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Federal Contractors Face Increased Scrutiny on Pay

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On March 15, 2022, the U.S. Department of Labor's Office of Federal Contract Compliance Programs issued [a new Directive](#) regarding contractors' obligation to evaluate their compensation system "to determine whether there are gender-, race-, or ethnicity-based disparities," as required by 41 CFR 60-2.17(b)(3). The OFCCP, according to the Directive, has the authority to access and review contractor records reflecting the evaluation of a contractor's compensation system, despite claims of attorney-client privilege. While it does not have the force of law, the Directive is a clear statement of the Agency's position on this very important issue affecting contractors.

The same day, President Biden issued an [Executive Order](#) on Advancing Economy, Efficiency, and Effectiveness in Federal Contracting by Promoting Pay Equity and Transparency. The Executive Order tasks the Federal Acquisition Regulatory Council with considering whether to issue proposed rules to limit or prohibit federal contractors from seeking and considering job applicants' or employees' past pay history.

These announcements signal what will likely be a wave of increased scrutiny on the pay equity audit and salary inquiry practices of companies that do business with the federal government.

Contractors' Obligation To Review Pay

As part of their affirmative action programs, covered contractors are required to "perform in-depth analyses of [their] total employment process to determine whether and where impediments to equal employment opportunity exist." Specifically, contractors must analyze their compensation system(s) – "to determine whether there are gender-, race-, or ethnicity-based disparities." 41 CFR § 60-2.17(b)(3). With increasing frequency, contractors retain counsel for purposes of performing an attorney-client privileged pay equity analysis of pay outcomes to evaluate legal risks and satisfy this obligation. Courts have recognized that, when properly done, an analysis of pay outcomes can be protected by the attorney-client privilege. The new Directive challenges whether contractors can assert the privilege and still prove compliance with the regulations.

OFCCP Compliance Evaluations Scrutinize Pay

During a compliance evaluation, contractors must provide the OFCCP with individual employee compensation data to enable the Agency to review and determine whether the contractor has a compliant affirmative action program and is satisfying its nondiscrimination obligations. The Agency often relies on regression and other statistical analyses to evaluate whether there are gender, race or

ethnicity disparities. If that review “reveals disparities in pay or other concerns about the contractor’s compensation practices,” the new Directive states, “OFCCP may request additional information . . . including [the contractor’s] pay equity audit conducted pursuant to [41 CFR § 60-2.17(b)(3)].”

Specifically, the Directive states that the OFCCP may request contractors subject to compliance reviews to provide:

- “a complete copy of the pay equity audit(s) conducted pursuant to 2.17(b)(3) that shows all pay groupings that were evaluated, any variables used, and the results of the analyses, including any disparities found;”
- “the model statistics (such as b-coefficients, significance tests, R-squared, F-tests, etc.) for all variables or comparisons in the model;” and
- “information relating to the frequency of pay equity audits, the communication to management, and how the results were used to rectify disparities based on gender, race and/or ethnicity.”

Contractors “may not withhold” their pay equity audit and compliance records “by invoking attorney-client privilege or the attorney work-product doctrine,” according to the Directive. It is the OFCCP’s position that “[f]ederal contractors have a regulatory obligation to provide [] pay equity audit and compliance records to OFCCP” and “[t]his obligation defeats any expectation that the pay equity audit and compliance records prepared with the assistance of counsel would remain confidential.” The Directive warns that “[f]ailure to provide the required pay equity audit will be considered by OFCCP as an admission of noncompliance with these regulatory requirements.”

What This Means for Federal Contractors

The implications of the OFCCP’s March 15 Directive are two-fold. First, federal contractors subject to compliance reviews can expect more detailed inquiries from the OFCCP on the method, model, and results of any pay equity study performed to satisfy the regulatory obligation to evaluate pay. The Directive therefore reinforces the importance of documenting—and retaining—the evaluation of compensation systems to determine whether there are gender-, race-, or ethnicity-based disparities, as provided in 41 CFR 60-2.17(b)(3).

Second, contractors performing the evaluation under the attorney-client privilege should develop alternative means of satisfying the regulatory obligation, in order to protect the sensitive self-critical and privileged analyses from production. Performing a separate, non-privileged study that can be provided to the OFCCP is the approach the Directive contemplates. “Where the contractor has produced to OFCCP an acceptable pay equity audit sufficient to demonstrate compliance with 2.17(b)(3),” the Directive states, “OFCCP will not require production of these separate pay equity audits, to the extent that the contractor can verify that [the separate pay equity studies] were conducted under privilege.”

Coming Soon: Contractors May Face Pay History Bans

Contractors may also soon be subject to a salary history inquiry ban, similar to those adopted by some state and local governments across the country. President Biden’s March 15, 2022 Executive Order tasks the Federal Acquisition Regulatory Council (the “FARC”) with “issuing proposed rules” that “enhance pay equity and transparency for job applicants and employees of Federal contractors and subcontractors.” The EO requires the FARC to “specifically consider whether any such rules should limit or prohibit Federal contractors and subcontractors from seeking and considering information about job

applicants' and employees' existing or past compensation when making employment decisions." The EO also requires the FARC to "consider the inclusion of appropriate accountability measures in any such rules."

Paul Hastings is monitoring these developments and will provide updates when they are available.



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