EDITOR’S NOTE: On January 30, we reported that President Barack Obama had signed three Executive Orders affecting federal contractors. At the time, we promised to follow up with a more in-depth analysis of the Executive Order treating as “unallowable” federal funds used in connection with union organizing efforts on “cost-plus” government contracts. The following is our promised analysis. A separate Client Bulletin discusses the Executive Order revoking the Bush Administration “Beck Rule,” requiring that federal contractors notify employees of their rights not to join a union and not to have their dues used for political or other non-representational purposes. The third Executive Order requires that “successor” contractors on federal service contracts offer positions to the non-management employees of the predecessor contractors in most cases.

Sending a clear pro-union signal to both employers and organized labor, President Obama initiated the first step toward what many believe will be a union-friendly agenda over the next four years. Executive Order No. 13495 could have a direct impact on a “cost-plus” contractor’s right and ability to react to a union organizing effort.

The Order, entitled “Economy in Government Contracting,” says it is intended “to promote economy and efficiency in Government contracting” and to “ensure the economical and efficient administration of Government contracts, contracting departments and agencies, when they enter into, receive proposals for, or make disbursements pursuant to a contract as to which certain costs are treated as unallowable....”

Under this Order, such “unallowable costs” would include the following activities, if those activities are undertaken to persuade employees “to exercise or not to exercise rights to organize and bargain collectively”:

* preparing and distributing materials;
* hiring and working with legal counsel or consultants;
* holding meetings (including paying the attendees at meetings held for this purpose); and
* planning or conducting activities by managers, supervisors, or union representatives during work hours.

The Executive Order mirrors an attempt of the Clinton Administration in 1999 to achieve the same objective through a rule amending the Federal Acquisition Regulation.
Order applies to “cost-plus” contracts only

As a general rule, the only government contracts that will be affected by the Order are those for which the government reimburses costs, as distinguished from fixed-price contracts for which a contractor’s costs are its own responsibility.

In the case of contracts for which the government reimburses costs (cost-plus contracts), the government reimburses contractors for costs that are reasonably incurred in performing the contracts and properly allocable to contract performance. Whether the government will reimburse any particular cost in connection with such contracts depends not only on the general concepts of reasonableness and allocability, but also on extensive regulations concerning costs that are specifically “allowable” and those which are specifically “unallowable.”

Before the Order was issued, the applicable Federal Acquisition Regulation provided that “[c]osts incurred in maintaining satisfactory relations between the contractor and its employees, including costs of shop stewards, labor management committees, employee publications, and other related activities, are allowable.” 48 C.F.R. §31.205-21. The Order effectively requires an exception to the regulation for specified activities undertaken to persuade employees in the exercise or non-exercise of particular rights. Costs incurred in connection with such activities will now be expressly “unallowable” and, therefore, non-reimbursable.

Effective date

Although the Executive Order takes effect “immediately,” it also provides for a 150-day regulatory period for agency adoption of rules and regulations connected with the Order. The Order will then apply only to contracts “resulting from solicitations issued on or after” the effective date of the Agency action taken at the end of the 150-day regulatory period.

For contracts awarded based on solicitations issued on or after this date, the employer would no longer receive reimbursement for costs incurred in connection with responding to a union organizing attempt. “Unallowable” costs on such contracts would then include consulting or legal fees, the cost of developing or distributing informational literature, the time spent by managers engaged in informational efforts, and even compensation to employees for the time spent by employees in information meetings.

Legal challenges may follow

It is clear that Executive Orders are subject to judicial review and under certain circumstances can be invalidated as unconstitutional. Prior Executive Orders dealing with issues related to management-union issues have been successfully challenged on grounds that the Orders were preempted by the National Labor Relations Act. In Chamber of Commerce v. Reich, the U.S. Court of Appeals for the District of Columbia Circuit struck down an Executive Order issued by President William Jefferson Clinton that prohibited federal contractors from hiring permanent replacement workers. The court found that the NLRA preempted President Clinton’s EO because the NLRA specifically allowed employers to hire permanent replacement workers as part of the delicate balance between the rights of management and labor to apply economic pressure on each other. The Court reasoned that President Clinton’s attempt to manage spending restrictions under the Procurement Act, albeit under the veil of fiscal responsibility, amounted to impermissible “regulatory” action that altered the NLRA.

Similarly, President Obama’s Executive Order may be vulnerable to a preemption challenge. The EO looks very much like a California law recently struck down by the U.S. Supreme Court in Chamber of Commerce v. Brown. In that case, the Supreme Court ruled that Section 8(c) of the NLRA allows an employer to express views, argument, or opinion on union-
ization, and to distribute materials in written, printed or graphic form, communicating those views, as long as they do not contain threats of reprisal, force, or a promise of benefit. Because this right is protected by the NLRA, the Court reasoned that California’s attempt to interfere with or modify it was preempted by the NLRA. The same argument could (and probably will) be made with respect to President Obama’s Executive Order.

If you need assistance in interpreting or applying Executive Order 13495, please contact any member of Constangy’s Labor Relations or Affirmative Action practice groups, or the Constangy attorney of your choice.

Carl Cannon, Bob Lemert, and Cliff Nelson assisted in writing this article.

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