SEC. 815. ENHANCEMENT OF DEPARTMENT OF DEFENSE CAPABILITIES TO DETER AND RESPOND TO CONTRACTOR FRAUD.

(a) WITHHOLDING OF CONTRACTUAL PAYMENTS.—Subsection (a) of section 2207 of title 10, United States Code, is amended—

(1) by striking "unless that contract provides that—" and inserting "unless that contract provides each of the following:";

(2) in paragraph (1)—

(A) by inserting "That" after "(1)"; and

(B) by striking "; and" and inserting a period;

(3) in paragraph (2), by inserting "That," after "(2)"; and

(4) by inserting after paragraph (2) the following new paragraphs:

"(3) That with respect to a contract that could have been terminated under paragraph (1) but for the prior completion of the contract's performance, the United States is entitled to exemplary damages as set forth in paragraph (2), in accordance with the notice and hearing process set forth in paragraph (1).

"(4) That the Secretary of a military department or head of a Defense Agency may, after notifying the contractor but pending the determination concerning exemplary damages referred to in paragraph (2), withhold from payments otherwise due to the contractor under any contract between the contractor and that military department or Defense Agency an amount that is up to 10 times the cost incurred by the contractor in giving gratuities to the officer, official, or employee concerned, as such cost is estimated by the Secretary.".

(b) RETENTION OF DAMAGES; FRAUD FIGHTING FUNDS.—Such section is further amended—

(1) by redesignating subsection (b) as subsection (c); and

(2) by inserting after subsection (a) the following new subsection (b):

"(b) RETENTION OF DAMAGES; FRAUD FIGHTING FUNDS.—(1) Exemplary damages recovered under subsection (a)(2), once assessed against a contractor, may be retained by the Secretary of Defense, if assessed by a Defense Agency, or by the Secretary of the military department that assessed the damages against the contractor without regard to section 3302 of title 31.

"(2) The Secretary of Defense and the Secretaries of the military departments shall each establish a 'Fraud-Fighting Fund' (in this section referred to as the 'Fund') for use by the Defense Agencies, in the case of the Fund established by the Secretary of Defense, or military department, in the case of a Fund established by the Secretary of a military department, which shall be available to provide funds, in addition to funds which may be otherwise available for activities including training, investigations, administrative proceedings, enforcement actions, and other related activities associated with deterring and preventing fraud. Exemplary damages identified in subsection (a)(2), once assessed against the contractor, shall be paid into the Fund and shall be available until expended.".

(c) BURDEN OF PROOF.—Subsection (a)(1) of such section, as amended by subsection (a), is further amended by inserting "and by a preponderance of the evidence" after "after notice and hearing".

(d) TECHNICAL AMENDMENTS.—Subsection (a) of such section is further amended by striking "clause (1)" in paragraph (2) and in the flush sentence at the end and inserting "paragraph (1)".

(e) EFFECTIVE DATE.—The amendments made by this section shall apply to contracts that are awarded on or after the date that is 90 days after the date of the enactment of this Act.

(f) CONFORMING AMENDMENTS.—Section 2410m(a) of title 10, United States Code, is amended—

(1) by inserting "or arising from an assessment of exemplary damages under section 2207 of this title," after "of title 41";

(2) by striking "or" at the end of paragraph (2);

(3) by striking the period at the end of paragraph (3) and inserting "; or"; and

(4) by adding at the end the following new paragraph:

"(4) any determination under section 2207 of this title.".

(g) PROCUREMENT REGULATIONS.—Regulations governing actions under section 2207 shall be revised to implement the amendments to section 2207 of title 10, United States Code, made by this section not later than 90 days after the date of the enactment of this Act.

Section-by-Section Analysis

This proposal would enact three primary changes to the existing statute, accompanied by a number of non-substantive changes. First, this proposal would authorize the Department to withhold contractual payments pending the resolution of allegations that the contractor offered or gave a gratuity to an officer, official, or employee of the United States to influence a contract. Second, the proposal would authorize the Department to assess exemplary damages under a breached contract that was performed fully before the gratuities allegations were known or adjudicated. Third, this proposal would authorize the Department to retain monies paid as exemplary damages under section 2207 of title 10, United States Code, to support fraud-fighting activities.

With respect to withholding contractual payments, while section 2207 as currently written allows the Department to terminate a breached contract and to assess exemplary

damages, the statute is silent on whether the Department may withhold contractual payments for the exemplary damages based on preliminary information that a violation occurred. Although the Department may have an implied right to withhold sums for exemplary damages prior to a final determination of a violation, there is no federal court ruling specifically affirming or rejecting the Government's right to withhold for exemplary damages under section 2207 and the contractual clause it requires before a final determination has been made by the agency head or designee. By incorporating a clear, explicit collection mechanism into the statute, the proposal would provide the Department with an efficient means to hold Government contractors accountable for wrongdoing. The proposal also would provide contractors with clear notice that corrupting or seeking to corrupt procurement personnel puts contract payments at risk. In the event that the allegations that the contractor offered or gave a gratuity to Department personnel to influence the contract were not substantiated, any payments withheld that were due and payable under the contract would be subject to the Prompt Payment Act (31 U.S.C. § 3902).

As currently written, section 2207 arguably allows the Department to assess exemplary damages only after a contract has been terminated after the offer or gifting of an improper gratuity. This can produce a result where the Government has no redress in the event of a tainted contract that has been fully performed. The Government should not be deprived of these remedy because of the timing of performance, which is irrelevant to the corruption problem section 2207 seeks to ameliorate. The Government frequently does not become aware of an alleged gratuity until after performance of a contract is complete, and so this aspect of the proposal would close a significant, inadvertent loophole.

This proposal will also permit Defense Agencies and the military departments to keep monies assessed as exemplary damages under section 2207 to support their fraud-fighting efforts. The proposal would permit the Secretary of Defense and the Secretaries of each military department to create their own fraud-fighting fund. The Defense Agencies would be permitted to place exemplary damages collected from contractors into the Secretary of Defense fund, and the military departments will also be permitted to place exemplary damages collected into their specific fraud-fighting funds. While section 2207 currently allows the Government to assess exemplary damages, section 3302(b) of title 31 requires that all money received for the Government from any source must be deposited into the U.S. Treasury as miscellaneous receipts. A primary exception to this rule is that an agency may retain and obligate funds that it collects if expressly authorized to do so by statute. Further, the statutory language permitting retention of money that is collected must specify the types of receipts that an agency may retain and the sources of those receipts. The proposed amendment to section 2207 meets these principals.

The Comptroller General has applied the requirement for specificity to agencies seeking to retain exemplary damage awards to fund other agency specific funds without the express authority to do so. There are a number of examples of statutory authority that permit agencies to retain monies received from a non-governmental source based on administrative procedures. For example, section 527 of title 28 permits the Department of Justice to place three percent of all amount collected by their civil debt collection litigation into a working capital fund.

Additionally, the proposal would clarify existing law by explicitly incorporating the burden of proof applicable to a determination of whether section 2207 was violated in a specific

instance. Currently, the Government applies a preponderance-of-the-evidence burden of proof to its determinations under section 2207. As the statute is civil in nature, that is appropriate. Including this standard in the statute would ensure that the Department continues to apply section 2207 in a consistent manner and would provide Government contractors with a clearer understanding of their rights. The proposed change would make clear that section 2207 is not available if there is a mere suspicion of improper activity.

This proposal would not make withholding of funds mandatory. The agency head or designee would retain discretion as to whether withholding contractual payments is appropriate and in the public's interest. The proposed amendment would retain, and build upon, the existing notice and hearing protections provided to contractors by requiring notice to be provided before the commencement of withholding. Incorporating a civil burden of proof into the law is likewise consistent with preserving the rights of Government contractors under the statute. Finally, retaining exemplary damages collected against contractors who have paid improper gratuities would further bolster the Government's ability to deter and address acquisition and procurement fraud through monies collected from those who would perpetrate fraudulent schemes against the Government. Because use of the retained monies would be limited to that purpose, a fraud-fighting fund would not create an incentive for military agencies to pursue actions under section 2207 as an alternative method of funding their operations.

Budget Implications: Although it is not possible to assess accurately in advance the impact of the proposed changes, this proposal is expected to have no budgetary impact and to result in cost avoidance by simplifying collection procedures and providing clear guidance to Government contractors. Presently there are no appropriations specifically directed towards fighting fraud and, as a result, Defense Agencies and the military departments expend mission funds on this important activity. Additionally, any decrease in Governmental exposure to fraud resulting from increased fraud-fighting funds would ultimately reduce money wasted due to fraud.

Changes to Existing Law: This proposal would make the following changes to section 2207 of title 10, United States Code:

§ 2207. Expenditure of appropriations: limitation

(a) Money appropriated to the Department of Defense may not be spent under a contract other than a contract for personal services unless that contract provides ~~that —~~ each of the following:

(1) That the United States may, by written notice to the contractor, terminate the right of the contractor to proceed under the contract if the Secretary concerned or his designee finds, after notice and hearing and by a preponderance of the evidence, that the contractor, or his agent or other representative offered or gave any gratuity, such as entertainment or a gift, to an officer, official, or employee of the United States to obtain a contract or favorable treatment in the awarding, amending, or making of determinations concerning the performance, of a contract. ~~; and~~

(2) That, if a contract is terminated under ~~clause~~ paragraph (1), the United States has the same remedies against the contractor that it would have had if the contractor had breached the contract and, in addition to other damages, is entitled to exemplary damages

in an amount at least three, but not more than 10, as determined by the Secretary or his designee, times the cost incurred by the contractor in giving gratuities to the officer, official, or employee concerned.

(3) That with respect to a contract that could have been terminated under paragraph (1) but for the prior completion of the contract's performance, the United States is entitled to exemplary damages as set forth in paragraph (2), in accordance with the notice and hearing process set forth in paragraph (1).

(4) That the Secretary of a military department or head of a Defense Agency may, after notifying the contractor but pending the determination concerning exemplary damages referred to in paragraph (2), withhold from payments otherwise due to the contractor under any contract between the contractor and that military department or Defense Agency an amount that is up to 10 times the cost incurred by the contractor in giving gratuities to the officer, official, or employee concerned, as such cost is estimated by the Secretary.

The existence of facts upon which the Secretary makes findings under ~~clause~~ paragraph (1) may be reviewed by any competent court.

(b) RETENTION OF DAMAGES; FRAUD FIGHTING FUNDS.—(1) Exemplary damages recovered under subsection (a)(2), once assessed against a contractor, may be retained by the Secretary of Defense, if assessed by a Defense Agency, or by the Secretary of the military department that assessed the damages against the contractor without regard to section 3302 of title 31.

(2) The Secretary of Defense and the Secretaries of the military departments shall each establish a 'Fraud-Fighting Fund' (in this section referred to as the 'Fund') for use by the Defense Agencies, in the case of the Fund established by the Secretary of Defense, or military department, in the case of a Fund established by the Secretary of a military department, which shall be available to provide funds, in addition to funds which may be otherwise available for activities including training, investigations, administrative proceedings, enforcement actions, and other related activities associated with deterring and preventing fraud. Exemplary damages identified in subsection (a)(2), once assessed against the contractor, shall be paid into the Fund, and shall be available until expended.

(~~b~~c) This section does not apply to a contract that is for an amount not greater than the simplified acquisition threshold (as defined in section 134 of title 41).

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§2410m. Retention of amounts collected from contractor during the pendency of contract dispute

(a) RETENTION OF FUNDS.—Notwithstanding sections 1552 (a) and 3302 (b) of title 31, any amount, including interest, collected from a contractor as a result of a claim made by a military department or Defense Agency under chapter 71 of title 41 or arising from an assessment of exemplary damages under section 2207 of this title, shall remain available in accordance with this section to pay—

(1) any settlement of the claim by the parties;

(2) any judgment rendered in the contractor's favor on an appeal of the decision on that claim to the Armed Services Board of Contract Appeals under section 7104 (a) of title 41; ~~or~~

(3) any judgment rendered in the contractor's favor in an action on that claim in a court of the United States; or.

(4) any determination under section 2207 of this title.

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