

Client Alert

Reporting Requirements For Executive Compensation And First-Tier Subcontract Awards

July 9, 2010

On July 8, 2010, the Civilian Agency Acquisition Council and Defense Acquisition Regulations Council issued an interim rule, requiring that, subject to several exceptions and limitations, contractors report executive compensation, first-tier subcontract awards, and executive compensation information for first-tier subcontractors. The government will make this information public via the USASpending.gov website.

The interim rule revises the FAR Subpart 4.14, and changes it from "Reporting Subcontract Awards" to "Reporting Executive Compensation and First-Tier Subcontract Awards." Under the revised Subpart 4.14, all solicitations and contracts of \$25,000 or more, except classified solicitations and contracts and solicitations and contracts with individuals, must contain a new clause, 52.204-10.

Contracting officers must modify existing ID/IQ contracts, including FSS contracts and GWACs, on a bilateral basis to include the clause for future orders, if the value is \$25,000 or more, except classified contracts and contracts with individuals.

The interim rule applies to all businesses, regardless of size or ownership (*e.g.*, large, small, disadvantaged, veteran-owned, women-owned, HUBZone, etc.), and is specifically made applicable to contracts for "commercial items," contracts for "commercial off the shelf" or "COTS" items, and to contracts at or below the simplified acquisition threshold (provided the contract value is at least \$25,000).

As illustrated below, the reporting requirements are essentially the same as those applied to recipients of American Recovery and Reinvestment Act ("ARRA") funds. Thus, those contractors who have been subject to ARRA reporting will recognize these reporting requirements and will likely have processes in place to collect and report the information required by this interim rule. However, those contractors who have not been subject to ARRA reporting will need to take steps to ensure compliance with the reporting obligations.

Reporting Requirements: Executive Compensation Information For Prime Contractor

Pursuant to Subpart 4.14 and contract clause 52.204-10, contractors must report the following information.

By the end of the month following the award of a contract, and annually thereafter, the contractor shall report via the Central Contractor Registration ("CCR") the names and total compensation of each of the five most highly compensated executives for the contractor's preceding completed fiscal year if, in the contractor's preceding fiscal year, the contractor received:

- 80 percent or more of the contractor's annual gross revenues from Federal contracts (and subcontracts), loans, grants (and subgrants) and cooperative agreements; and
- \$25,000,000 or more in annual gross revenues from Federal contracts (and subcontracts), loans, grants (and subgrants) and cooperative agreements; and
- The public does not have access to information about the compensation of the executives through periodic reports filed under section 13(a) or 15(d) of the Securities Exchange Act of 1934 (15 U.S.C. 78m(a), 78o(d)) or section 6104 of the Internal Revenue Code of 1986. (To determine if the public has access to the compensation information, see the U.S. Security and Exchange Commission total compensation filings at <http://www.sec.gov/answers/execomp.htm>.)

"Executive" is broadly defined as officers, managing partners, and any other employees in management positions. However, the definition does not seem to require the disclosure of compensation information for a partner or shareholder that does not exercise management authority.

"Total compensation" means the cash and noncash dollar value earned by the executive during the contractor's past fiscal year, including salary and bonus, awards of stock, stock options, and stock appreciation rights, earning for services under non-equity incentive plans, changes in pension value, above-market earning on deferred compensation which is not tax-qualified, and other compensation, including severance, termination payments, value of life insurance paid on behalf of the employee, perquisites or property, if the aggregate value of the other compensation for the executive exceeds \$10,000.

Depending on how they are interpreted, the compensation reporting requirements may impose no new burdens on publicly traded companies, but they will require closely-held companies, non-profit organizations, and others to report details about executive compensation that have previously been confidential (unless reported due to receipt of ARRA funding).

One likely area of confusion is the requirement that "the Contractor" report compensation for its five most highly compensated executives. Given the cross-reference to the SEC reporting requirements, one might think that "the Contractor" means the legal entity that is required to file reports under the SEC rules and not every wholly-owned subsidiary that may happen to be the recipient of an individual contract. However, the CCR reference (see p. 27) to "the legal entity to which the specific CCR record, represented by a DUNS number, belongs" indicates that the reporting requirement most likely applies to each entity in receipt of a qualifying federal award. In some cases, calculation of the amount of compensation other than cash payments may be difficult and should be done carefully to avoid unintended consequences with respect to tax matters.

Reporting Requirements: Executive Compensation For First-Tier Subcontractors

Pursuant to Subpart 4.14 and contract clause 52.204-10, contractors must report the following information.

By the end of the month following the month of award of any first-tier subcontract with a value of \$25,000 or more, the contractor shall provide information about the executive compensation at its first-tier subcontractors. In particular, the contractor must provide names and total compensation of each of the five

most highly compensated executives for the subcontractor's preceding completed fiscal year if, in the subcontractor's preceding fiscal year, the subcontractor received:

- 80 percent or more of the subcontractor's annual gross revenues from Federal contracts (and subcontracts), loans, grants (and subgrants) and cooperative agreements; and
- \$25,000,000 or more in annual gross revenues from Federal contracts (and subcontracts), loans, grants (and subgrants) and cooperative agreements; and
- The public does not have access to information about the compensation of the executives through periodic reports filed under section 13(a) or 15(d) of the Securities Exchange Act of 1934 (15 U.S.C. 78m(a), 78o(d)) or section 6104 of the Internal Revenue Code of 1986.

In this context, "first-tier subcontract" means "a subcontract awarded directly by a Contractor to furnish supplies or services (including construction) for performance of a prime contract, but excludes supplier agreements with vendors, such as long-term arrangements for materials or supplies that would normally be applied to a Contractor's general and administrative expenses or indirect cost."

Reporting Requirements: Information About First-Tier Subcontract Awards

Pursuant to Subpart 4.14 and contract clause 52.204-10, contractors must report the following information.

By the end of the month following the month of award of any first-tier subcontract (following the same definition as set forth above) with a value of \$25,000 or more, the contractor shall provide information about these awards via the Federal Funding Accountability and Transparency Act Subaward Reporting System.

The contractor must provide the following information for each first-tier subcontract (and any modifications made to that subcontract if they change information previously provided):

- Unique identifier (DUNS Number) for the subcontractor receiving the award and for the subcontractor's parent company (if any)
- Name of the subcontractor
- Amount of the subcontract award
- Date of the subcontract award
- Description of the products or services (including construction) being provided under the subcontract, including the overall purpose and expected outcomes or results of the subcontract
- Subcontract number (the subcontract number assigned by the prime contractor)
- Subcontractor's physical address including the street address, city, state, county, nine-digit zip code and congressional district
- Subcontractor's primary performance location including the street address, city, state, county, nine-digit zip code and congressional district
- Prime contract number, and order number (if any)
- Awarding agency and code

- Funding agency and code
- Government contracting office code
- Treasury account symbol (TAS) as reported in the Federal Procurement Data System
- Applicable North American Industry Classification System (NAICS) code

There are three important exceptions to the subcontractor award reporting requirements. First, if a contractor in the previous tax year had gross income from all sources under \$300,000, then the contractor does not have to report any subcontractor awards. Second, if a subcontractor in the previous tax year had gross income from all sources under \$300,000, the prime contractor does not need to report awards to that subcontractor.

Third, the reporting requirements about first-tier subcontracts is being phased-in.

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

As the interim rule is written, it appears that these three exceptions relate only to reporting of subcontractor awards, but have no bearing on the reporting of executive compensation for first-tier subcontractors. However, the originating statutory language indicates the exceptions apply equally to the reporting of executive compensation for first-tier subcontractors and from a practical standpoint, it is difficult to understand why a contractor should be required to obtain, and a subcontractor to disclose, compensation information when a report of the subcontract award itself is not necessary.

Failure To Comply

Contracting officers must exercise "appropriate contractual remedies" if a contractor fails to comply with reporting requirements for. Section 4.1402 also requires contracting officers to make the contractor's failure to comply with these reporting requirements a part of the contractor's performance information. Furthermore, improperly certifying compliance with reporting requirements may subject contractors to False Claims Act liability and the CCR section pertaining to executive compensation warns that "Knowingly providing false or misleading information may result in criminal or civil penalties as per Title 18 Section 1001 of the US Criminal Code."

Comments Due 60 Days After Publication

Comments on the revised Subpart 4.14 must be submitted before September 7, 2010. Given the broad reach of the interim rule and the questions raised by the rule, submission of comments would be well worth consideration.

For more information, please contact the professional(s) listed below, or your regular Crowell & Moring contact.

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