

# Akerman Practice Update

CONSTRUCTION

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## Government Contractor Defense Protects Corps Dredging Contractors from Hurricane Katrina Claims

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On November 25, 2009, the United States Court of Appeals for the Fifth Circuit affirmed a District Court decision dismissing with prejudice two class action lawsuits filed against dredging contractors on behalf of Louisiana citizens who allegedly suffered property damage from Hurricane Katrina's floodwaters. The first suit was brought against the United States and thirty-two firms that had performed dredging work in the Mississippi River Gulf Outlet (MRGO) pursuant to contracts with the U.S. Army Corps of Engineers. The second suit was brought just against the same thirty-two contractors but not against the United States. The suits alleged that the dredging of the MRGO caused the destruction of wetlands, which had provided a natural barrier to hurricanes and severe storms. The suits alleged that this loss of a natural barrier contributed to the failure of levees in and around New Orleans following Hurricane Katrina. The suits asserted claims of negligence, breach of implied warranty, concealment and violations of the Water Pollution Control Act.

Several of the dredging contractors filed motions to dismiss based on government-contractor immunity. This immunity, also known as the government contractor defense, is a judicially-created doctrine used to shield government contractors from tort claims when performing under a government contract. The immunity is based on policy considerations and separation of powers, namely that courts generally should not review decisions made by the executive branch pursuant to authorizations by Congress that are carried out by private contractors.

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The District Court granted the dredging contractors’ motions to dismiss concluding that they were entitled to government-contractor immunity. The District Court denied requests by the plaintiffs to conduct discovery to determine whether the dredging contractors had done anything to place them outside the immunity. The District Court also denied a request by the plaintiffs to amend their complaints to allege that the contractors had violated various laws and regulations in an apparent attempt to plead around the immunity. The plaintiffs appealed.

On appeal, the plaintiffs argued that the District Court erred in applying government-contractor immunity to the defendants because such immunity requires the existence of an agency relationship between the contractor and government which the plaintiffs argued was not evident on the face of the pleadings. The plaintiffs’ argument was based upon dicta in the Supreme Court’s decision in *Yearsley v. W.A. Ross Constr. Co.*, 309 U.S. 18 (1940). The *Yearsley* case involved a claim against a contractor that had built dikes on the Missouri River pursuant to a federal contract. The plaintiffs in that suit contended that the dikes caused damage to their property. The Supreme Court concluded that the contractor was entitled to government-contractor immunity because the underlying project was authorized and directed by government officials pursuant to an Act of Congress.

The Fifth Circuit rejected the plaintiffs’ argument that the government-contractor immunity defense based on *Yearsley* requires that an agency relationship exist between the contractor and the government. The Circuit distinguished post-*Yearsley* decisions which seemingly included the requirement for an agency relationship by noting that these cases were product liability cases against military equipment manufacturers which were themselves subsequently distinguished from general *Yearsley*-based immunity by the Supreme Court in *Boyle v. United Technologies Corp.*, 487 U.S. 500 (1988). In *Boyle*, the Supreme Court articulated a three-part test for application of the government contractor defense to shield a defense contractor from state product liability law: (1) the United States approved a reasonably precise specification; (2) the equipment conformed to those specifications; and (3) the supplier warned the United States about dangers in the use of the equipment that were known to the supplier but not to the United States.

The Circuit found that public works contractors like the dredging contractor defendants need not show an agency relationship with the government to successfully assert *Yearsley*-based government-contractor immunity. The

Circuit noted that the facts in this action were virtually indistinguishable from the facts in *Yearsley* inasmuch as the MRGO was a project approved by Congress and carried out by the Corps just like the dikes at issue in *Yearsley*. The Circuit found that the plaintiffs' complaints largely attacked the MRGO project itself and did not contain any allegation that the dredging contractors exceeded their authority or deviated from Congress's directions or expectations. These allegations amounted to an attack on a Congressional policy and not any separate acts of negligence by the dredging contractors. The Circuit

found that the District Court did not abuse its discretion in denying the plaintiffs' request to conduct discovery to find potential acts of negligence. The Circuit also found that the District Court did not abuse its discretion in denying the plaintiffs' request to amend their complaints to allege the dredging contractors violated various statutes and regulations because the plaintiffs did not make such allegations with sufficient specificity.

The Fifth Circuit's decision in this Hurricane Katrina case is noteworthy on several levels. First, it was issued exactly one week after Judge Duval

issued his opinion in the Katrina Canal Breaches Consolidated Litigation that the Corps's failure to properly maintain and operate the MRGO was a substantial cause for certain levee failures. This presumably means the United States will likely stand alone defending these Katrina suits. For public works contractors, this decision highlights an important protection they enjoy when performing a government contract.

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## Identifying Stimulus-Funded Construction Opportunities

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“...less than 60 percent of the Recovery Act funds have been awarded and less than 15 percent of the funds have been disbursed.”

The American Recovery and Reinvestment Act of 2009 (Recovery Act) creates real opportunities for construction companies. Of the \$787 billion in spending and tax relief in the law, \$149 billion was designated for construction spending and \$98 billion was allotted to transportation and infrastructure projects. Except for broad guidelines favoring projects that can get underway quickly and create jobs, states and federal agencies have broad discretion in selecting projects. States and federal agencies are nevertheless required to advise Congress and the public of the specific projects that will be funded and to submit periodic reports summarizing their use of the funds. Since they are publicly available, contractors are able to use the agency reports to identify specific construction opportunities. As of December 2009, less than 60 percent of the Recovery Act funds have been awarded and less than 15 percent of the funds have been disbursed.

The Department of Defense (DoD) expenditure plan includes a 185-page report identifying construction projects valued at more than \$6 billion. The two largest projects are the construction of new hospitals at Fort Hood and Camp Pendleton, which together reflect estimated construction costs of more than \$1.3 billion. Other

major projects include the construction of child development centers, warrior-in-transition complexes, and military housing at bases around the country. The report indicates the anticipated date of contract award as well as dates contemplated for the start and finish of construction. Although government cost estimates have typically been withheld from public view before a contract is awarded, the DoD report also includes the estimated cost of each project.

The General Services Administration's (GSA's) stimulus expenditure plan identifies \$5.5 billion in spending. Of this amount, \$4.2 billion is targeted for implementing the Recovery Act requirement to convert existing government facilities to "high performance green buildings." As part of the green building effort, the GSA spending plans identify more than \$3.1 billion in full and partial building modernizations spread across more than 20 states. Major green-building renovation projects include the Herbert Hoover building (\$225 million) and 1800 F Street (\$161 million) in Washington, DC. Other major green-building renovation projects include the United Nations Plaza in San Francisco (\$121 million), the Rogers Federal Building in Denver (\$167 million), and the Leland Federal Building in Houston (\$109 million). Even for those buildings that are not scheduled for a major renovation, small scale energy efficiency improvements are planned. GSA plans to replace all seriously deteriorated roofs, for example, with new energy efficient roof membranes. A specific effort will be made to install photovoltaic solar roof membranes or planted roofs whenever possible.

**"As part of the green building effort, the GSA spending plans identify more than \$3.1 billion in full and partial building modernizations spread across more than 20 states."**

The Corps of Engineers' Civil Works Expenditure Plan identifies hundreds of planned construction projects throughout United States totaling approximately \$2 billion. The largest projects on the list include an \$84-million lock-and-dam project on the Monongahela River in Pennsylvania and a \$70-million lock-and-dam project on the Mississippi River in Minnesota. Most of the Corps's planned smaller projects appear on a separate 280-page list of operations-and-maintenance projects.

A significant portion of the funds appropriated by the Recovery Act are designated for grants to state and local governments. Of the \$49 billion allocated to construction spending by the states, \$27 billion is designated for highway construction. Highway construction funds are allocated to the states according to an existing formula that gives the most credits to states that already have the most federal-aid highways. California, Texas, Florida, and New York, for example, are

receiving the largest portion of highway construction funds. As with the federal construction spending, selecting specific projects is up to the individual states.

State and local governments receiving stimulus funds are required to publish reports identifying the projects funded by the Recovery Act and showing the use of stimulus funds over time. Many of these project lists have already been published and are accessible online. The District of Columbia, for example, received \$123.5 million for road and bridge projects. The DDOT project list includes not only a description of each of the planned projects, but also the amount of federal funds requested for the project, and the planned construction start date. Similar lists of stimulus-funded transportation projects have been published by other states.

The Recovery Act website, [www.recovery.gov](http://www.recovery.gov) is proving to be a useful central repository of information relating to the use of stimulus funds. Contractors can use the mandatory stimulus reports to identify construction opportunities requiring their specific skills and in their geographic area. The Recovery Act website already includes detailed plans prepared by the states and federal agencies describing their planned and actual use of stimulus funds. Although the form and content vary tremendously, state Recovery Act websites are accessible through [www.recovery.gov](http://www.recovery.gov).

Monitoring [www.FedBizOpps.gov](http://www.FedBizOpps.gov) for opportunities and announcements continues to be an important source of information about federal contract opportunities. Agencies publicizing

stimulus-funded projects are required to identify them as such when listing them in FedBizOpps. Recovery Act projects can be identified simply by checking the “Recovery Act” box on the search page or by using the term “recovery” in the title field. Indeed, given the broad new requirements for publication of contract opportunities and awards, contractors can expect announcements relating to stimulus-funded contracts to appear on FedBizOpps even when there will be no competition.

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## The Recovery Act “Buy American” Rule

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On March 31, 2009, the FAR Councils issued an interim rule amending the Federal Acquisition Regulation and implementing the Buy American provisions set forth in Section 1605 of the American Recovery and Reinvestment Act of 2009 (Recovery Act). These provisions require that iron, steel, and manufactured products used in Recovery-Act funded public projects be produced in the United States. On a finding of “urgent and compelling reasons,” the interim rule was issued without any opportunity for prior public comment. Despite a public comment period on the interim rule that concluded on June 1, 2009, no final rule has been issued and the interim rule remains in effect.

### Definitions and Differences between the Recovery Act’s Buy American Provision and the Buy American Act

The interim rule modified the FAR to add a new Subpart 25.6 entitled “American Recovery and Reinvestment Act—Buy American Act—Construction Materials,” along with corresponding Part 52 clauses. Section 25.601 provides a list of applicable definitions—many of which were crafted by the FAR Councils as a means of providing needed guidance on the meaning of vague terms included in the Recovery Act. Specifically, the interim rule provides a definition of “steel,” as well as of “manufactured,” “foreign,” and “domestic” construction materials. For iron and steel to be compliant, all of the manufacturing processes – except for the metallurgical processes involved in refinement of steel additives – must take place in the United States.

As a means of clarifying the most substantive difference between Section 1605 and the Buy American Act itself, the Recovery Act Buy American section notes that “[t]here is no requirement with regard to the origin of components or subcomponents in other manufactured construction material.” Thus, because the Recovery Act did not contain the Buy American Act’s requirement that construction materials be comprised substantially from articles, materials, or supplies mined, produced, or manufactured domestically, the interim rule’s definition of “domestic construction material” does not contain any requirements with respect to the origin of components.

The term “manufactured” is not clearly defined in the rule, but it appears to mimic the definition of “manufactured” as applied in the traditional Buy American Act which looks to whether the material comes to the construction site in a form assembled in the United States. Some readers of the rule have said that the goods must have been “substantially transformed” in the United States. On a FAR-covered federal project, unmanufactured construction material must also be

produced in the United States. For projects on the state and local level, there is no specific restriction on the source of “unmanufactured” material (i.e., raw materials).

### **The Impact of Trade Agreements on the Recovery Act’s Buy American Provision**

If a project is worth less than \$7.443 Million, then all of the construction materials (i.e., items delivered to the site for inclusion in the project), must be produced in the United States or its outlying areas (including U.S. territories). If the estimated value of the project is greater than \$7.443 Million, then the iron, steel, and other construction materials will be compliant with the law as long as the material delivered to the site for inclusion in the project was “substantially transformed” into a “new and different manufactured good from the materials from which it was formed” in the United States or another Recovery Act designated country with which the United States has an international agreement.

The countries with which the United States has international agreements and which are considered Recovery Act Designated Countries are:

- World Trade Organization (Government Procurement Agreement) Countries
- Free Trade Agreement Countries
- Least Developed Countries

Notably, construction materials from Mexico, Bahrain, and Oman may be used only for projects exceeding \$8.817 Million.

“On state and local projects, all iron, steel, and manufactured goods...must be manufactured in the U.S. unless the state is a signatory to an international agreement with the country for state procurements.”

### **State and Local Projects**

On state and local projects, all iron, steel, and manufactured goods (materials delivered to the site for inclusion in the project) must be manufactured in the U.S. unless the state is a signatory to an international agreement with the country for state procurements. Products from Canada and Mexico do not qualify for any state and local projects because no states are signatories to NAFTA and the states have excluded Canada from WTO application for state procurements. Thus, whether a contractor can use foreign material on a project will depend on the government-entity procuring the work.

For instance, in Florida, a project worth more than \$7.443 Million could use manufactured goods from any World Trade Organization (WTO-GPA) country (except Canada), Dominican Republic-CAFTA free trade agreement

country (Dominican Republic, Costa Rica, El Salvador, Nicaragua, Guatemala, and Honduras) or from Australia, Chile, Morocco, Peru, or Singapore. But Florida has excluded foreign construction grade steel from its obligations under the trade agreements. Therefore, a stimulus project over \$7.443 Million in Florida can use manufactured construction materials from the foreign countries listed above, but it can only use iron or steel made or produced in the United States.

In California, a project worth more than \$7.443 Million can use iron, steel, or manufactured goods from any WTO country (except Canada), Australia, Chile, or Singapore. In Virginia, a contractor would have to use all US-made iron, steel, or manufactured goods because Virginia has not agreed to make its state-level procurements subject to any free trade agreement.

### **Exceptions to the Recovery Act’s Buy American Provision**

In setting out the exceptions to applicability of the Recovery Act’s Buy American restrictions, the FAR provisions closely tracks the exceptions outlined in the Buy American Act itself. One exception, however, is that the Recovery Act requires publication in the Federal Register of the agency’s detailed written justification for making an exception to the applicability of Section 1605.

Finally, the remaining sections of the new Subpart 25.6 provide the procedures for determinations of inapplicability, evaluation of offers containing foreign construction material, and the consequences for

contractor noncompliance. Section 25.604 makes clear that determinations of inapplicability should be made pre-award. To make a pre-award determination based on claimed unreasonable cost of domestic construction material, the contracting officer is required to apply a 25 percent price adjustment factor for an offer using non-domestic iron, steel, or other foreign manufactured construction materials. This price adjustment factor is applied to the entire price of the project—not just to the cost of foreign materials. The contracting officer is also required to apply a 6 percent price adjustment factor to the cost of foreign unmanufactured construction materials before making a determination of inapplicability based on unreasonable cost. Once a determination of inapplicability is made, Section 25.605 provides the procedures for evaluation of bids offering foreign construction material. It requires application of the same 25 percent and 6 percent price evaluation factors discussed above, with a preference for offers using domestic construction material in the event two of more offers are equal in price. Section 25.606 discusses the circumstances upon which post-award determinations of inapplicability must be based, and Section 25.607 outlines the consequences of contractor noncompliance with Section 1605.

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As a whole, Section 1605 is slightly less cumbersome than the restrictions applicable under the Buy American Act itself. However, the differences between the Recovery Act rules and the typical Buy American provisions can prove confusing. In the context of state and local contract using Recovery Act funds, the sorting through application of the Recovery Act's Buy American requirement and its interaction with trade agreements can be a daunting task.

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## The Changing Legal Landscape on Federal Construction Projects

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A combination of Executive Orders and changes in the Federal Acquisition Regulation (FAR) have significantly shifted the legal obligations of contractors performing work on federal construction projects. These changes are accentuated by the

burst of federal construction projects associated with the American Recovery and Reinvestment Act of 2009 (Recovery Act). The following is a summary of some key Orders and changes.

### **Use of Project Labor Agreements on Federal Projects:**

President Obama signed Executive Order 13502 on February 6, 2009,

permitting federal agencies to require the use of Project Labor Agreements (PLAs) on federal construction projects. The Executive Order reverses a prohibition against PLAs adopted by the Bush Administration through prior Executive Orders. The Order is permissive and not mandatory, and only applies to projects where the total cost to the federal government is \$25 million or more.

If an agency chooses to employ a

“The Executive Order has provoked substantial reaction from labor and management groups. “

PLA, the Executive Order requires that the PLA:

- bind all contractors and subcontractors through appropriate bid specifications;
- contain guarantees against strikes, lockouts, or job disruptions;
- incorporate prompt and binding procedures for resolution of labor disputes; and
- permit contractors and subcontractors to compete for contracts, irrespective of whether they are parties to a collective bargaining agreement.

The National Labor Relations Act (NLRA) prohibits employers from entering into collective bargaining agreements with a labor union unless the union represents a majority of its employees. However, the NLRA’s “construction industry” proviso permits PLAs or “prehire agreements” for construction projects. Under this proviso, PLAs control the terms of employment, such as hiring, firing, wages, benefits, and hours of work. Indeed, by their terms, the PLAs apply to all contractors and subcontractors on the project irrespective of whether the particular contractor or subcontractor is a signatory to a collective bargaining agreement.

The Executive Order has provoked substantial reaction from labor and management groups. Labor organizations have supported the Executive Order, praising its goal of stability and efficiency in the execution of federal construction projects. Representatives of non-union groups such as Associated Builders & Contractors, Inc. (ABC), have criticized the Order as imposing a labor union monopoly on federal projects. The debate is accentuated by the Recovery Act, which is pouring billions of dollars into infrastructure and related construction projects.

The Federal Acquisition Regulatory Council (FAR Council) is charged with developing appropriate regulations to implement the Order. In addition, the terms of the Order require the Office of Management and Budget to recommend whether the Order should be expanded to include construction projects receiving federal financial assistance. The practical impact of the Order may in large part depend upon these regulations and recommendations. Nevertheless, the Order has the potential to substantially circumscribe the ability of non-union contractors to compete on federal construction contracts and independently control the terms and conditions of employment for their employees.

### **Notification of Employee Rights Under Federal Labor Laws**

Executive Order 13496, issued January 30, 2009, requires all government contracting departments and agencies (unless exempted) to incorporate mandatory provisions in their contracts requiring the contractor to post a notice regarding the rights of employees under the National Labor Relations Act.

Two features of the Order are significant. First, the Order requires that government contractors incorporate the mandatory provisions in subcontracts requiring the subcontractor to comply with the Order's requirements. Second, a government contract subject to the Order may be suspended, cancelled, or terminated for noncompliance with the requirements. Likewise, a noncompliant contractor may be deemed ineligible for further government contracts.

The Secretary of Labor is given principal responsibility for implementation of the Executive Order, including not only the size and content of the notices, but also the investigation of complaints regarding the violation of the Order's provisions.

### **Disallowance of Employer's Costs Incurred to Counter Union Organizing**

Executive Order 13494, issued as "Economy in Government Contracting," prohibits reimbursement of costs incurred by government contractors to counter union organizing efforts or collective

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bargaining activities. Such costs are deemed "unallowable" whether incurred with respect to the employees of the contractor or "any other entity." Examples of such costs include:

- costs for preparation and distribution of materials;
- legal or consulting costs; and
- costs of meetings held for such purposes.

The Executive Order seeks to preserve the allowability of costs for "maintaining" labor-management relations, provided such activities are not undertaken or directed to persuading employees against union organizing or collective bargaining efforts. This Order necessarily implicates cost accounting standards and sanctions associated with cost reimbursement under federal contracts.

### **Business Ethics and Fraud Provisions**

New FAR provisions add requirements for a written Code of

Business Ethics and Conduct, an internal control system and prompt disclosure of crimes, civil false claims and overpayments by the contractor, subcontractor or their principals. These FAR provisions implement the Close the Contractor Fraud Loophole Act, Public Law 110-252, Title VI, Chapter 1, enacted in 2008. The law also provides that the contractor's internal control system shall be established within 90 days after contract award, unless the contracting officer establishes a longer time period. The internal control system is not required for small businesses or for commercial item contracts. But it otherwise applies to construction contracts and subcontracts. These FAR provisions, in FAR clause 52.203-13, are to be included in all federal contracts over \$5 million with durations over 120 days.

The FAR provisions provide for the suspension or debarment of a contractor for up to three years for a knowing failure by a principal to timely disclose to the agency Office of the Inspector General, in writing with a copy to the contracting officer, certain violations of criminal law, violations of the civil False Claims Act, or significant overpayments. A principal is defined to include an owner, director, or manager.

The FAR provisions require that all contractors and subcontractors on contracts over \$5 million and 120 day-durations must have a written Code of Business Ethics and Conduct issued within 30 days of contract award and made available to all employees performing the contract.

They also require the contractor to promptly disclose to the government when “the Contractor has credible evidence that a principal, employee, agent, or subcontractor of the Contractor has committed” a crime involving fraud, conflict of interest or bribery or a violation of the civil False Claims Act (which prohibits the knowing submission of a false claim for payment).

For all but small business contractors and “commercial item contracts,” the new FAR provision requires that prime and subcontractors have, within 90 days of contract award, an ongoing business awareness and compliance program with an internal control system. This must include training of the contractor’s principals and employees about the company’s ethics program. The internal control system must promote discovery of improper conduct regarding government contracts, call for periodic reviews of company business practices for improvement, have a mechanism for reporting improper conduct, and provide for timely disclosure of improper conduct to the government.

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While a federal prime contractor may already have a business ethics program in place, a subcontractor may not have one. The prime contractor is responsible for flowing down these requirements to its subcontractors in subcontracts exceeding \$5 million and a 120-day duration. Prime contractors may need to work with subcontractors to help them become compliant with these new requirements.

## New Reporting Requirements for Recovery Act Funds

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Unique reporting rules imposed by the American Recovery and Reinvestment Act of 2009 (Recovery Act) require contractors to provide detailed information on the use of Recovery Act funds in an effort to promote transparency and accountability in the use of taxpayer dollars. Contractors who receive Recovery Act funds, in whole or in part, are required by the Recovery Act to provide a quarterly

report on the use of such funds, and have an obligation to provide the names and total compensation of the five most highly compensated officers for the calendar year in which the contract is awarded.

The reporting requirements apply to a broad base of contracts, including contracts for commercial items and commercially available off-the-shelf items, as well as to contracts under the simplified acquisition threshold. Reports from contractors for all work funded in whole or in part by the Recovery Act

prior to June 30, 2009 were initially required to be submitted no later than July 10, 2009. However, the initial reporting deadline was later moved to October 10, 2009. Thereafter, all reports must be submitted no later than the 10th day after the end of each calendar quarter. Reports can be submitted through an online tool via either a web browser, Excel spreadsheet, or other software system extract in XML format.

### Reporting Requirements

Some of the information that contractors are required to report under the Recovery Act includes: (1) the government contract and order number; (2) the amount of Recovery Act funds invoiced by the contractor for the reporting period; (3) a list of all

“The requirement to provide the names and total compensation of the five most highly compensated officers applies only where certain conditions are met.”

significant services performed or supplies delivered; (4) the program or project title; (5) a description of the overall purpose or expected outcomes or results of the contract, including but not limited to expected deliverables; (6) an assessment of the contractor's progress towards completion of the purpose and expected outcomes or results of the contract; (7) a narrative description of the employment impact of work funded by the recovery act; and (8) the names and total compensation of the five most highly paid officers of the contractor for the calendar year in which the contract was awarded. Similar requirements are imposed on subcontractors under limited circumstances.

The requirement to provide the names and total compensation of the five most highly compensated officers applies only where certain conditions are met. First, contractors must comply with the requirement if in the preceding fiscal year the contractor received (1) 80 percent of its revenue from federal contracts, loans, grants or cooperative grants; and (2) \$250,000 or more in annual gross revenues from federal contracts, loans, grants, and cooperative agreements. Compensation information of senior executives must also not be available to the public through periodic reports filed pursuant to Section 13(a) or 15(d) of the Securities and Exchange Act of 1934.

#### **Requirements on Contracting Officers:**

When allocating Recovery Act funds, contracting officers must indicate in the contract action that the contract action is being made under the Recovery Act and indicate which specific products and services are funded under the Recovery Act. Contracting officers must also include the appropriate reporting requirement contract clauses in all contract awards. To minimize the burden of different reporting requirements for Recovery Act funds and other government funds, contracting officers are empowered to issue separate contracts contemplating Recovery Act funds and other funds. Contracting officers are also charged with ensuring that contractors comply with the reporting requirements outlined above. If contractors fail to comply with reporting requirements, contracting officers are empowered to exercise appropriate contractual remedies.

The new reporting requirements place additional responsibilities on both contractors and contracting officers to provide information on the use of Recovery Act funds and promote transparency and accountability for contracts awarded under the Recovery Act. Contractors and subcontractors pursuing Recovery Act contracts should be aware of these requirements and be prepared to comply if they receive the work.

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## Stimulus Contractors & Old-Timers: Beware of the New Audit Clause

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“... businesses that receive contracts funded with appropriations from the American Recovery and Reinstatement Act of 2009 (Recovery Act) are subject to more expansive audits at the contractor and subcontractor levels.”

On March 31, 2009, the FAR Councils issued two interim rules to change the audit clauses found in federal contracts. Both rules expand the traditional Audit and Records Clause to allow the government to interview contractor employees involved in a “transaction” – an expansion from the right to review records. In addition, businesses that receive contracts funded with appropriations from the American Recovery and Reinstatement Act of 2009 (Recovery Act) are subject to more expansive audits at the contractor and subcontractor levels.

First, in October 2008, as part of the National Defense Authorization Act, Congress added the right to “interview any current employee regarding such transactions” to the powers of the Comptroller General under 10 U.S.C. § 2313(c)(1) and 41 U.S.C. § 254d(c)(1). On March 31, 2009, the FAR Councils issued an interim rule on an “urgent and compelling” basis to amend the audit clauses at FAR 52.214-26 and FAR 52.215-2 to allow the GAO to “interview any current employee regarding” the contract or subcontracts issued under the contract. In addition, FAR 12.603, regarding the laws that apply to commercial item transactions, is now amended to state that the new legislation expanding the GAO’s audit rights now applies. This change still does not change the portions of the Audit and Records clause providing the Contracting Officer and its authorized representative (usually DCAA) to examine costs or review cost or pricing data submissions. However, DCAA has also been pressing on access to contractor employees.

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Akerman is ranked among the top 100 law firms in the U.S. by *The National Law Journal NLJ 250* (2009) in number of lawyers and is the largest firm in Florida. With more than 500 lawyers and government affairs professionals, we serve clients from major business centers in Florida, New York, Washington, D.C., California, Virginia, Colorado, and Texas.

For more information, please contact a member of our Construction practice.

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