

# You Say You Aren't A Government Contractor — Or Is It Just Wishful Thinking?

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It happens all the time—we find in due diligence for an acquisition, in the investigation of a violation, or just in conversation—clients who have been insisting vociferously that they don't have any obligations to comply with government contract regulations, actually do. Some common reasons organizations claim they are exempt from compliance measures are:

- We have no direct contracts with any governmental customer.
- We only sell commercial-off-the-shelf (“COTS”) products.
- We sell in large lots to wholesalers, so it is impossible to trace any of our products to a government contract.
- We are a small business and we are the fifth company down in the supply chain.

For some government contract compliance requirements, these facts do make a difference and will insulate the organization. For others, however, they do not. Over the last two years, the emphasis on compliance and enforcement of laws and regulations that had, for at least a decade, largely only been enforced through whistleblower complaints, has swelled immensely. In fact, over these last two years that have brought an increased number of compliance reviews and audits, federal agencies have been hiring thousands of new employees to perform audits, investigations, and

bring enforcement actions against contractors. Now, more than ever before, is the time to assess your status as an organization and face the reality that you may, in fact, fall under the umbrella of the laws and regulations governing contractors and subcontractors providing goods or services to the government.

In assisting you with this assessment, review the threshold compliance issues below and decide whether any of the issues may apply to your organization.

The most stringent and invasive requirements impact the human resources department of any organization that may be considered a government contractor or subcontractor.

## Equal Opportunity Employment

The equal opportunity requirements of Executive Order 11246, also found in the Federal Acquisition Regulation (“FAR”) clause 52.222-26 and 41 C.F.R. Part 60-1, apply to every subcontractor, at any tier, that has received \$10,000 or more in federal contracts or subcontracts in the last twelve months. Contractors and subcontractors must submit required reports and conduct hiring and promotions in accordance with the requirements set forth in these regulations. Executive Order 11246 and its implementing regulations prohibit nonexempt government contractors and subcontractors from discriminating on the basis of race, color, religion, sex, or national origin and also require statements in employment advertisements conveying the notion that applicants will be considered without regard to race, color, religion, sex, or national origin.

Organizations are subcontractors if the products or services they perform are included in the scope of work for the prime contract. This is true regardless of whether the subcontractor is aware that its products or services are within the scope

of work. For example, in a large construction project, the doorknob supplier may be considered a low level COTS supplier, but because doorknobs are required in the building, the doorknob supplier is a government subcontractor for compliance purposes. Thus, regardless of the supplier's belief of its status as a government subcontractor, the supplier is, in fact, a government subcontractor and must comply with the regulations relating to equal opportunity employment. The equal opportunity requirements apply to work performance and hiring activities in the United States.

## Affirmative Action

The affirmative action requirements contained in Executive Order 11246, also found in the Federal Acquisition Regulation ("FAR") clause 52.222-26 and 41 C.F.R. Part 60-1, apply to every subcontractor, at any tier, that has received \$50,000 or more in federal contracts or subcontracts in the last twelve months. If an organization's actions are within the scope of the affirmative action regulations, it must comply with the three main affirmative action requirements including: maintaining a written affirmative action plan; posting notices; and collecting and reporting employment data.

Generally, an organization must establish affirmative action plans if it has at least \$50,000 in government contracts or subcontracts and there are 50 or more employees. Affirmative action regulations apply to work performance and hiring activities in the United States.

There are separate affirmative action requirements for workers with disabilities<sup>1</sup> and veterans.<sup>2</sup> The requirements for disabled workers apply to subcontracts exceeding \$15,000 and requirements for veterans apply to subcontracts exceeding \$100,000.

Just as with the Equal Opportunity Employment regime, even when the requirement has not been expressly included in a subcontract, the Department of Labor has held employers responsible for failing to implement affirmative

action obligations, reasoning that the organization should be able to tell when it is supporting a government contract.<sup>3</sup> Possible penalties imposed by the Department of Labor for failure to comply include suspension and debarment from government contracts, grants, loans and related federal programs. State and local governments and many very large corporations will also refuse to do business with an organization that is on the federal government list of suspended or debarred entities, which is why federal suspension or debarment are considered "death sentences" for organizations.

## Employment Eligibility Verification

The employment eligibility verification, or E-Verify requirements apply to first tier subcontractors that have services and construction subcontracts with a value of at least \$3,000. E-Verify requirements apply to work performance and hiring activities in the United States. The Immigration and Customs Enforcement branch of the Department of Homeland Security has dramatically increased its administrative enforcement actions against government contractors that have knowingly hired or harbored illegal aliens and has commenced suspension and debarment actions against violators.

## More

The compliance requirements listed above highlight just a few examples of regulations that are applicable in almost every government subcontract and that have caused extensive disruption when an organization suddenly discovers they are germane to operation and must be obeyed. Additional compliance obligations are also likely to apply when an organization operates as a subcontractor to the government. These requirements include a code

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<sup>1</sup> FAR 52.222-36 and 41 C.F.R. § 60-741.5.

<sup>2</sup> FAR 52.222-37 and 41 C.F.R. § 60-250.40.

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<sup>3</sup> See e.g., *In the Matter of Office of Federal Contract Compliance Programs, United States Dept. of Labor v. Fl. Hosp. of Orlando*, 2009-OFC-00002 (Oct. 2010) (an organization is responsible for complying with affirmative action regulations, even when it does not know it is considered a subcontractor to the government, when the organization is "performing [or] assuming or undertaking" of another company's prime contract to provide goods or services to the government.).

of business conduct and ethics, along with training and internal controls; domestic preference requirements; regulations requiring minimum wages by labor category and minimum benefits; plans to provide small businesses subcontracting opportunities; and identification of intellectual property rights, marking requirements, and licenses to the government.

## The Ever-Changing Regulatory World

New regulations are constantly being drafted, proposed and adopted as final,<sup>4</sup> and old regulations are revised. Adoption of new regulations and changing old ones can play a significant role in operational planning. Alterations in the regulatory scheme may bring an organization that was previously not affected by the compliance requirements, into the sphere of government contract regulations, burdening the organization with previously unknown requirements such as implementing certain procedures, gathering certain data, reporting that data, and record retention.

## Penalties For Non-Compliance

The risks of failing to comply with rules and regulations are substantial. As stated above, whether the organization believes it is a government contractor has no bearing on the

penalties imposed for failing to comply with regulations. All entities that do business with the government can expect their compliance program to be tested by auditors, investigators, competitors, or whistleblowers.

If, as the result of an audit, the Department of Labor or any other regulatory body finds that an organization is not in compliance with rules and regulations, substantial penalties can be imposed. For example, the organization runs the risk of having its contracts terminated, receiving a government claim for repayment or penalties, extensive and invasive civil or criminal investigations, or suspension or debarment from government contracting, grants, loans and other federal government programs.

## Conclusion

An organization can no longer afford to play the ostrich and put its head in the sand and hope the government never notices its role in government contracting. If your organization meets any of the criteria discussed above, you are a subcontractor and it is time to spend an adequate amount of time and resources to meet regulatory requirements rather than spending the time and resources in defending against draining government investigations.

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<sup>4</sup> See e.g., Executive Order 13496, Notification of Employee Rights Under Federal Labor Laws, January 30, 2009.

