OFCCP AND FEDERAL CONTRACTORS ARE SIGNIFICANT FOCUS OF EXECUTIVE BRANCH ACTIONS FOR EQUAL PAY DAY

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U.S. Labor, Employment, and Workplace Safety Alert

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This alert addresses the following:

- The Office of Federal Contract Compliance (OFCCP) has issued its first Directive of the Biden Administration, the Pay Equity Audit Directive (DIR 2022-01) (Directive);
- The Directive was part of numerous related Executive actions that President Biden announced for Equal Pay Day;
- The Directive maintains the Trump-era Compensation Directive while also indicating that longer, more extensive audits and more information requests may be on the horizon for contractors;
- Most of the Directive addressed pay equity self-audits that contractors do annually as part of affirmative action programs;
- OFCCP indicated that it would be focusing on enforcing the self-audit requirement, and seeking those self-audits more often during compliance reviews;
- OFCCP also provided its position on how the attorney-client and work product privileges apply to self-audits done for OFCCP compliance, as well as those done for legal advice (or a combination of both); and
- Contractors must be careful to consult with counsel on how to set up their pay equity self-audits so they comply with OFCCP requirements while preserving privilege where applicable.

OVERVIEW OF EXECUTIVE BRANCH PRONOUNCEMENTS ON PAY EQUITY

The Directive dovetails with President Biden's presidential announcement on 15 March 2022 (Announcement), which outlined “critical steps that the Biden-Harris Administration is taking to advance pay equity and promote women's economic security,” specifically highlighting the issuance of the Directive by OFCCP. The Announcement focused on the following additional key action items:

1. Advancing pay equity for the federal workforce;
2. Promoting efforts to achieve pay equity for job applicants and employees of federal contractors;
3. Ensuring equitable access to well-paying jobs; and

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4. Addressing discrimination against caregivers.[1]

As part of the Announcement, President Biden directly referenced the Directive, as well as a 15 March 2022 executive order (Executive Order) that instructed the Federal Acquisition Regulatory Council (FAR Council) to consider enhancing pay equity and transparency, including by limiting or restricting federal contractors from requesting and considering information about both job candidates' and employees' current or past compensation in the context of hiring and other employment decisions.

Under the Executive Order, the FAR Council will consult with the Secretary of Labor and other executive branch agencies and departments as to whether proposed rules should be issued "to promote economy, efficiency, and effectiveness in Federal procurement by enhancing pay equity and transparency for job applicants and employees of Federal contractors and subcontractors."[2] If such rules and regulations are proposed, they would mirror state and local government actions that limit, and in some cases, prohibit, employers from seeking prior compensation information from candidates for employment.[3] The nationwide effects could be much broader, though, as this would be the first federal regulation to set such a standard.

With the Announcement, Executive Order, and Directive, the Biden administration is signaling its prioritization of pay equity, especially as it applies to federal employees and the federal contractor workforce. Therefore, employers who are federal contractors should closely monitor these developments to ensure continued compliance with applicable regulations.

ANALYSIS OF THE OFCCP DIRECTIVE

The Directive focuses on the following key issues, which are discussed in detail below: preserving the Trump-era Compensation Directive (DIR 2018-05) (Compensation Directive), which governs how OFCCP evaluates contractor pay systems; broadening the pay equity component of audits and increasing reliance on supplemental information requests; increasing focus on ensuring contractors are conducting annual compensation reviews as part of their affirmative action programs; and indicating that OFCCP will request contractors' internal pay equity audits during compliance reviews. Finally, and likely of utmost importance to employers subject to OFCCP jurisdiction, the Directive outlines OFCCP's position as to the scope of the attorney-client privilege as it applies to internal pay equity audits.

Directive Preserves the Trump-Era Compensation Directive

The Directive preserves the Compensation Directive issued during the Trump administration, which committed the agency to (1) evaluating pay equity based on how the contractor has set up its job and compensation structure, (2) recognizing the legitimate, nondiscriminatory factors on which a contractor relies to set pay, and (3) generally requiring both statistical and anecdotal evidence of compensation discrimination in audits before making a finding, except in extraordinary circumstances. This is one of the most significant components of the Directive.

The preservation of the Compensation Directive is not surprising given that many contractors have been using this as a guide in how to conduct annual pay equity self-audits—the primary focus of the Directive. A change to the Compensation Directive would likely have required giving contractors more time to adjust to any new guidance before the agency could scrutinize their pay equity self-audits.

Directive Indicates Broader, More Extensive Audits Planned

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The Directive also emphasizes OFCCP's intent to audit a contractor's workforce more broadly and extensively than before, which could lead to longer audits, while also meaning fewer total audits, since more time would be required for each one.

OFCCP indicated that it "will look broadly at a contractor's workforce" during a desk audit, evaluating "across job titles, levels, roles, positions, and functions[] to identify patterns of segregation by race, ethnicity, and gender, which may result from assignment, placement, or upgrading/promotion barriers that drive pay disparities." This all-encompassing language could conceivably indicate OFCCP's intent to audit a contractor's entire workforce across establishments (or create very large pay analysis groups) instead of focusing on specific establishments and specific job titles or job groups. It also indicates the importance of contractors retaining counsel to run broader internal pay equity audits to proactively address potential inequities across establishments.

The Directive goes on to say that OFCCP will utilize regression analysis to look for disparities in patterns in salary paid across similar functions and positions. In the event this examination results in concerns with the contractor's compensation patterns or practices, OFCCP can request further information, including more compensation data, records and copies of the contractor's pay equity audits. The Directive identifies four instances in which OFCCP would likely request additional information and the contractor's full pay equity audit results:

5. Pay disparities or other evidence of pay discrimination among similarly-situated employees based on race, ethnicity, or gender;
6. Employee complaints of pay discrimination or other anecdotal evidence of discrimination;
7. Inconsistencies in how the contractor is applying its pay policies; or
8. Statistical or other evidence that a group of workers is disproportionately concentrated in lower paying positions or lower pay levels within a position based on a protected characteristic.

Presumably, these supplemental requests would still comply with the Transparency Directive (DIR 2020-02) (Transparency Directive), which mandates that such requests "must include the basis for the request, be reasonably tailored to the areas of concern, and allow for a reasonable time to respond." The purpose of this requirement is to ensure that OFCCP goes beyond the documents required by the scheduling letter (which goes through a notice and comment process) only when there is an articulable basis and the contractor is informed of that basis.

Tension Between Efficiency and Expansion

This expansion in audit scope could potentially signal a departure from the Efficiency Directive (DIR 2018-08) (Efficiency Directive), which focused on shortening compliance audits through a clearly delineated collection of evidence/information based on the scheduling letter and the promotion of early resolution. The Efficiency Directive establishes a goal of completing compliance evaluations within 180 days where there are no preliminary findings of discrimination.

The expanded scope of information requests to contractors under the new Directive and OFCCP's "systemic analyses to look for disparities in patterns of assignment or in salary paid across similar functions and positions" may make meeting the 180-day benchmark more difficult in more audits. Moreover, with a broader data set to analyze, there is an increased chance that the preliminary findings will trigger additional information requests,

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including a request for the contractor's pay equity audit, methodology and model statistics, further extending audits.

It is possible this expanded view of entire workforces across establishments and the evaluation of data across similar functions and positions means that OFCCP is thinking about contractor workforces more broadly and may eventually seek a regulation to compel companies to adopt Functional Affirmative Action Programs. Contractors should continue to conduct self-audits in accordance with 41 C.F.R. § 60-2.17(b)(3) to identify whether pay disparities exist and develop action-oriented programs to address these problems, now with the understanding that OFCCP may request "a complete copy" of any pay equity audit showing all pay groupings that were evaluated, any variables used, and the results of the analyses. Contractors with establishment-based affirmative action plans should consider whether their pay equity audit should analyze functional lines as well (under protection of privilege, where possible).

Finally, this part of the Directive could possibly signal a return towards the policy of longer, more in depth audits, referred to as Active Case Enforcement (ACE), during the Obama administration. Nonetheless, this remains an open question, because OFCCP's Transparency and Efficiency Directives, which commit the agency to shorter, less burdensome audits, continue as agency guidance as well.[4] This is definitely an area where contractors should stay tuned and continue to monitor.

Annual AAP Pay Equity Self-Audits Will Be Requested in Audits

OFCCP indicates that in some compliance reviews it will start directly requesting production of internal pay equity audits done pursuant to OFCCP regulations, including information as[5] 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." OFCCP has historically requested such information from time to time in compliance reviews on an ad hoc basis, but this is the first time it has indicated it will do so as a matter of agency policy when certain conditions are present.

Notably, the agency does not provide specific guidance as to what constitutes an adequate pay equity analysis for purposes of this regulation, which could be welcomed by contractors if they were given a meaningful opportunity to provide input on the guidance, particularly if following the guidance creates something like a safe harbor. This may be an area on which OFCCP will focus in the future. Until it does, contractors should be consulting with counsel as to the sufficiency of a self-audit for their specific situation, particularly as this information may end up being turned over to OFCCP.

OFCCP'S APPROACH TO THE ATTORNEY-CLIENT PRIVILEGE

One of the most important features of OFCCP's Directive is its position on the attorney-client privilege as it pertains to pay equity self-audits. Although OFCCP has previously taken the position that it can request these self-audits in a compliance review, this is its most prominent statement in a guidance document to date that it **can and will** request these self-audits.

OFCCP then goes further to state that when requested by OFCCP, contractors cannot withhold these items based on either attorney-client privilege or the work-product doctrine (while allowing that a separate audit done for legal advice would be protected by privilege). Importantly, OFCCP will also consider a failure to provide the required self-audits as an admission of noncompliance.

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Of course, the Directive does not establish the scope or applicability of the attorney-client or work product privileges, which is largely determined by courts in litigation.[6] Nevertheless, the Directive states OFCCP's position on these privileges, which indicates that OFCCP may be more assertive in requesting documents that contractors have previously shielded from disclosure by raising privilege.

OFCCP Asserts That Privilege Does Not Apply to Certain Self-Audits

Contractors frequently retain counsel to assist them in performing pay equity audits. However, OFCCP regulations *require* contractors to conduct at least a basic compensation review as part of their annual affirmative action programs and to provide those audit records to OFCCP upon request.[7] The Directive emphasizes that a contractor's pay equity audit is an "important component of the contractor's affirmative action program."

To implement these regulations, OFCCP's most recent Directive takes the position that OFCCP has the authority to request the analyses the contractor has conducted to comply with the regulations. The Directive further explains that contractors may not withhold documentation of their compliance with OFCCP regulations based on the attorney-client privilege or the work-product doctrine because contractors have a regulatory obligation to maintain and provide OFCCP with evidence of their compliance with their affirmative action obligations.

In support, the Directive notes that a communication is not confidential if it is intended to be disclosed to a third party. Given that "contractors have a regulatory obligation to provide the pay equity audit and compliance records to OFCCP," OFCCP asserts that this obligation "defeats any expectation that the pay equity audit and compliance records prepared with the assistance of counsel would remain confidential." Similarly, the Directive states that a contractor engaged in litigation against OFCCP may not withhold its pay equity audit and compliance records by invoking the work product doctrine, noting that the "detailed requirements" of 41 C.F.R. § 60-217(b) "mean that the documents would have been prepared in substantially similar form in the absence of litigation."

OFCCP Recognizes Privilege Applies to Certain Pay Equity Audits Done for Legal Advice

Nonetheless, the Directive provides that contractors may conduct a separate pay equity audit to obtain privileged legal advice and not for demonstrating compliance with OFCCP regulations, and OFCCP will not require production of those separate audits so long as the contractor can verify that they were in fact conducted under privilege. However, if a contractor conducts a dual-purpose pay equity audit or analysis of employment processes (i.e., one that implicates *both* legal concerns *and* OFCCP compliance), OFCCP indicates that it may request those records.

Contractors should consider OFCCP's privilege guidance carefully. OFCCP is essentially committing to recognizing attorney-client privilege for more complex pay equity reviews conducted through an attorney under privilege to provide legal advice, where the contractor also performs a basic pay equity audit in compliance with the regulations (which would be subject to discovery to demonstrate compliance with the obligation). Going forward, contractors may wish to work with counsel to conduct self-audits through this approach, with greater comfort that the agency will recognize privilege for the audit done for legal advice.

One potential concern for contractors will be for audits performed before the Directive was issued, where a combined audit to comply with regulations and for legal advice was conducted and where the contractor believed the audit was being conducted under privilege. OFCCP has not indicated how it will treat those audits or whether

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it will apply its Directive retroactively. Contractors will have to consider with their counsel to what extent to assert privilege for all or part of these audits, knowing it may lead to litigation with OFCCP.

In OFCCP audits, there is no subpoena process. As a result, the only legal mechanism through which a contractor can obtain a ruling on privilege issues from a court (if OFCCP rejects the assertion of privilege), is to deny access to documents or information requested. OFCCP may then file litigation through the Solicitor of Labor before an administrative law judge regarding the denial of access. That process is very inefficient and expensive for resolving simple privilege disputes, and unlikely to be in either side's best interests. Accordingly, contractors should use their best judgment in consultation with counsel in determining to what extent they wish to assert attorney-client communication or work-product over these self-audits.

Contractors Should Consult With Counsel in Determining How to Both Comply and Preserve Privilege

To comply with the Directive, while maintaining the greatest possible protections for privileged information, contractors should strongly consider conducting routine pay equity self-audits annually that comply with Section 60-2.17(b)(3). The Directive does not require these to be regression analyses. Contractors could potentially use a more qualitative or evaluative approach to reviewing compensation, including through the use of more basic quantitative techniques or cohort analysis, if that is sufficient to meaningfully asses the compensation system in compliance with the regulation.

Contractors who comply with Section 60-2.17(b)(3) would then have the opportunity to conduct more detailed, regression analyses separately under privilege with an expert and under the direction of counsel. This would allow counsel to provide legal advice about pay equity issues. One point that should be remembered about attorney-client privilege is that it facilitates employers taking proactive steps to obtain and follow legal advice in the area of pay equity, likely helping enhance pay equity, not harming it.

Ultimately, the Directive is a valuable reminder that contractors should be careful in how they conduct pay equity audits. Contractors should also take care, in general, in preserving confidentiality and privilege in structuring affirmative action programs and other diversity, equity, inclusion and accessibility practices. To do so, contractors should consult with counsel at the start of any such initiative, including an internal pay equity audit. Best practices for preserving the attorney-client privilege include:

- A written engagement letter with counsel detailing the project and that counsel will be rendering legal advice with respect to the project
- Engagement by counsel—rather than directly with the contractor—of any vendor (e.g., consulting company, labor economist, statistician) involved in the initiative
- Limiting the distribution of the communications and documentation relating to the initiative within the contractor's organization to those who have a business reason to be involved with the matter
- Strict instructions to employees within the contractor's organization working on the project to preserve the privilege, including not to forward confidential and privileged materials externally
- Consulting with counsel prior to disclosing any documents or information to prevent accidental or unintended waivers of the privilege

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- Labeling communications and documentation associated with the initiative as privileged and confidential where appropriate.
- Storing all documents and information relating to annual pay equity audits for 41 C.F.R. § 60-2.17(b)(3) compliance separately from documents and information relating to pay equity audits undertaken for the purpose of obtaining legal advice

CONCLUSION

The first Directive of the Biden Administration demonstrates a continued prioritization of compensation and pay equity in compliance reviews. It also emphasizes the importance of conducting annual self-audits, which are helpful tools in proactively addressing and maintaining pay equity. Contractors should use the Directive as an opportunity to consult with counsel and reassess the current compensation system reviews they are doing as part of their Affirmative Action Programs, ensuring they are done in a way that maximizes benefit and minimizes risk.

FOOTNOTES

[1] On 14 March 2022, the Equal Employment Opportunity Commission published technical assistance on caregiver discrimination against caregivers in the workplace, with a focus on discrimination against applicants and employees due to pandemic-related caregiving responsibilities.

[2] Further, the federal hiring process may see similar changes as the Office of Personnel Management announced that, consistent with the President's Executive Order on Diversity, Equity, Inclusion, and Accessibility in the Federal Workforce, it anticipates issuing a proposed regulation addressing the use of prior salary history in hiring and compensation determinations for federal employees.

[3] *See, e.g.*, Equal Pay Act of 2003, 820 Ill. Comp. Stat. 112/ et seq; N.Y. Lab. Law § 194-a; N.J. Stat. Ann. § 34:6B-20; Washington Equal Pay and Opportunities Act, Wash. Rev. Code § 49.58; and Cal. Lab. Code § 432.3.

[4] Likewise, the agency continues to have its Compliance Review Procedures Directive (DIR 2019-01), which formally rescinded ACE in favor of following OFCCP's Federal Contract Compliance Manual in audits.

[5] 41 C.F.R. 60-2.17(b)(3).

[6] In general, the attorney-client privilege attaches to any confidential communications made between an attorney and client for the purpose of obtaining legal advice. *See Fisher v. United States*, 425 U.S. 391, 403 (1976). The work-product doctrine is distinct from the attorney-client privilege and protects from disclosure any documents that an attorney or an attorney's representative prepares in anticipation of litigation or for trial, and any documents recording the attorney's mental impressions, conclusions, opinions, or legal theories concerning the litigation or potential litigation. FED. R. CIV. P. 26(b)(3)(A).

[7] 41 C.F.R. § 60-21.7(b)(3); 60-2.10(c).

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