



## Internal Confidentiality Agreements

*By Michael Steen, CPA, Senior Director at Redstone Government Consulting, Inc.*

Although it remains a proposed rule, Federal Acquisition Register: Contractor Employee Confidentiality Agreements (Federal Register, January 22, 2016) will likely prohibit government agencies from contracting with a company which requires employees or subcontractors to sign a confidentiality agreement that restricts such employees or subcontractors from lawfully reporting waste, fraud or abuse to a designated Government representative. The fact is that the proposed rule is a requirement from a 2015 Appropriations Act; hence, only “proposed” in the context of the rule making process and to sort out the particulars.

The proposed FAR rule is hardly unique, notably both the SEC and the EEOC already have rules or interpretations which prohibit certain employer-employee confidentiality agreements. In 2015, the SEC announced its first enforcement action directed at a corporation whose employment policy “could” illegally stifle whistleblowing (Rule 21F-17 under the 2010 Dodd-Frank Act). Although the SEC didn’t identify any situation where the confidentiality agreement had actually stopped an employee from “whistleblowing”; the fact that it “could stifle” reporting was enough for the SEC to pursue remediation. While not acknowledging any wrong-doing, the company “voluntarily” revised its confidentiality agreement to clearly indicate that nothing prohibits an employee from reporting possible violations of federal law or regulation to a government agency, including but not limited to the Department of Justice, the SEC, Agency Inspector Generals (IGs) or other disclosures that are protected under the whistleblower provisions of federal law or regulation.

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Regarding the EEOC, they've made it clear that similar employee non-disclosure or confidentiality agreements cannot prohibit an employee from contacting the EEOC, making it an issue that a severance payment (or risk of having to forfeit a severance payment) cannot be linked to a non-disclosure agreement. Although the severance agreement (at issue) did permit the employee (or ex-employee) to cooperate should there be an EEOC review or investigation; the EEOC insisted that the employee must not be constrained from filing an initial complaint (reference: 2013 EEOC vs. Baker & Taylor where the EEOC alleged that the confidentiality provision of the severance agreement violated Title VII).

"The EEOC Title VII enforcement actions, including settlements/payments wherein the company admits to no wrongdoing (but does make a payment and does agree to modify policies and practices) raises the question of cost allowability under FAR Part 31. Nothing in FAR expressly states that the severance payment is unallowable and coincidentally the issue of cost allowability was the focus of a mid-1990s DCAA audit policy which initially asserted that severance payments linked to non-disclosure agreements were unallowable backpay. At the time, DDP (Director of Defense Procurement) compelled DCAA to rescind its initial audit policy; which was then reissued wherein DCAA changed its reasoning that such severance payments might be unreasonable (FAR 31.201-3). Then and now, if cost reasonableness is the issue, the contractor is placed in the precarious position of proving that the cost is reasonable.

Noting that the January 22, 2016 proposed rule does not make costs unallowable, it only prohibits the government from contracting with a contractor with a non-disclosure agreement. Hence, a contractor with existing contracts may choose to retain certain non-disclosure agreements which risk new contract awards, but don't render the costs unallowable on existing contracts (by implication, a decision to exit government contracting). Regardless, given the multi-front attacks on employee non-disclosure agreements (as a conditions of employment and/or linked to a severance payment), it is safe to conclude that retaining such provisions is inviting unwanted attention from EEOC, SEC, OFCCP, or other federal agencies.

## Contractor Settlement on 401K Management Allowable or Unallowable Costs

*By Michael E. Steen, CPA, Senior Director at Redstone Government Consulting, Inc.*

Recently, a number of media sources reported that a government contractor paid \$62 million to settle a 401K lawsuit. Per the settlement, it covered 108,000 employees or ex-employees who will be compensated for i) excessive administrative fees which reduced overall returns and ii) concealing overly-conservative investments within the stable funds (by definition, conservative, low-risk investments, but apparently too conservative). In settling, the government contractor denied any wrong-doing, but settled through mediation to avoid the cost of additional litigation along with the litigative risk of a costlier settlement (the trial would have been in the federal court, East St. Louis, Illinois). Not that it matters, but the attorneys filing the class action lawsuit maybe paid up to \$20.67 million, whereas the individuals who allegedly suffered poor 401K investment returns will (on average) receive less than \$400 each.

Noting that these costs are being incurred by a government contractor, the test question, are they allowable on cost type contracts which invoked FAR Part 31? The answer, it depends upon who you ask. FAR 31.205-47 does define allowable and unallowable legal costs; however, with few exceptions, nothing specific to a third party lawsuit and certainly nothing specific to a third-party lawsuit alleging mismanagement of employee 401K investments. However, there is reasonableness (FAR 31.201-3) whose criteria includes incurring a cost in an amount which would be incurred by a prudent business person in a competitive (commercial) marketplace. In that context, was it prudent to incur legal costs (undisclosed) and a \$62 million settlement to avoid more legal costs and an indeterminable amount of settlement costs (could have been higher or could have been zero)? Is reasonableness a function of the alleged mismanagement which then lead to the legal costs and settlement costs? Is reasonableness an issue because FAR 31.201-3(b)(3) mentions reasonableness in the context of a contractor's responsibilities to its employees?



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We may never know the answer because the contractor may take the conservative approach and voluntarily disallow the \$62 million plus its legal costs ("voluntarily" because the costs are not expressly unallowable and may in fact be allowable). Lastly, what may seem to be an issue unique to a particular contractor, is unlikely to be limited to that contractor given that the law firm (representing the 108,000 persons in the class action lawsuit) has made it known that they will be pursuing similar opportunities where large numbers of employees are covered by a 401K plan which is managed (directly or indirectly) by the employer.

## Contractor Entitlement to Costs After Contract Performance

*By Michael E. Steen, CPA, Senior Director at Redstone Government Consulting, Inc.*

A recent CBCA (Civilian Board of Contract Appeals) decision may have opened the door for contractors to claim and to recover costs which continue after contract performance or in the particular CBCA case (CBCA 3407), after partial termination (May 18, 2011) of the contract. In the CBCA case, a subcontractor (whose statement of work was fully terminated) notified the prime, who in turn notified the ACO or TCO that the subcontractor would retain employees needed to support government audits (incurred costs as well as the termination settlement proposal). In September 2011, the contracting agency began the audit of subcontractor incurred cost proposals for 2008-2010 and for two years the subcontractor responded to more than thirty auditor requests for information. Unfortunately, the agency auditors never knew about the termination; hence, none of their audits covered the termination settlement costs (editors' comment: it is inconceivable that the agency auditors had not been made aware of the termination which would have been the impetus initiating the audit request).

As the process evolved, the prime contractor submitted interim requests for payment; ultimately two requests were denied based primarily on the ACO contention that post-termination costs in support of the agency audits are not allowable. This denial led to a certified subcontractor claim of \$997,651 which was then the subject of the CBCA hearing and decision. In particular, the appellant (subcontractor) stated:

Had the government agency audited and settled the open contract years or negotiated the termination settlement proposal in a timely manner, we (subcontractor) could have placed all of the audited records in permanent storage and discontinued operations. However, the government agency did not do either of these things. Instead, the government agency required us to undergo a protracted audit. As a consequence, we were compelled to continue to incur costs in order to close out the subcontract in accordance with the requirements of FAR 52.216-7.

The CBCA decided for the appellant (subcontractor), but only on entitlement. Now the parties must attempt to settle on quantum which may or may not cause the action to revert to the CBCA. Although the CBCA decision was triggered by a termination, the implications go far beyond contract termination given that the fundamental issue is costs continuing after contract performance. A significant victory for government contractors because it may lead to the recovery of costs which are required by the administrative clauses of the contract; specifically, FAR 52.216-7 which requires the annual final indirect cost rate proposal, the audit, final rate negotiations/agreement, prime contractor settlement of subcontractor costs and ultimately contract close-out. In many cases, these costs are buried in continuing operations (i.e. embedded in current G&A expenses albeit related to prior period contracts); hence, a non-issue for a government contractor with current cost-type contracts which provide for at least some cost recovery. Not the case for a contractor who is no longer an active contractor and/or who no longer continues to perform on cost type contracts. In fact, a reminder, that administrative functions, actions and costs related to prior periods or prior contracts are not truly a G&A function. These are requirements which are unique to certain government contract types; hence, neither caused by or benefiting other contracts (fixed price or commercial).

Lastly, and perhaps sadly, a statement concerning the government's inability to do its part to timely administer and close contracts. The government agency was compelled to attempt to perform its own audits of certain incurred cost years because DCAA was missing in action (essentially stopped performing incurred cost audits in 2009-2011). The government agency was incapable of timely completing the audits and was completely oblivious to the requirement to audit the termination settlement costs. The subcontractor was contractually compelled to maintain the capability to support



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the audits (even if the prime contractor was primarily responsible for reviewing or auditing the subcontractor termination proposal, the fact is that the government auditors were already at the subcontractor and it should have been more efficient for the government auditors to add the termination costs to their other audits); inexplicably, the government agency asserted that it was unreasonable for the subcontractor to claim these continuing subcontract costs. The case is one clear example of the most ubiquitous problem in government procurement and acquisition management, the inability to timely plan and execute contract award or contract administration. Although it does not directly pertain to the CBCA issue, this problem is at the heart of a 2017 NDAA (National Defense Authorization Act) section to grant the government and the government contractor a waiver from regulatory requirements for contract(s) close-out. In this case, Section 811, which will allow the Navy to close out \$9.96 billion in submarine contracts that were physically performed from 1974-1998. With respect to timeliness in government contracting, “we have met the enemy and he might be us”.

## Training Opportunities

### 2016 Redstone Government Consulting Sponsored Seminar Schedule

**September 8, 2016** – **The Life Cycle of an Indirect Cost Rate Proposal**

LIVE event; Huntsville, AL – [REGISTER HERE](#)

### 2016 Federal Publications Sponsored Seminar Schedule

**September 19-20, 2016** – **Cost and Price Analysis in Government Contracts**

Fort Worth, TX

**October 24-25, 2016** – **Accounting Compliance for Government Contractors**

Sterling, VA

**November 3-4, 2016** – **Cost and Price Analysis in Government Contracts**

Sterling, VA

Go to <http://www.fedpubseminars.com/> and click on the Government Contracts tab.



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**Save the Date:**

### **The Redstone Edge Conference**

September 22, 2016  
Jackson Center  
600 Genome Way  
Huntsville, AL

#### **We will have a wide range of topics including:**

- Policy & Strategy briefing from Kenneth Saccoccia, Deputy Director, Defense Contract Audit Agency
- Current Events & Better Buying Power 3.0 Update from Jon Shire, Director DCMA Cost & Pricing Center
- Morning Panel Session on Acquisition and Exit Strategies with insight from Jeff McGrath, Managing Director, Wells Fargo Securities and Jerry Ripperger, VP Consulting, Principal Financial Group. Joining them on the panel are Walter Batson, co-founder of InterFuze Corporation and Camber Corporation and Bill Roark, co-founder and CEO of Torch Technologies, Inc. to provide a first-hand insight on Acquisitions and ESOP transactions from a company's perspective.
- Afternoon Session on Changes in SBA Regulations affecting small business government contractors, including changes to Limitations on Subcontracting; the new universal Small Business Mentor-Protégé Program; and the overhaul of Joint Venture requirements. This session will be led by Steve Koprince, noted attorney and small business advocate, with participation from other small business industry and government experts.

**8 hours of NASBA CPE credits will be offered for this event**

Breakfast, a plated lunch and snacks throughout the day will be provided to all attendees. Immediately following the event we will have an after-hours networking session at the Jackson Center Pub sponsored by Deltek where conference attendees will be able to meet and interact with speakers.

[CLICK HERE](#) to register The Redstone Edge Conference



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## Blog Articles to our Website

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### **Be Aggressive with Your MMAS Compliance - DCAA Will**

Posted by Wayne Murdock Steen on Thu, Aug 25, 2016 – [Read More](#)

### **DOD-IG Reports Trillions in Unsupported Journal Entries DFAS and the Army**

Posted by Michael Steen on Thu, Aug 18, 2016 – [Read More](#)

### **Provisional Billing Rates ARE NOT Pricing Bid Rates**

Posted by Michael Steen on Thu, Aug 11, 2016 – [Read More](#)

### **Blending Multiple Compensations Caps**

Posted by Kimberly Basden on Mon, Aug 1, 2016 – [Read More](#)

### **Unanet 2015 Partner of The Year: Certified Implementation Consultant**

Posted by Katie Donnell on Mon, Jul 25, 2016 – [Read More](#)

### **DOE Withdraws Contractor Business Systems' Rule**

Posted by Michael Steen on Thu, Jul 14, 2016 – [Read More](#)

### **DCAA Incurred Cost Audits Yield New and Novel Audit Cost Recovery Issues**

Posted by Michael Steen on Fri, Jul 8, 2016 – [Read More](#)

### **DCAA Should Resume Its Full Mission**

Posted by Wayne Murdock on Thu, Jun 23, 2016 – [Read More](#)

### **When a Firm-Fixed Price Contract Becomes a Curse**

Posted by Cheryl Anderson on Fri, Jun 3, 2016 – [Read More](#)

### **Department of Labor Issues New Dollar Threshold for Salary Exempt Employees**

Posted by Sheri Buchanan on Tue, May 24, 2016 – [Read More](#)

For More Blog Articles: <http://info.redstonegci.com/blog>

## Whitepapers Posted to our Website

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### **What Are The Prime Contractor's Risks Related to Subcontracts**

A Whitepaper by Asa Gilliland – [Read More](#)

### **The Audit World's Biggest Myths**

A Whitepaper by Wayne Murdock – [Read More](#)

### **Government Contracting and Uncompensated Overtime**

A Whitepaper by Wayne Murdock – [Read More](#)

### **DCAA Rejection of Incurred Cost Proposals**

A Whitepaper by Michael Steen – [Read More](#)

For More Whitepapers:

<http://www.redstonegci.com/resources/white-papers>

## CFO Roundtable

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Redstone Government Consulting, Inc., Radiance Technologies, Inc., & Warren Averett will be sponsoring a CFO/Controller roundtable for Government Contractors.

All Government contractor CFO's or Controllers are invited to participate. The meetings will be held quarterly and will include lunch and networking from 11:30am – 1:00pm. The next meeting is scheduled for September 30, 2016 at deciBel Research, Inc. Corporate Office, 325 Bob Heath Drive, Huntsville, AL 35806. Participants will be notified via email announcements for all future locations and seminar topics.

The CFO Roundtable is **free** to attend. All participants will be invited to share topics of interest and the group will be interactive. Redstone GCI, Radiance Technologies, and Warren Averett will strive to provide speakers on topics that are of interest to the group each quarter. Please provide us your email address and we will notify you 30 days in advance of each meeting. RSVP's are required.

Sign up for CFO Roundtable [here](#)



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### About Redstone Government Consulting, Inc.

Our Company's Mission Statement: RGCI enables contractors doing business with the U.S. government to comply with the complex and challenging procurement regulatory provisions and contract requirements by providing superior cost, pricing, accounting, and contracts administration consulting expertise to clients expeditiously, efficiently, and within customer expectations. Our consulting expertise and experience is unparalleled in understanding unique challenges of government contractors, our operating procedures are crafted and monitored to ensure rock-solid compliance, and our company's charter and implementing policies are designed to continuously meet needs of clients while fostering a long-term partnership with each client through pro-active communication with our clients

In achieving government contractor goals, all consulting services are planned and executed utilizing a quality control system to ensure client objectives and goals are fully understood; the right mix of experts with the proper experience are assigned to the requested task; clients are kept abreast of work progress; continuous communication is maintained during the engagement; work is managed and reviewed during the engagement; deliverables are consistent with and tailored to the original agreed-to scope of work, and; follow-up communication to determine the effectiveness of solutions and guidance provided by our experts.

### Specialized Training

Redstone Government Consulting, Inc. will develop and provide specialized Government contracts compliance training for client / contractor audiences. Topics on which we can provide training include estimating systems, FAR Part 31 Cost Principles, TINA and defective pricing, cost accounting system requirements, and basics of Cost Accounting Standards, just to name a few. If you have an interest in training, with educational needs specific to your company, please contact Ms. Lori Beth Moses at [lmoses@redstonegci.com](mailto:lmoses@redstonegci.com), or at 256-704-9811.



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