 31 U.S.C. §§ 3729-3733 to encourage third parties to identify and institute civil *qui tam* actions[62] involving allegations of fraudulent conduct and to share in the recovery of those actions. Coupled with this statute are requirements for self-reporting and/or hotlines as discussed in **Section IV.F** of this chapter.

The federal false claims and anti-fraud statutes are varied in terms of the subject matter of the prohibited conduct or activities. Some of the statutes provide for civil penalties or sanctions for prohibited activities while others provide for criminal sanctions. **Table 1.2** lists many of the statutes in the government's arsenal of remedies for contractor fraud and false claims.

C. Civil False Claims Act Actions

Although there are multiple statutes available to the government to combat improper conduct, fraud, and false claims, the civil False Claims Act[63] (FCA) is often invoked by the government as the preferred statutory basis for an action rather than the parallel criminal FCA statute or other anti-fraud statutes. Through 2008, an average of 457 new FCA matters were begun each year. There are several reasons for this preference: the *qui tam* provisions of the FCA, the proof of knowledge standard, and the way in which the statute deals with and assesses damages.

1. Qui Tam Provisions of the FCA

Included in the 1986 revisions of the False Claims Act, the *qui tam* provisions allow for private individuals to bring suits as "whistleblowers" against entities that may be liable under the FCA.[64] These suits are brought on behalf of the federal government.

[62]Essentially means private attorney general actions.
[63]31 U.S.C. §§ 3729 *et. seq.*
[64]31 U.S.C. § 3730(b)(1).

Table 1.2 Federal Anti-Fraud/False Claims Laws

Title	Statutory Reference	Subject Matter/Notes
Criminal Statutes		
Anti-Kickback Act	41 U.S.C. §§ 51–58	Prohibits payments by subcontractors at any tier to prime contractors or subcontractors to obtain a government contract
Conspiracy to Defraud	18 U.S.C. § 286; 18 U.S.C. § 371	Addresses claims and general conspiracy to defraud the government
False Claims Act, Criminal Liabilities	18 U.S.C. § 287	False claim need not have been paid by government to provide basis of liability
Theft from Federal Programs	18 U.S.C. § 666	Applies to theft from state and local public agencies receiving federal funds by "agents" of those agencies
False Statements Act	18 U.S.C. § 1001	Includes statements, false entries, oral and unsworn statements
Mail and Wire Fraud	18 U.S.C. §§ 1341–1350	Applies to use of mails and telecommunications to execute a scheme to defraud the United States
Major Fraud Act	18 U.S.C. § 1031	Applies to procurement fraud on a government contract or subcontracts there under valued at $1 million or more
Obstruction of Federal Audit	18 U.S.C. § 1516	Applies to any person employed on full-, part-time, or contractual basis to conduct an audit or a *quality assurance inspection* for or on behalf of the United States
Sarbanes-Oxley Act of 2002	18 U.S.C. § 1519	Applies to anyone who knowingly alters a document with intent to influence proper administration of any matter within jurisdiction of department or agency of the United States; violators subject to fines or imprisonment up to 20 years, or both
Civil Statutes		
Anti-Kickback Act	41 U.S.C. §§ 51–58	Prohibits kickback by subcontractors and suppliers
Contract Disputes Act of 1978	41 U.S.C. § 604	False or unsupported claims submitted to contracting officer; necessity for certification
False Claims Act	31 U.S.C. §§ 3729–3733	Applies to any request for money or property used on the government's behalf or to advance a government program or interest if the government provides any portion of the money or property or reimburses a third party for any portion of the money or property
Forfeiture of Claims Act	28 U.S.C. § 2515	Allows a special plea in United States Court of Federal Claims providing for forfeiture of entire claim if any part of it is tainted by fraud
Program Fraud Act	31 U.S.C. §§ 3801–3812	Administrative alternative to litigation in civil false statements and smaller false claims cases
Truth in Negotiations	10 U.S.C. § 2306a; 41 U.S.C. § 254	Cost or pricing data on negotiated contracts or subcontracts; modifications of contracts in excess of $650,000;[a] necessity for certification

[a.] This amount is subject to adjustment for inflation every five years.

The individual bringing suit, whether a person or a corporate entity, called a relator in the litigation, is entitled to share in any recovery that results from the suit. Individuals who are in positions to know of potentially unlawful conduct have an incentive to bring the allegations to light primarily because of the prospect of sharing in any recovery from the contractor. The government benefits from the *qui tam* provisions because the individual bringing the FCA suit is often in a position to know a great deal more information concerning the activities of a contractor or subcontractor than the government agency administering the contract or the Department of Justice might know. The *qui tam* provisions in conjunction with other changes to the FCA made in 1986 have had an impact. According to Department of Justice statistics, the average number of FCA *qui tam* actions outnumbers non-*qui tam* actions by a ratio of nearly 2 to 1.[65] Since 1986, more than $21 billion has been recovered though FCA judgments and settlements. In fiscal year 2008 alone, recoveries amounted to at least $1.34 billion.[66] Of that recovery, the *qui tam* relator usually shares approximately 15% of the amount recovered.

2. Proof of Knowledge Standard

The criminal False Claims Act requires proof that the false statement was made with intent to deceive, was designed to induce a belief in the false statement or to mislead.[67] A "knowing" act means "[a]n act is done knowing if the defendant realized what he or she is doing, and did not act through ignorance, mistake or accident."[68] Intentional ignorance has been held to constitute constructive knowledge sufficient to satisfy this element of the offense.[69] In addition, the false statement need not be delivered to the government if it was relied on in the disbursement of funds provided by the government.[70]

In contrast, the civil FCA has a lower scienter, or knowledge, requirement. There is no requirement of specific intent to defraud. Unless an allegation of conspiracy is made, the level of "knowledge" for a civil FCA action is defined in 31 U.S.C. § 3729(b)(1) as:

(i) [having] actual knowledge of the information;
(ii) [acting] in deliberate ignorance of the truth or falsity of the information; or
(iii) [acting] in reckless disregard of the truth or falsity of the information.

In *United States ex rel Bettis v. Odebrecht Contractors of CA, Inc.,*[71] the court applied this standard to a civil false claims action related to a project for the construction of an embankment dam. During the bidding, the contractor Odebrecht underbid the contract so that the second-lowest bidder was approximately $30 million higher

[65]*See www.usdoj.gov/opa/pr/2008/November/fraud-statistics1986-2008.htm* (accessed July 14, 2009).
[66]*See www.usdoj.gov/opa/pr/2008/November/08-civ-992.html* (accessed July 14, 2009).
[67]*United States v. Lichenstein*, 610 F.2d 1272 (5th Cir. 1980), *cert. denied,* 447 U.S. 907 (1980).
[68]*United States v. Ibarra-Alcarez*, 830 F.2d 968 (9th Cir. 1987).
[69]*United States v. Petullo*, 709 F.2d 1178 (7th Cir. 1983).
[70]*Id.* at 1180.
[71]297 F.Supp. 2d 272, 277-8 (D.D.C. 2004).

and the estimate made by the Corps of Engineers was approximately $35 million higher than the contractor's bid. The plaintiff alleged in his FCA suit that the contractor underbid the project in order to seek adjustments to the contract price at a later date. The court rejected this argument as contrary to the reality of government contracting, which allows for flexibility through the process of equitable adjustments.[72] What the FCA requires is that a contractor knowingly make a claim for monies to which it would not otherwise be legitimately entitled.[73]

In cases asserting violations of the False Claims Act, courts will, when it is appropriate, impute the knowledge of employees to a contractor in order to impose direct liability upon the contractor. The imposition of direct liability on the contractor will depend on whether the employee at fault was acting within the scope of his or her employment with the intent to benefit the contractor. In *United States v. Dynamics Research Corp.*,[74] the district court faced the question of whether to impute the knowledge of the employees to the contractor. The employees used their position to influence the Air Force to purchase goods and services from third parties that in turn paid the employees when the employees provided the goods or services.[75] However, the court did not impute the knowledge of the employees to the contractor because the employees concealed their actions from their employer.[76] The court refrained from entering summary judgment for the government on the *direct liability* theory partly due to the lack of proof that the contractor enjoyed any benefit from the conduct of the employees. The court found that the contractor did not receive any payment and the government's argument that the contractor received the benefit of meeting contractual obligations as to minority-owned subcontractors was not persuasive.[77] Also, the court found that the employees did not hold positions in the company so that their actions were indistinguishable from the corporation.[78] The court ruled that the employees did not constitute the "apex of power" in the company. If the employees were the "apex of power," then questions of scope of employment and benefit would be irrelevant.[79]

The court then discussed whether it could impose *vicarious liability* on the contractor. Vicarious liability turns on whether the employee had **apparent authority**. If an employee occupies a position in which "according to the ordinary habits of persons in the locality . . . it is usual for such an agent to have a particular kind of authority, anyone dealing with him is justified in inferring that he has such authority."[80] In *Dyanmics Research*, the employee at fault occupied a position where he was to provide technical advice to the Air Force and to steer the Air Force to third-party contractors for needs relating to the prime contract. The court found that the

[72]*Id.* at 281.
[73]*Id.*
[74]2008 WL 886035 (D.Mass. 2008).
[75]*Id.*
[76]*Id.* at *13.
[77]*Id.*
[78]*Id.*
[79]*Id.* (citing *United States. v. DiBona*, 614 F. Supp. 40, 44 (E.D. Pa. 1984).)
[80]*Id.* at *14 (quoting *Restatement (Second) of Agency 14* § 49(c).

employee had apparent authority and that the contractor could be held vicariously liable.[81] Under the theory of vicarious liability, there is no consideration of whether the employee was acting as to benefit the contractor, as under a direct liability theory.[82] If a court finds the employee had apparent authority for his actions, then it will not consider whether the company received a benefit. Instead, the court will hold the contractor vicariously liable. Ultimately the vicarious liability theory may be easier for the government to prove because it does not require proof of employee intent.

On a practical level, these two theories of liability under the FCA increase the benefit of "self-policing" by the contractor and the adoption of a meaningful ethics compliance program. A contractor should know what its employees are doing and what other business affairs they are involved in, and take steps to make sure that its employees are maintaining the same expectations of integrity that the contractor as a whole is required to maintain.

3. Fines and Damages

The monetary penalties for a contractor found liable under the False Claims Act may include fines, damages or both. Under the civil FCA, a court may assess a fine of between $5,000 to $10,000 fine for each false claim submitted to the government. In *United States v. United Technologies Corp.*,[83] the court found that the contractor had submitted 709 invoices to the Air Force for payment under its multi-year contract to furnish jet engines that were tainted by a false claim (misrepresentation) made at the time of the proposal on the contract. In finding that United Technologies was liable under the FCA, the court considered each individual invoice to be a separate claim and assessed fines in the amount of $7,090,000.[84] The basis for the false claim action was the contractor's explanation of the factual basis for the pricing of the engines over a multi-year period. Although the contractor stated to the government that it had utilized certain data in predicting future costs and prices, it did not utilize that data, and the court found the contractor was obliged to have followed through with its representation.[85] There were no damages because the court additionally found that the contractor reduced the price of the engines so that the government saved money over the term of the contract.[86] A contractor should recognize that even if the government is not harmed or even benefits from a false statement, as in *United Technologies*, the contractor still can be held liable for civil penalties under the False Claims Act.

However, the false claim in a case may not be each individual voucher submitted to the government. In *United States ex rel. Longhi v. Lithium Power Technologies, Inc.*,[87] the court disagreed with the government's contention that the defendant submitted 54 vouchers, each of which would incur the $10,000 penalty. Rather, the court

[81] *Id.* at *16.
[82] *Id.* at *15.
[83] 2008 WL 3007997 (S.D. Ohio 2008).
[84] *Id.* at *12.
[85] *Id.* at *10.
[86] *Id.* at *12.
[87] 530 F.Supp. 2d 888 (S.D. Tex. 2008).

looked at the "causative act" of the defendant and awarded the penalty only for each of the four contracts in the case.[88] What constitutes an individual false claim in a case appears to be a issue that may be given wide interpretation by a trial court.

In addition to the fines that may be assessed, treble damages may be awarded to the government.[89] The determination of the extent of the damages that the government suffered will vary depending on the type of contract and the circumstances of an individual case. In *Lithium Power*, the defendants misrepresented information about their history and qualifications in order to obtain a contract under the Small Business Innovation Research Program (SBIR). In assessing damages, the court disregarded the argument that the government received benefit from the research done by the defendants. Rather, it found that the purpose of the SBIR was to award contracts to foster entrepreneurship by and the development of eligible small businesses. Since the defendants were not eligible to participate in the program, as they had misrepresented their capabilities and resources,[90] the purpose of the program was not met and the government received no benefit. The court then assessed damages equal to the value of each of the four contracts that the defendants had been awarded.[91]

4. Potential Subcontractor Liabilities

The limit of potential liability of subcontractors under the False Claim Act centers on whether the FCA would apply if a subcontractor makes a false statement but that statement is not made directly to the government. In 2008, the Supreme Court of the United States addressed this issue in *Allison Engine Co. v. United States*.[92] In *Allison Engine*, the Navy contracted with two shipyards to build a fleet of destroyers. The shipyards then subcontracted with Allison Engine to construct generator sets. Allison Engine subcontracted with other firms to manufacture parts of the generator sets and to assemble the generator sets.[93] The subcontractors were required to submit a certificate of conformance to contract specifications along with delivering each unit. Employees of one of the subcontractors filed a False Claim Act suit alleging that invoices submitted by Allison Engine and the other subcontractors had not been done in accordance with contract requirements and that the subcontractors had falsified the certificates of conformance.[94]

The Supreme Court interpreted two sections of the FCA to determine whether liability under the act could be imposed when the false statement or claim is not made to the government itself but is made to a private entity. In the prime contract for the destroyers, the shipyards were paid sums of money in advance. The shipyards then received invoices and claims for payment by the subcontractors. The Supreme Court ruled that in a situation like this, the key issue is whether "a subcontractor . . . makes

[88] *Id.* at 901.
[89] 31 U.S.C § 3729(a)(7).
[90] 530 F.Supp. 2d at 898.
[91] *Id.* at 899.
[92] 128 S.Ct. 2123 (2008).
[93] *Id.* at 2126.
[94] *Id.* at 2127.

a false statement to a private entity and does not intend the Government to rely on that false statement."[95] The subcontractors in *Allison Engine* were not held liable under the False Claims Act because the money used to pay the invoices, although originating from the government, had passed on to the shipyards, and the government no longer had any involvement in its disbursement nor any opportunity to rely on the false statements.

In 2009, Congress responded to the *Allison Engine* decision by passing amendments to the False Claims Act in the Fraud Enforcement and Recovery Act of 2009 (FERA).[96] These amendments were clearly intended to overrule the *Allison Engine* decision by eliminating the requirement that a false claim be made "to get" the claim paid by the government.[97] This amended provision is also retroactive to all claims pending on June 7, 2008, two days before the Court issued the *Allison* decision, demonstrating Congress's intent to substantially negate the effect of that decision.[98] The FERA also expands a contractor's potential liability under the FCA by changing the statute's definition of "claim." The new definition of claim now includes situations where a claim is made to a contractor where the "money is to be spent or used on the government's behalf or to advance a government program or interest."[99] Congress intentionally has closed the loophole allowed by *Allison Engine* by defining a claim to include situations where the government has already provided money to a higher-tier contractor.[100] Moreover, the expanded definition of "claim" may have an impact on contracts that do not involve the United States directly as a contracting party but instead are part of a federally funded grant to state, local, or private entities. For more on federal grants in general and the FCA's impact on those grants, see **Chapter 16**.

D. Other Remedies for Prohibited Conduct

In addition to assessing penalties and fines under the False Claims Act, the government has a number of other remedies that it can use to further accomplish the goal of preventing fraud in future contracts. These remedies are not used alone but will be employed in conjunction with the remedies of the FCA or other applicable fraud statutes, such as the Anti-Kickback Act, which calls for double damages.

1. Contract Cancellation Remedy

In addition to the specific remedies set forth in the various statutes, a government contractor faces the total cancellation of the underlying contract if it is tainted by

[95] *Id.* at 2130.
[96] PUB. L. 111-21.as codified 31 U.S.C. 3129(a)(1)(B) (2009).
[97] *Id.*
[98] In a subsequent proceeding in the *Allison* litigation, the retroactive provision of this statute was ruled to be unconstitutional under the Ex Post Facto Clause of the United States Constitution, Art. I, § 9, cl.3. *See United States v. Allison Engine Co., Inc.,* Nos.1:95-cv-970, 1:99-cv-923 (S.D. Ohio October 28, 2009).
[99] 31 U.S.C. § 3129(b)(2)(ii).
[100] 31 U.S.C. § 3129(b)(2)(ii)(1).

conduct that is considered to be a corrupt practice. In *United States v. Acme Process Equipment Co.,*[101] the contractor sued to recover breach of contract damages after the government canceled its contract. The cancellation was based on the fact that three of the contractor's employees accepted compensation for awarding subcontracts in violation of the Anti-Kickback Act. The contractor argued at the Court of Claims that contract cancellation was not an authorized remedy for a violation of the Anti-Kickback Act because both civil and criminal remedies were set forth in that statute. The Court of Claims accepted that argument on the grounds that Congress had intended to set forth the *entire* set of remedies available to the United States for a violation of that statute. The Supreme Court reversed that decision, holding that public policy requires that the United States be able to rid itself of a prime contract tainted by kickbacks. In such cases, the contractor would not be entitled to payment on a theory of *quantum merit* or otherwise, regardless of the incurrence of otherwise allowable performance costs.[102]

Applying this public policy, contract cancellation has been permitted when the contract was tainted by the making of false statements and false claims.[103] Similarly, in *Beech Gap, Inc.,*[104] the board upheld a termination for default following the conviction of the contractor's employees for submission of falsified test reports and pay estimates. The board refused to consider the contractor's argument that the government had superior knowledge of the alleged false test reports and pay estimates as an effort to relitigate an issue unsuccessfully litigated in the prior criminal action and dismissed the contractor's appeal.

Even if government insists on contract performance after becoming aware of the prohibited conduct, that action by the government does not operate to ratify the underlying contract. For example, in *Schuepferling Gmbh & Co., KG,*[105] the contract was tainted by bribery. Even though the government insisted on and accepted further performance by the contractor, those actions did not negate the government's right to void the contract *ab initio* (from the outset).

2. Other Remedies

Four decisions issued in 2006 and 2007 demonstrate the other remedies available to the government and give an indication of the heightened agency and court awareness of fraud and false claims as related to construction projects. These decisions illustrate the variety of remedial approaches and the ways in which a court will employ several statutes and remedies to protect the government's interest in eliminating fraud from government contracting.

The first decision, although concerning commercial banking rather than construction or procurement, is extremely important due to its holding that any claim

[101]385 U.S. 138 (1966).
[102]*United States v. Mississippi Valley Generating Co.,* 364 U.S. 520 (1961).
[103]*See Brown v. United States,* 524 F.2d 693 (Ct. Cl. 1973).
[104]ENGBCA Nos. 5585 et al., 95-2 BCA ¶ 27,879.
[105]ASBCA No. 46564, 98-1 BCA ¶ 29,659.

under a contract that has been tainted by fraud is forfeited under the Forfeiture of Fraudulent Claims Act, 28 U.S.C. § 2514, even if the wrongdoing is not directly related to the contract performance. In *Long Island Savings Bank, FSB v. United States*, the Federal Circuit specifically invoked the holding in a 50-year-old Court of Claims decision that stated when a contractor practices fraud against the government, the court does not have the right to divide the valid claims from the claims related to the fraud.[106] Therefore, even if a contractor has valid claims unconnected to the fraud, those claims will be forfeited, in effect increasing the penalty assessed against the contractor. However, the forfeiture remedy is appropriate only where the contract has been tainted from its inception.[107] In such a case, the government would have to prove that the contract itself was obtained by the contractor by means of a false statement.[108]

In *Veridyne Corp. v. United States*,[109] the government asserted a counterclaim against the contractor on the theory that it had committed fraud by underpricing modifications to its contract. Otherwise, the contract would have been rebid because the contractor was on the verge of "graduating" from eligibility in a § 8(a) program administered by the Small Business Administration.[110] The government argued the contract should be found to be void *ab initio* (i.e., void from its very inception) and that money paid to the contractor under modifications to the contract should be forfeited and returned to the government because the act of fraud.[111] However, the court stated that for such a remedy to be imposed, the government would have to prove that a bribe took place or that there was a violation of the conflict of interest laws.[112] The discussion in *Veridyne* does not diminish the potential liability of the contractor or restrict the remedies available to a great extent. In that case, the court declined to enter summary judgment, stating that there were still issues of fact to be resolved regarding the conduct of the contractor and government and the consequences of that conduct.[113] The contractor should note, as illustrated in *Long Island* and *Veridyne*, that fraudulent conduct to obtain a contract will likely result in the very harsh treatment (potentially total forfeiture) whereas fraud that occurs later may still permit the contractor to retain some of the money it earned on the contract. However, other remedies or penalties may be imposed against the contractor.

In *Morse Diesel Int'l, Inc. d/b/a AMEC Constr. Mgmt., Inc. v. United States*,[114] the contractor was found liable under the False Claims Act as well as the Anti-Kickback Act. The conduct that formed the basis for the government's claims included billing for the full amount of bond premiums when there was a discount or rebate agreement

[106]476 F.3d 917, 925 (Fed. Cir. 2007) citing *Little v. United States*, 138 Ct.Cl. 773, 152 F.Supp. 84 (1957).
[107]*Id*. at 926.
[108]*Id.*
[109]83 Fed. Cl. 575 (2008).
[110]*Id.* at 576.
[111]*Id.* at 581.
[112]*Id.* at 586.
[113]*Id.* at 589.
[114]79 Fed. Cl. 116 (2007).

with the bonding company; providing invoices from the bonding company marked "Paid" when payments had not been made; advance billings by reallocating $5.4 million in subcontractor line items, which were allegedly billed but not paid to the trade contractors, which was a violation of the progress payment certification provided for under the contract. These actions provided the basis for liability under the FCA. In addition, the government showed that the contractor had received kickbacks ("rebates" on the bond premium) from bonding companies that were in violation of the Anti-Kickback Act. The contractor argued during the trial that imposing penalties under the Anti-Kickback Act and the False Claims Act was duplicative or prohibitive.[115] The court rejected this argument on the grounds that Congress intended both statutes to be used to compensate the government and to heighten the degree of deterrence for future fraudulent conduct on the part of contractors. In addition to the penalties assessed under the fraud statutes, Morse Diesel's claims under the contract, in excess of $50 million, were forfeited.[116]

The fourth decision, *Daewoo Engineering and Construction, Ltd. v. United States*,[117] demonstrates the manner in which a court may find a contractor liable under the False Claims Act as well as the anti-fraud provisions of the Contract Disputes Act. In *Daewoo*, the contractor initially submitted a proposal to build a road around an island in Palau. This initial proposal was approximately $28 million less than the next lowest offer. Even after resubmitting its price prior to award, Daewoo was $13 million less than the next lowest offer and was awarded the contract by the Army Corps of Engineers.[118] The project was intended to take 1080 days but quickly met with problems associated with the soil conditions and specifications for the road. Daewoo submitted a certified claim based on delay for approximately $64 million.[119] The government responded claiming that Daewoo had violated the Contract Disputes Act and the civil FCA.[120] The Court of Federal Claims found that Daewoo had committed fraud largely based on testimony by one of its employees that the claim he certified contained about $50 million in claims that had not been incurred and were included in order to get the government's attention.[121] As a result of this finding, the court determined that Daewoo was liable to the government in the amount of the overstated claim—in excess of $50 million. In addition, the court found that Daewoo was liable under the civil FCA. Under this statute, the court only assessed a $10,000 fine because it did not have the evidence to find that the government had been damaged.[122] In addition to penalties under these two statutes, the court ruled that Daewoo would have had to forfeit any valid claim under 28 U.S.C § 2514 if it had proven liability on the part of the government.[123] Also, the court found that Daewoo had

[115] *Id.* at 122.
[116] *Morse Diesel Int'l, Inc. d/b/a AMEC Constr. Mgmt., Inc. v. United States*, 74 Fed. Cl. 601 (2007).
[117] 73 Fed. Cl. 547 (2006) *aff'd* 557 F.3d 1332 (Fed. Cir. 2009).
[118] *Id.* at 550.
[119] *Id.* at 560.
[120] *Id.* at 581.
[121] *Id.* at 585.
[122] *Id.*
[123] *Id.* at 584.

committed fraud in the inducement by including in its bid statements that specific people and subcontractors would work on the project, although these people and companies never did, and also by submitting a schedule that it quickly abandoned and which the court doubted it had ever intended to keep.[124] The fraud in the inducement would have worked in conjunction with the forfeiture if Daewoo had been entitled to any recovery from the government.[125] The *Daewoo* case illustrates the wide range of theories that a court can employ in finding liability and imposing sanctions.

These recent cases are important illustrations of the wide range and severity of possible remedies if a contractor is found to have committed fraud against the government. The wide range of possibilities underscores the importance that a contractor ensures that it maintains the highest level of honesty and integrity in its dealings with the government.

E. Contractor Business Ethics and Conduct

1. FAR Requirements Applicable to Contractors

The FAR provisions detailing a contractor's obligations are found in FAR Subpart 3.10, Contractor Code of Business Ethics and Conduct; FAR Subpart 9.4, Debarment, Suspension and Ineligibility; and the implementing FAR clauses.[126] These provisions combine a *statement of expectations applicable* to all contractors; differing *mandatory requirements* depending on a company's size, the dollar value, and duration of a government contract; and *potential sanctions* applicable to *any contractor* if it fails to make certain required disclosures to the government. (*See* **Section IV.F** of this chapter.) The next sections provide an overview of these requirements and their potential effect on a government contractor.[127]

a. Contractor Standards of Conduct The FAR addresses contractor codes of business ethics and conduct with a combination of a statement of expectations applicable to any contractor and mandatory requirements that vary with the size of the contractor and the value and duration of the contract.

STATEMENT OF EXPECTATIONS

- All contractors "must conduct themselves" with the "highest degree of integrity and honesty."
- All contractors "should have" a written code of business ethics and conduct.
- As part of an effort to promote compliance with the written code, all contractors "should have" an employee business ethics and training program suitable for the

[124]*Id.* at 587.
[125]*Id.* at 588.
[126]FAR §§ 52.203-13; 52.203-14.
[127]For a more comprehensive review of the background for these requirements and guidance on implementing an effective compliance program, *see Federal Government Contractor Ethics and Compliance Programs, Toolkit and Guidance* (Thomas J. Kelleher, Jr. [Associated General Contractors of America, 2009]).

size of the company that will "facilitate discovery and disclosure of improper conduct" and "ensure corrective measures" are carried out.

- If the contractor is aware that the government has overpaid on a contract financing or invoice payment, the contractor is expected to remit the overpayment amount to the government. A contractor may be suspended and/or debarred for knowing failure by a principal to "timely" disclose "credible evidence" of a significant overpayment.

The FAR does not define either "timely" or "credible evidence" in the regulations or the related contract clauses. However, the commentary that accompanied these provisions indicated that "timely disclosure" depended on the date that the contractor had "credible evidence" of a violation or the date of the contract award, whichever was later.[128]

MANDATORY REQUIREMENTS

Any contractor receiving a government contract in excess of $5 million[129] and with a contract duration of 120 days or more ("Covered Contract") shall:

- Have a written code of business ethics and conduct.
- Make a copy of that code "available" to each employee engaged in the performance of a Covered Contract.
- Exercise "due diligence" to prevent and detect criminal conduct.
- Promote an organizational culture that "encourages" ethical conduct and a commitment to compliance with the law.
- Make a "timely" written disclosure to the agency Inspector General, with a copy to the contracting officer, whenever the contractor has "credible evidence" of a violation of the civil False Claims Act (31 U.S.C. §§ 3729– 3733), or of federal criminal law involving fraud, conflict of interest, bribery, or gratuity violations.

b. Contractor Awareness Programs and Internal Control Systems Except for small business concerns,[130] every contractor performing a Covered Contract must establish an ongoing business ethics and awareness program and an internal control system within 90 days of contract award.[131] The program shall include:

- Reasonable steps to communicate the contractor's compliance program standards and procedures.

[128]The FAR Councils stated that they adopted a "credible evidence" standard in lieu of "reasonable grounds to believe." The "credible evidence" standard is described as "a higher standard, implying that the contractor will have the opportunity to take some time for preliminary examination of the evidence to determine its credibility before deciding to disclose to the government. *See* 73 Fed. Reg. 667073. However, an opportunity to investigate seems to imply an obligation to investigate.

[129]FAR § 3.1004 authorizes agencies to reduce this monetary threshold.

[130]Based on the contractor's representation at the time of proposal or bid submission of its size in accordance with FAR Part 19, Small Business Programs, and 13 CFR Part 121. Commercial item suppliers are also excluded. *See* FAR § 52.203-13(c).

[131]Unless extended by the contracting officer.

- Effective training programs and dissemination of information appropriate to an employee's responsibilities and including training, "as appropriate," for the contractor's subcontractors.[132]

The internal control system shall:

- Establish procedures to facilitate timely discovery of improper conduct.
- Ensure corrective measures are promptly instituted and carried out.
- Assign responsibility for the internal control system at a "sufficiently high level" within the company and provide "adequate resources to ensure effectiveness" of the program and internal control system.
- Make reasonable efforts not to hire or engage as "principal"[133] of the contractor any person whom due diligence would have exposed as having engaged in conduct in conflict with the contractor's code of business ethics.
- Provide for periodic reviews to determine if the contractor's practices and procedures are in compliance with the contractor's code of business ethics and any special requirements of government contracting.
- Provide a monitoring and auditing process to detect criminal conduct.
- Make periodic evaluations of the effectiveness of the compliance program, particularly if criminal conduct has been discovered.
- Make periodic assessments of the risk of criminal conduct and modify the compliance program and internal control system to reduce that risk.
- Provide an internal reporting mechanism such as a hotline for employees to report improper conduct and instructions encouraging such reports.
- Provide for disciplinary action in the event of improper conduct or for failure to prevent or detect improper conduct.

When developing and implementing a business ethics and compliance program, contractors should expect that the Defense Contract Audit Agency (DCAA) will examine the contractor's compliance program during the course of an audit of a contractor's claim or proposal. Section 3 of Chapter 5 of DCAA's audit manual[134] states that the compliance program is an indicator of the "contractor's control environment" and provides detailed direction to auditors regarding the review of the contractor's compliance program for the purpose of assessing the effectiveness of the contractor's internal controls and risk of mischarging of costs to a contract.

[132]The FAR Councils did not further explain what is intended by the inclusion of subcontractors in the training requirement.

[133]FAR § 2.101 defines a "principal" as "an officer, director, owner, partner, or a person having primary management or supervisory responsibilities within a business entity (*e.g.*, general manager; plant manager; head of a subsidiary, division, or business segment; and similar positions)."

[134]*DCAA Contract Audit Manual* (*CAM*)2. Disclosure of Wrongdoing, Cooperation with Investigations, and Whistleblower Protection.

As noted above, the government now expects that a contractor will make a "timely disclosure" in writing to the agency Inspector General, with a copy to the contracting officer, whenever the contractor has "credible evidence" that a principal, employee, agent, or subcontractor of the contractor has committed a violation of the civil False Claims Act or a violation of federal criminal law involving fraud, conflict of interest, bribery, or gratuity violations in connection with the award, performance, or closeout of any government contract performed by that contractor or a subcontractor under that subcontract. The disclosure obligation related to a specific contract "continues until at least three years after final payment" on that contract.[135] Finally, the contractor is obligated to provide "full cooperation"[136] with any government agency responsible for audits, investigations, or corrective actions.

In addition to the requirements for disclosure and cooperation with the government, FAR Subpart 3.9, Whistleblower Protection for Contractor Employees, also addresses the potential for contractor efforts to discourage an employee from reporting perceived wrongdoing to the government. In addition to setting forth a detailed procedure in that subpart for investigating complaints about a contractor's alleged reprisal actions related to its employees, FAR § 3.903 policy provides:

> Government contractors shall not *discharge, demote or otherwise discriminate* against an employee as a reprisal for disclosing information to a Member of Congress, or an authorized official of an agency or of the Department of Justice, relating to a substantial violation of law related to a contract (including the competition for or negotiation of a contract). [Emphasis added.]

Consistent with that requirement, the FAR also expressly prohibits retaliation against an employee for making certain disclosures to the government. FAR § 3.907-2 policy details that prohibition:

> Non-Federal employers are prohibited from discharging, demoting, or otherwise discriminating against an employee as a reprisal for disclosing *covered information* to any of the following entities or their representatives:
>
> (1)The Board.[137]
> (2)An Inspector General.
> (3)The Comptroller General.
> (4)A member of Congress.

[135]These disclosure obligations are found in FAR § 3.1003(a)(2) and in two separate sections of FAR § 52.203-13. Subparagraph (b)(3) of FAR § 52.203-13 makes them applicable to all firms including small business concerns. Paragraph (c)(2)(F) restates them in the context of the elements of an internal control system. Therefore, even if a small business contractor is exempt from the requirement for an ethics awareness program and an internal control system, it *remains obligated* to comply with the disclosure provisions of FAR § 52.203-13. FAR § 3.1003(a)(2) states that any contractor's *"knowing"* failure to make a required disclosure provides grounds for suspension or debarment.

[136]"Full cooperation" is defined in FAR § 52.203-13(a).

[137]"Board" means the Recovery Accountability and Transparency Board established by Section 1521 of the American Reinvestment and Recovery Act of 2009 (ARRA). *See* **Chapter 17** for a review of ARRA.

(5)A State or Federal regulatory or law enforcement agency.
(6)A person with supervisory authority over the employee or such other person working for the employer who has the authority to investigate, discover, or terminate misconduct.
(7)A court or grand jury.
(8)The head of a Federal agency.[138]

"Covered information" is a defined term in that FAR Subpart. FAR § 3.907.1 defines that term in a rather broad manner:

> *Covered information* means information that the employee reasonably believes is evidence of gross mismanagement of the contract or subcontract related to covered funds, gross waste of covered funds, a substantial and specific danger to public health or safety related to the implementation or use of covered funds, an abuse of authority related to the implementation or use of covered funds, or a violation of law, rule, or regulation related to an agency contract (including the competition for or negotiation of a contract) awarded or issued relating to covered funds.

F. Contractor Self-Reporting/Hotline Requirements

1. Hotlines

Unless the contractor performing a Covered Contract has a business ethics and awareness program and an internal control system that includes a reporting mechanism with a company hotline and hotline posters, the contractor shall prominently display at all common work areas within business segments performing work on the contract and at the contract work sites any agency fraud hotline poster or the Department of Homeland Security fraud hotline poster as identified in the contract.[139] If the contractor uses a company Web site as a means of providing information to its employees, the contractor must also display an electronic version of the anti-fraud hotline posters on that Web site.

2. Self-Reporting of Potential Violations

A contractor must make a "timely disclosure" in writing to the agency Inspector General, with a copy to the contracting officer, whenever the contractor has "credible

[138]Emphasis added.
[139]See FAR § 52.203-14, Display of Hotline Poster(s). A small business concern under 13 CFR Part 121 that elects not to adopt a business ethics and awareness program and an internal control system must post agency hotline posters, such as the DOD Hotline poster.. In accordance with FAR § 3.1004, the Display of Hotline Poster(s) clause does *not* apply to contracts performed entirely outside of the United States or for commercial items. The requirement for company hotlines as set forth in FAR § 52.203-13 does apply to contracts performed entirely outside of the United States if the dollar and duration thresholds are met. The Federal Highway Administration at 23 CFR § 635.119 requires that the anti- fraud notices be posted on each federally funded highway project.

evidence" that a principal, employee, agent, or subcontractor of the contractor has committed a violation of the civil False Claims Act or a violation of federal criminal law involving fraud, conflict of interest, bribery or gratuity violations in connection with the award, performance, or closeout of any government contract performed by that contractor or a subcontractor thereunder. The disclosure obligation related to a specific contract "continues until at least three years after final payment" on that contract.[140] Finally, the contractor is obligated to provide "full cooperation"[141] with any government agency responsible for audits, investigations, or corrective actions.

3. Flow-down Requirements

Contractors are required to flow down these requirements to subcontracts in excess of $5 million and 120 days in duration. Contractors are to verify their subcontractors' compliance with these requirements.[142]

G. Potential Nondisclosure Sanctions: Suspension and Debarment

While the Contractor Code of Business Ethics and Conduct clause at FAR § 52.203-13 contains explicit requirements for certain contractor disclosures, that clause does not contain an express statement of the consequences if the contractor fails to provide a disclosure as specified by that clause. The sanctions are addressed in a revised version of FAR § 3.1003(a)(2) and (3)[143] and are included in the revisions to the statement of the grounds for contractor suspension or debarment found in FAR §§ 9.407-2 and 9-406-2, respectively. These two provisions set forth as grounds for suspension or debarment of any contractor:

- "Knowing failure" by a "principal" of the contractor to make a "timely" written disclosure to the government in connection with a government contract awarded to that contractor when the contractor has "credible evidence" of:
  - Violation of federal criminal law involving fraud, conflict of interest, bribery or gratuity violations.

[140]These disclosure obligations are found in FAR § 3.1003(a)(2) and in two separate sections of FAR § 52.203-13. Subparagraph (b)(3) of FAR § 52.203-13 makes them applicable to all firms including small business concerns. Paragraph (c)(2)(F) restates them in the context of the elements of an internal control system. Therefore, even if a small business contractor is exempt from the requirement for an ethics awareness program and an internal control system, it *remains obligated* to comply with the disclosure provisions of FAR § 52.203-13. FAR § 3.1003(a)(2) states that any contractor's *"knowing"* failure to make a required disclosure provides grounds for suspension or debarment.

[141]"Full cooperation" is defined in FAR § 52.203-13(a).

[142]The FAR Councils' commentary to the regulation expressly states that there is *no requirement* for a contractor to "review or approve" a subcontractor's ethics code, compliance program, or internal control system. *See* 73 Fed. Reg. 67084.

[143]FAR § 3.1003(a)(2) extends the mandatory disclosure obligations related to wrongdoing or overpayments and the related sanctions to *all contractors*, not just those subject to the requirements of the clause at FAR § 52.213-13.

  - Violation of the civil False Claims Act, (31 U.S.C. §§ 3729-3733).
  - "Significant overpayments" on the contract other than those resulting from contract financing as defined in FAR § 32.001.[144]
- The disclosure sanctions applies to any government contract in existence as of the effective date of the new suspension/debarment regulations and reach back to closed contracts for a period of three years following final payment on that contract (i.e., December 12, 2005).[145]
- The disclosure obligation relates to the award, performance, or closeout of the contract or a subcontract under that contract.

The apparent purpose for the placement of the sanction provisions in parts 3 and 9 of the FAR was disconnect the sanctions of debarment or suspension from the presence or absence of the Contractor Code of Business Ethics and Conduct clause in a particular contract. Consequently, even if the clause is not in the contract or if the contract is less than the $5 million-120-day thresholds, or if the firm qualifies as a small business, every contractor performing a government contract remains subject to the potential sanctions of debarment or suspension for a failure to make one of these disclosures.

H. Defense Contract Audit Agency Fraud Indicators

Contractors should be mindful of the possibility of being audited either by the DCAA or by an agency's internal auditing service. The DCAA performs audit services for all DOD contracts as well as the majority of contract audit services for all other federal agencies.[146] The DCAA publishes the *DCAA Contract Audit Manual* (*CAM*), which is the handbook for its auditors. The manual requires that "auditors should be familiar with specific fraud indicators" that are both listed in the *CAM* itself as well as a separate publication, *Handbook on Fraud Indicators for Contract Auditors.*[147] While the auditors are not responsible for proving fraud, they are required to find and report fraud indicators discovered during an audit to the appropriate law enforcement official. Additionally, if *qui tam* False Claims Act actions are filed against contractors, the Department of Justice attorneys often will seek information from DCAA audits to assist in the investigation of the claims.[148]

[144]FAR § 32.001 excludes payments made under the Payments under Fixed-Price Construction Contracts clause from this definition. An express requirement to notify the contracting officer of an overpayment on construction contracts is already set forth in FAR § 52.232-27(l). (*See also* FAR § 52.232-5(d) addressing refunds of "unearned amounts.")

[145]While these regulations are effective as of December 12, 2008, the FAR Councils expressed a clear intent that the sanctions for failure to make a disclosure apply to all existing contracts as of that date and to closed contracts up to three years following final payment. *See* 73 Fed. Reg. 67074.

[146]See *www.defense.gov/comptroller/defbudget/fy2007/budget_justification/pdfs/01_Operation_and_Maintenance/O_M_VOL_1_PARTS/DCAA.pdf* (accessed May 19, 2009).

[147]DCAA CAM 4-702.3147.DCAA CAM 4-709.

[148]DCAA CAM 4-709.

The *Handbook on Fraud Indicators* lists dozens of individual fraud indicators relating to labor, materials, and subcontractors among others. The type of contract and the work involved in performing the contract is central to determining which fraud indicators that an auditor will be especially on the lookout for. However, two main themes are apparent throughout the fraud indicators. First, the government has a major interest to protect in its procurement contracts, so auditors are instructed to investigate not just the government contracts that an individual contractor has been awarded but also the full scope of the contractor's operations including its business ethics and compliance program. For example, in evaluating patterns of labor costs, the *Handbook* contemplates that a DCAA auditor will gather information on the way labor is assigned to all of its contracts, both with the government and with private parties or internal divisions to determine whether the contractor is shifting labor costs to possibly defraud the government. The second theme is the highly subjective wording used in many of the fraud indicators. The indicators commonly contain words such as "significant," "weak," or "consistent" without defining how these words are to be used. The end result is that the auditor will use his or her own individual idea of what these indicators mean when deciding to refer the contractor to law enforcement.

➢ LESSONS LEARNED AND ISSUES TO CONSIDER

- Like private commercial contracts, government contracts are based on the concepts of an *exchange of promises* by the contracting parties and express and *implied obligations* binding on the parties.
- Construction projects are awarded by numerous agencies of the government. Each agency has a *unique organization* and mission. There are often key differences within the same agency from office to office.
- Similar to private work, construction for the government is a *people business,* and a contractor should gain an appreciation of the organization and operation of any agency for which it contemplates performing work.
- Government agencies maintain a *variety of Web sites* providing information on contracting opportunities, organization of a particular agency, and extensive online libraries listing standards and guides that often are incorporated into that agency's contracts by reference.
- Government construction contracts are replete with *jargon and acronyms*. These terms and abbreviations need to be understood by anyone doing business with a federal agency.
- While it is often stated that the United States submits to the same rules as private parties when it enters into a contract, there are important *exceptions* to that concept involving *authority* and fundamental *public policy* considerations.

(*Continued*)

- Federal government construction contract forms, policies, and procedures are devised from *multiple statutes* and a *comprehensive regulatory* system.
- Contractors must recognize that many key contract provisions are *incorporated by reference*. That practice by many government agencies does not diminish the significance of those provisions.
- To deter *fraud and false claims,* the federal government has available a broad spectrum of criminal and civil statutes that carry severe penalties for contractor wrongdoing.
- *Contractor certifications* are a key element of the government's effort to deter fraud and false claims. Such certifications should not be considered mere formalities.
- A growing trend in government contracting is a requirement that contractors employ programs encouraging employees to *report suspected fraud and wrongdoing.*
- Many key *resources* for government contractors are available on the Internet. Consistent with an effort to reduce reliance on paper, the federal government requires its contractors to report and post key information electronically.

APPENDIX 1A: BRIEF HISTORY OF THE DISPUTES PROCESS IN GOVERNMENT CONTRACTS

During World War I, the use of a board of contract appeals in the War Department became prevalent as the federal government sought to address issues arising out of the extraordinary increase in wartime procurement actions. Following that war, the use of boards to resolve contract claims diminished. However, with the increased volume of procurement during World War II, the nature of the boards and their practices became a concern to both industry and government procurement professionals. One decision, *Penker Construction Co. v. United States,*[149] highlighted the problems that could occur in the absence of established boards and fairly balanced rules of procedure. The saga of *Penker* was summarized by Joel F. Shedd Jr. in his excellent article, "Disputes and Appeals: The Armed Services Board of Contract Appeals."

> In *Penker* the contractor was refused permission to see the report on his claim that had been submitted by the constructing quartermaster, on the stated ground that it might be useful to him in prosecuting his claim against the government; and he was also told that no investigation would be made of the facts reported by the constructing quartermaster and that any doubts concerning interpretation of the specifications would be resolved in favor of the government. After congressional intervention, the Assistant Secretary of War told the contractor that he did not have time to hear appeals. The Assistant Secretary of War referred the appeal to a colonel, who referred it to a major, who referred it to a captain, who referred it back to the Quartermaster General, who referred it to the contracting officer, a brigadier general in his office, who referred it back to the captain who had prepared the contracting officer's decision from which the appeal has been taken. The Assistant Secretary of War's decision denying the appeal stated that he acted only in an administrative capacity, relying solely on the evidence and data presented to his office by the Office of the Quartermaster General. Under these facts, the Court of Claims held that the contractor had not received the kind of decision he was entitled to under the disputes clause and refused to accord any finality to such decision.[150]

The establishment of boards of contract appeals together with the further refinement of appeal rights to the United States Court of Claims resulted from the need to prevent the repetition of cases such as *Penker.* Following World War II, the contract claim disputes process essentially involved a three-step process. If the matter could not be resolved by agreement at the agency level, resolution required: (1) a decision by the contracting officer, (2) an appeal to the agency's board of contract appeals,

[149]96 Ct. Cl. 1 (1942).
[150]29 Law & Contemporary Problems at 50.

and (3) a limited right of appeal to the Court of Claims. A major problem with this process was that the boards were not authorized to decide "breach of contract" cases. This limitation on the board's jurisdiction precluded the resolution of "all disputes" at the board level because breach of contract claims had to be filed in the Court of Claims.

The modern disputes practices reflect the reforms and changes enacted with the Contract Disputes Act of 1978.[151] The details of the current process are set forth in **Chapter 15**. Many of the current procedures reflect an effort to address problems, enact reform, and provide a more efficient and credible process for all participants (federal government agencies and contractors).

Prior to the enactment of the CDA, the process for addressing contract disputes was a mixture of statutes, regulations. and interpretive case law. Federal government contracts contained a disputes clause, and every federal agency utilized a board of contract appeals. After a series of U.S. Supreme Court decisions,[152] the boards became the principal forum for the resolution of contractor claims, while the Court of Claims assumed the more limited role of an appellate court under the Wunderlich Act.[153] Except for the relatively unusual circumstance that could be characterized as a claim for breach of contract, nearly all claims arising under a contract had to be brought to the boards. However, the boards' jurisdiction was limited to "contract" claims, and any suit alleging breach of contract had to be filed in the Court of Claims.

Each agency board had its own rules and procedures, which had varying degrees of formality. In some agencies, board members or judges served only on a part-time basis. In those situations, the board judge often had other duties within the same agency that had awarded and administered the contract. In addition, due to the decision of the U.S. Supreme Court in *S&E Contractors, Inc. v. United States,*[154] the federal government had no right of appeal from an adverse decision by a board. The *S&E* decision also precluded efforts by an agency to obtain a review of an adverse board decision by the then General Accounting Office.[155]

Attempting to improve the overall disputes process, the CDA creates a comprehensive statutory basis for the disposition of contract disputes. The CDA applies to

[151]41 U.S.C. §§ 601-613.

[152]*United States v. Wunderlich,* 342 U.S. 98 (1951); *United States v. Moorman,* 338 U.S. 457 (1950); *United States v. Holpuch,* 328 U.S. 234 (1946).

[153]The reaction to the *Moorman* and *Wunderlich* decisions resulted in the passage of the Wunderlich Act, which limited the finality of board decisions. 41 U.S.C. §§ 321-322. This act was subsequently interpreted by the U.S. Supreme Court in *United States v. Bianchi,* 373 U.S. 709 (1963) and *United States v. Grace & Sons, Inc.,* 384 U.S. 424 (1966). *Bianchi* and *Grace* establish that a court reviewing a board decision was confined to the record created during the board proceeding and could not conduct an independent evidentiary hearing into issues not addressed by the board. Thus the boards became the primary fact-finding bodies, with significant emphasis placed on the development of a record that would support the board's findings with substantial evidence.

[154]406 U.S. 1 (1972).

[155]Now the Government Accountability Office.

any express or implied contract that is entered into by an "executive agency" of the federal government for the "procurement of [the] construction, alteration, repair, or maintenance of real property."[156] The act also applies to "the executive agency contracts for the procurement of property, other than real property, for the procurement of services and for the disposal of personal property, as well as for supplies.[157]

The term "executive agency" is defined in 41 U.S.C. § 601(2). It encompasses those entities that are commonly thought of as federal government agencies, such as the Department of Defense, the General Services Administration, the Department of Energy, the Department of Transportation, and the Department of Veterans Affairs. It also includes the U.S. Postal Service, the Postal Rate Commission, and various independent bodies and government corporations.[158]

The CDA's comprehensive statutory basis for resolution of disputes made significant changes to the old process. It makes the boards and their members more professional by requiring that all board members be full-time positions, and it is no longer possible for a board judge to function as an attorney for the agency on a part-time basis. Also, it gives the contractor a choice of a forum to appeal a contracting officer's final decision. Depending on the agency that awarded the contract, the contractor may elect to appeal to one of the two boards of contract appeals[159] or to file a suit on the contracting officer's final decision in the U.S. Court of Federal Claims (formerly the United States Claims Court). This concept is known as contractor's right of direct access. Furthermore, the CDA's provisions apply "notwithstanding any contract provision, regulation, or rules of law to the contrary."[160] As a result, it is not possible to agree by contract to limit the right of appeal to a particular forum.[161] In addition, the Act effectively reverses the *S&E* decision by giving the federal government the right to appeal an adverse board decision to the United States Court of Appeals for the Federal Circuit. Thus both parties are provided equal rights to appeal adverse board decisions.

[156]41 U.S.C. § 602(a).

[157]It is well established that the Contract Disputes Act applies to leases for real property. *See George Ungar,* PSBCA No. 935, 82-1 BCA ¶ 15,549; *Goodfellow Bros. Inc.,* AGBCA No. 80-189-3, 81-1 BCA ¶ 14,917; *Robert J. DiDomenico,* GSBCA No. 5539, 80-1 BCA ¶ 14,412. However, jurisdiction over a dispute outside of the terms of the lease, such as a decision to expand the area subject to the lease, has been rejected by a board. *See John Barrar & Marilyn Hunkler,* ENGBCA No. 5918, 92-3 BCA ¶ 25,074.

[158]The Act also contains provisions covering the Tennessee Valley Authority. *See* 41 U.S.C. § 602(b).

[159]Armed Services Board of Contract Appeals or the Civilian Board of Contract Appeals.

[160]41 U.S.C. § 609(b).

[161]*OSHCO-PAE-SOMC v. United States*, 16 Cl. Ct. 614 (1989).