

# False Claims Act and *Qui Tam* Quarterly Review

## INSIDE... 1 FALSE CLAIMS ACT AND *QUI TAM* DECISIONS

### Prefiling Release of *Qui Tam* Claim

*U.S. ex rel. Green v. Northrop Corporation et al.* (9th Cir. July 12, 1995) . . . . . p. 1

*U.S. ex rel. Pogue v. American Healthcorp, Inc. et al.* (M.D.Tenn. Sept. 14, 1995) . . . p. 3

### Public Disclosure Bar

*U.S. ex rel. Schumer v. Hughes Aircraft Co.* (9th Cir. Aug. 22, 1995) . . . . . p. 4

*U.S. ex rel. LeBlanc v. Raytheon Company, Inc.* (1st Cir. Aug. 9, 1995). . . . . p. 6

*U.S. ex rel. Eitel v. Roy D. Reagan et al.* (D.Ore. Aug. 16, 1995). . . . . p. 6

### Relator Responsibility for Costs in Non-Frivolous Action

*U.S. ex rel. Lindenthal and Willis v. General Dynamics* (9th Cir. Aug. 2, 1995) . . . . . p. 7

### False Progress Reports

*U.S. ex rel. Schwedt v. Planning Research Corporation* (D.C. Cir. July 7, 1995) . . . . . p. 9

### Knowledge Standard

*Covington, Sidicane, U.S. v. Sisters of the Third Order of St. Dominic of Hanford, California, d/b/a Sacred Heart Hospital et al.* (9th Cir. July 13, 1995) . . . . . p. 11

### Dischargeability of Fraud Settlement in Bankruptcy

*U.S. v. Spicer* (D.C. Cir. June 30, 1995) . . . . . p. 14

### Filing and Service Requirements

*U.S. ex rel. Pilon et al. v. Martin Marietta Corporation and General Electric Company* (2nd Cir. July 25, 1995). . . . . p. 15

*U.S. ex rel. Windsor v. DynCorp, Inc. et al.* (E.D. Va. Aug. 9, 1995). . . . . p. 16

### Limitation by Relator of Government Communication with Defendant

*U.S. ex rel. Pentagon Technologies International Limited v. CACI International Inc. et al.* (S.D.N.Y. July 6, 1995) . . . . . p. 17

### Section 3730(h) Retaliation Claims

*Childree v. UAP/GA Ag-Chem et al.* (N.D.Ga. June 20, 1995) . . . . . p. 18

*U.S. ex rel. Lamar v. Burke and Arsenal Credit Union* (E.D.Mo. Aug. 21, 1995). . p. 19

### Third Party Indemnification Claims

*U.S. ex rel. Public Integrity v. Therapeutic Technology Inc. et al.; Therapeutic Technology Inc. et al., Third-Party Plaintiffs v. HNE Healthcare, Inc., Third-Party Defendant* (S.D.Ala. Aug. 7, 1995) . . . . . p. 20

### Anti-Kickback and Self-Referral Violations

*U.S. ex rel. Pogue v. American Healthcorp, Inc. et al.* (M.D.Tenn. Sept. 14, 1995) . . p. 21

### Davis-Bacon Act Violations

*U.S. ex rel. Windsor v. DynCorp, Inc. et al.* (E.D.Va. Aug. 9, 1995). . . . . p. 23

### Falsity of Claim

*U.S. ex rel. Hindo v. University of Health Sciences/The Chicago Medical School* (7th Cir. Sept. 6, 1995). . . . . p. 25

29

## SPOTLIGHT

### *Qui Tam* Statistics

### Recoveries Top \$1 Billion

30 **DOJ INTERVENTIONS AND UNSEALED CASES**32 ***QUI TAM* SETTLEMENTS**34 **DOJ SETTLEMENTS**

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The *False Claims Act and Qui Tam Quarterly Review* is published by Taxpayers Against Fraud, The False Claims Act Legal Center (TAF). This publication provides an overview of major False Claims Act and *qui tam* developments including case decisions, Department of Justice interventions, and settlements.

TAF is a nonprofit public interest organization dedicated to combating fraud against the Federal Government through the promotion and use of the *qui tam* provisions of the False Claims Act. TAF's mission is both activist and educational. Established in 1986, TAF serves to: (1) collect and evaluate evidence of fraud against the Federal Government and report such fraud through the filing of False Claims Act *qui tam* suits; (2) work in partnership with the Government to effectively prosecute *qui tam* suits; (3) inform and educate the general public, the legal community, and other interested groups about the False Claims Act and its *qui tam* provisions; and (4) advance public, legislative, and government support for *qui tam*.

TAF is based in Washington, D.C., where it maintains a comprehensive False Claims Act library for public use and a staff of lawyers and other professionals who are available to assist *qui tam* plaintiffs and counsel.

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## Prefiling Release of *Qui Tam* Claim

*U.S. ex rel. Green v. Northrop Corporation et al.*, 59 F.3d 953 (9th Cir. July 12, 1995)

**A relator who executed a general release with his former employer to settle an employment action should not have been barred from pursuing a subsequent *qui tam* case against that employer, according to the 9th Circuit. In reversing the district court's dismissal of the relator's case, the appellate panel ruled that the release was unenforceable on public policy grounds because enforcement of such releases would significantly dilute the FCA's incentives to encourage more *qui tam* actions. The relator's action alleging double-billing on the B-2 bomber program was remanded for further proceedings.**

In November 1988, Green filed a wrongful termination case in California state court against Northrop. Green maintained that his discharge in October 1988 resulted from his uncovering and bringing to the attention of Northrop officials evidence that Northrop had "double charged" the U.S. Air Force for equipment procured for the B-2 bomber program. Northrop and Green negotiated a settlement to that suit and entered into a "Settlement Agreement and General Release" on April 16, 1990.

On January 11, 1991, Green filed a *qui tam* suit against Northrop, a third party contractor (Autek), and several employees of both companies. In February 1992, the Government declined to intervene in the suit. Defendants Northrop and Bussard then moved for summary judgment on the grounds that Green had bargained away his right to bring a *qui tam* action and share in any recovery and, as a consequence, could not demonstrate a personal stake in the outcome sufficient to satisfy Article III standing requirements.

The district court agreed with the defendants and dismissed the action for lack of subject matter jurisdiction. The court concluded that the April 16, 1990 agreement unambiguously released all claims that Green had against Northrop, including any under the FCA. Moreover, the court asserted, because the Government had elected not to intervene, "there are no public policy considerations which would bar the enforcement of the General Release. On the contrary, public policy strongly favors the enforcement of 'ironclad and enforceable general releases.'" Finally, the court ruled that, by bargaining away his right to recovery under the FCA, Green had lost any standing he might otherwise have had to bring a *qui tam* action against Northrop. Green appealed.

The 9th Circuit assumed for purposes of analysis that the April 16 settlement release encompassed Green's right to bring a *qui tam* action as well as to any recovery from that action. Nonetheless, the court reversed the district court and held that the release was unenforceable because "its enforcement would impair impermissibly a substantial public policy."

## Uniform Federal Common Law Rule Governs in Absence of Congressional Intent

As an initial matter, the 9th Circuit addressed whether federal common law or congressional intent governed the enforceability of a release of a *qui tam* claim. The court agreed with the defendants that, if Congress has expressed its intent regarding such, that intent must be given effect. However, the court found no basis in the statute or legislative history for inferring that Congress intended such a release to be either enforceable or unenforceable. Moreover, the court found it "inappropriate to presume Congress' intent from its failure to resolve the question expressly."

While the FCA is silent regarding the enforceability of a pre-filing release of a *qui tam* claim, the statute does address the ability of relators, defendants, and the Government to enter into a settlement following

the filing of a *qui tam* action. Invoking an elemental canon of statutory interpretation, the defendants argued that Congress' decision to address postfiling settlements of *qui tam* claims necessarily meant that it intended prefiling releases of such claims to be enforceable.

The court, however, found the cited canon to be irrelevant. It traditionally has been applied in addressing whether the statute at issue permits an implied private right of action. The canon ensures that "courts do not upset a 'comprehensive legislative scheme' by creating additional 'procedures for enforcement' that Congress did not intend." By contrast, the court explained, the FCA clearly permits a *qui tam* suit to be brought by private parties as "a key part of the statute's 'integrated system' for enforcement." In short, "[t]he general presumption that Congress did not intend to create remedies by implication provides no guidance as to whether Congress intended to permit parties to release a particular remedy that it expressly created, and, if so, under what circumstances." The court suggested that, in fact, preventing parties from releasing the remedy without government consent may be more consistent with the enforcement scheme established by Congress.

Faced with a "gap" in the statutory scheme, the court noted that "[i]t is well established that federal common law properly is invoked to determine the validity of a release of a statutorily-conferred federal right." The court then applied the test set forth in United States v. Kimbell Foods, 99 S.Ct. 1448 (1979), and determined that the formulation of a uniform federal common law rule was justified, rather than reliance on state law.

### **Rumery/Davies Test**

The uniform federal common law test applied by the appellate court was articulated by the Supreme Court in Town of Newton v. Rumery, 107 S.Ct. 1187 (1987), and further elaborated upon by the 9th Circuit in Davies v. Grossmont Union High Sch. Dist., 930 F.2d 1390, 1396 (9th Cir.), cert. denied, 111 S.Ct. 2892 (1991). In Rumery, the Supreme Court held that "a promise is unenforceable if the interest in its enforcement is outweighed in the circumstances by a public policy harmed by

enforcement of the agreement." In Davies, the 9th Circuit concluded that "when there is a substantial public interest that would be harmed by enforcement . . . the party seeking enforcement must, at the least, advance some important interest in addition to the interest in settlement." Summarizing the Davies test, the 9th Circuit explained that it must undertake "(1) to determine whether the agreement waives a right that impacts upon the public interest; (2) determine whether a substantial public interest would be impaired by enforcement of the agreement; and (3) to ascertain the reasons apart from the general interest in settling disputes that support enforcing the agreement." Under Davies, the interest in the settlement of litigation "cannot by itself outweigh a substantial public interest on the other side of the scales."

### **Enforcing Prefiling Release Would Impair A Substantial Public Interest**

The 9th Circuit concluded that enforcing Green's release would impair a substantial public interest by threatening to nullify the incentives Congress sought to create in amending the FCA in 1986. According to the court, "[t]he vital importance of the incentive effect is demonstrated by the reasons set forth by Congress in 1986 in undertaking the first extensive revision of the Act since its enactment in 1863." According to legislative history, Congress concluded that widespread fraud that significantly threatened the federal treasury "only could successfully be combated by 'a coordinated effort of both the Government and the citizenry.'" Recognizing both the difficulties in detecting fraud and the lack of government enforcement resources, Congress' overall intent was "to encourage more private enforcement suits."

Accordingly, the court emphasized: "[O]ur focus must be on what impact the release will have on the incentive effect Congress intended to create and the importance of that incentive effect in achieving the FCA's goals of detecting and deterring fraud on the government." The court concluded that enforcing a prefiling release would not only plainly undermine the incentives and operation of the Act but also dilute the Act's important deterrence objectives.

The court found unpersuasive the defendants' argument that enforcing the release would not impair the objectives of the *qui tam* provisions because other Northrop employees could bring claims under the Act. The court noted that in this particular case the §3730(e)(4) jurisdictional bar would likely prohibit other persons from bringing suit. More importantly, as a general matter, the court stated: "[H]ypothesizing the existence of other employees who possess relevant information and are willing to come forward is far too fragile a basis for enforcing the Release. There is, of course, no guarantee that such persons exist." Moreover, under Northrop's logic, the company could enter into similar release agreements with other employees as long as it stopped short of demanding a release from all employees as a matter of course. Thus, according to the court, "it is unclear how the government or the courts could ensure that potential relators remain."

The defendants also maintained that the public interest would not be impaired because a pre-filing release, unlike a post-filing release, does not foreclose the Government from bringing suit. The court responded that "this argument misses the point." Again, "the very purpose of the Act's *qui tam* provisions is to create incentives for relators to supplement government enforcement."

The defendants further argued that any effect on the public interest would not be "substantial." They relied on Rumery, which involved the release of a Section 1983 civil rights claim. A plurality of that court "characterized the public interest at issue as 'diffuse[ ]' and refused to 'elevate' it 'above Rumery's considered decision that he would benefit personally from the [release].'" In rejecting this argument, the 9th Circuit emphasized that Section 1983 and the *qui tam* provisions serve very different goals. Unlike a Section 1983 claim, which serves both a public interest and to compensate those actually injured, "*qui tam* actions exist only to vindicate the public interest." The relator's right to recovery exists to deter fraud and return funds to the federal treasury, not to compensate the relator. Moreover, "Congress itself has stated that the public interests that the *qui tam* provisions serve are substantial."

## Interests That Favor Enforcement of Release Are Clearly Outweighed

Lastly, the court assessed the interests favoring enforcement of the release. The defendants argued that the most important public policy issue before the court was "whether a defense contractor will ever be able to settle, fully and finally, the disputes that may arise with its employees." In fact, explained the defendants, all entities that receive federal funds will be less likely to settle employment-related claims "if they lack the ability to 'buy complete peace' with employees." This result would impose significant costs on these entities, their employees, and the judicial system that, in sum, would outweigh any harm to the public interest that would result from enforcing the release.

The court responded that the defendants' argument relied primarily on the "general interest in the settlement of litigation" that it had found in Davies to be insufficient to overcome the impairment of a substantial public interest. Furthermore, any additional costs suffered by defendants, employees, and other employers from the inability of employers to obtain fully enforceable releases such as the one at hand are not sufficient to alter the balance. Finally, the court noted that "the imposition of these additional costs may in fact further the purposes of the FCA." Defendants who likely committed fraud in the first place are those who will be deterred most from settling non-FCA claims because of the possibility of a *qui tam* suit. "Therefore, if refusal to enforce the Release in this case increases defendants' costs, this actually might have the salutary effect of further deterring defendants from engaging in fraud."

***U.S. ex rel. Pogue v. American Healthcorp, Inc. et al., Memorandum and Order, No. 3-94-0515 (M.D.Tenn. Sept. 14, 1995)***

See "*Anti-Kickback and Self-Referral Violations*" below in this section.

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## Public Disclosure Bar

*U.S. ex rel. Schumer v. Hughes Aircraft Co.*, 63 F.3d 1512 (9th Cir. Aug. 22, 1995)

Neither the Government's disclosure of audits to employees of the defendant company nor the theoretical availability of audits through the Freedom of Information Act (FOIA) constitutes a "public disclosure" within the meaning of the False Claims Act, the 9th Circuit ruled in a case brought by a former Hughes Aircraft employee who alleged mischarging and other improprieties involving work on radar systems for F-15 fighter planes and the B-2 bomber program. The court also ruled for the relator on the issues of retroactivity and constitutionality. On the merits, the court affirmed summary judgment against the relator on all but two claims, which it reversed and remanded for further proceedings.

### Government Disclosure of Audit to Employees Not a "Public Disclosure"

In holding that the Government's disclosure of audits to Hughes and Northrop employees was not a "public disclosure," the 9th Circuit declined to adopt the ruling of *U.S. ex rel. John Doe v. John Doe Corp.*, 960 F.2d 318 (2d Cir. 1992), upon which the defendants relied. In *Doe*, the 2nd Circuit held that a public disclosure occurred when federal investigators executing a search warrant informed employees of their investigation into fraudulent overcharging. According to that court, "once allegations of fraud are revealed to members of the public with no prior knowledge thereof, the Government can no longer throw a cloak of secrecy around the allegations." By contrast, the 9th Circuit found that treating company employees as members of the public is "unrealistic," noting that there are strong economic incentives for employees to keep the information from outsiders. As a result, disclosures to employees are less likely to lead to

fraud being exposed and remedied than disclosures to the general public.

The 9th Circuit analogized disclosure to company employees to disclosure by one government employee to another, which the appellate court had previously held not to constitute "public disclosure." According to the court, the analogy is especially true in the context of defense procurement where the parties involved "operate within a closed loop of secrecy." In other words, "both situations involve the release of information within a private sphere." Giving the public disclosure provision a "practical, commonsense interpretation," the court found that information "disclosed in private" to company employees does not constitute a "public disclosure" under the Act.

### Court Finds *Doe* Rule Contrary to Congress' Intent to Expand *Qui Tam* Jurisdiction

The 9th Circuit found that the *Doe* court's approach was, in effect, a return to the pre-1986 restrictive jurisdictional bar based on government possession of information because *Doe* curtails the ability of relators to bring suit once the Government becomes involved. According to the court, this is contrary to Congress' intent to expand the opportunity for more *qui tam* suits and to avoid complete reliance on government action. Finally, the 9th Circuit noted Hughes' concern that the court's rule would open the floodgates to parasitic actions whenever the Government audited a company. The court responded that "any such effect would be limited to a single lawsuit in each instance" and that the concern is "offset by Congress's desire to avoid total reliance on government enforcement."

### Disclosures Through FOIA Not "Public Disclosures" Unless Actually Made Available to the Public

Again giving the FCA a "practical, commonsense interpretation," the court ruled that only actual disclosures (as opposed to theoretical or potential disclosures) are "public disclosures." The court rejected Hughes' argument that, because the unclassified audits were theoretically available under FOIA

prior to the filing of the *qui tam* action, the audits were publicly disclosed. Hughes relied on U.S. ex rel. Stinson et al. v. Prudential Ins. Co., 944 F.2d 1149 (3d Cir. 1991), in which the 3rd Circuit held that allegations made available through the discovery process and “equally available to strangers to the fraud transaction” are considered to be publicly disclosed even if the material has not actually been filed with the court. The 9th Circuit, however, rejected the Stinson rule, following instead the approach in U.S. ex rel. Springfield Terminal v. Quinn, 14 F.3d 645 (D.C.Cir. 1994), in which the D.C. Circuit distinguished between discovery material actually versus theoretically made public through filing.

According to the 9th Circuit, this distinction is particularly relevant in the FOIA context because “a document held by the government and subject to public inspection only after all FOIA conditions have been satisfied is far less accessible to the public” than even a document on file with the court. Here, Schumer had filed suit prior to his request for and receipt of copies of the audits through FOIA. In this context, “information cannot be deemed disclosed until a member of the public requests the information and receives it from the government.” Since the audits were not actually made available prior to Schumer’s suit, the audits were not publicly disclosed. Because the court found that there was no public disclosure of the government audits, it did not address whether Schumer’s claims were “based upon” the audits or whether Schumer was an “original source.”

### **1986 Jurisdictional Provision Applies Retrospectively**

For the third time in recent months, the 9th Circuit ruled that the 1986 amendment to the jurisdictional bar involving public disclosures applies retrospectively because the amendment does not infringe on the substantive rights of the defendant and, therefore, does not rebut the presumption of retrospective application of jurisdictional provisions. Hughes had argued that the more restrictive pre-1986 provision should apply because Schumer’s allegations involved cost allocations primarily made prior to 1986.

As in its previous decisions on retroactivity, the court followed the test established in Landgraf v. USI Film Products, 114 S.Ct.1483 (1994). First, the court examined whether Congress intended for the 1986 amendments to apply retrospectively. Finding that Congress had not demonstrated such an intent, the court followed the presumption stated in Landgraf that jurisdictional statutes apply retrospectively because they ordinarily “speak to the power of the court rather than to the rights or obligations of the parties.”

To rebut that presumption, Hughes had to show that the amendment had retroactive effect, i.e., impaired substantive rights existing at the time of the conduct, increased liability for past conduct, or imposed new duties upon completed transactions. However, the court, citing its recent decisions U.S. ex rel. Lindenthal and Willis v. General Dynamics Corp., 61 F.3d 1402 (9th Cir. Aug. 2, 1995) and U.S. ex rel. Anderson v. Northern Telecom, Inc., 52 F.3d 810 (9th Cir. Apr. 20, 1995), found that the 1986 jurisdictional provision did not alter substantive rights. Rather, it only “altered the conditions under which a *qui tam* relator can bring an action to enforce that liability.” Therefore, the 1986 provision applied in this case.

### **Summary Judgment Against Relator Affirmed on All But Two Claims**

Schumer, a former Hughes manager, alleged that Hughes defrauded the Government by establishing unauthorized and illegal internal “commonality agreements” to allocate certain costs of projects over more than one subcontract. The alleged mischarging involved Hughes subcontracts with Northrop to develop a radar system for the B-2 bomber program and its subcontracts for other aircraft projects such as the F-14, F-15, and F-18. The district court granted Hughes’ motion for summary judgment, finding that Hughes had properly informed and secured the approval of the Air Force and all but one of the contractors for the commonality agreements, and that any failure by Hughes to inform was excusable because of the security concerns relating to the B-2 program.

On appeal, the 9th Circuit reversed the district court’s grant of summary judgment on Schumer’s

claims that Hughes failed to disclose properly the terms of its commonality agreements to Northrop and that Hughes did not comply with the disclosure requirements of the Cost Accounting Standards (CAS). However, the appellate court affirmed the district court's rulings on Schumer's remaining claims. Those claims included that Hughes mischarged development costs for "gate array" technology for the Analog Signal Converter to the B-2 subcontract and violated a CAS prohibition against pooling of direct costs.

### **Constitutionality of *Qui Tam* Provisions Upheld**

Relying on its decision in U.S. ex rel. Kelly v. Boeing, 9 F.3d 743 (9th Cir. 1993), cert. denied, 114 S.Ct. 1125 (1994), the 9th Circuit was quick to affirm the constitutionality of the *qui tam* provisions, thus reinforcing the unanimity among the federal courts to have addressed this issue. Specifically, the court held that the FCA did not violate Article III standing requirements, the doctrine of separation of powers, or the Appointment Clause's limitation on who may conduct litigation on behalf of the United States.

### **Relator Prohibited from Adding Retaliation Claim Three Years After Filing Complaint**

The 9th Circuit also affirmed the lower court's rejection of Schumer's attempt to amend his complaint to add a §3730(h) retaliation claim and similar state law claim three years after bringing the *qui tam* action. According to the court, because Schumer knew all the facts relevant to these claims when his complaint was first filed, the district court did not abuse its discretion by finding "undue delay" and denying Schumer's motion for leave to amend.

*U.S. ex rel. LeBlanc v. Raytheon Company, Inc.*, 62 F.3d 1411 (1st Cir. Aug. 9, 1995)

**Characterizing the district court's opinion as "a careful, well-reasoned opinion that correctly analyzed and applied the relevant doctrines," the 1st Circuit summarily affirmed**

**the dismissal of a *qui tam* suit under the public disclosure jurisdictional bar. In January 1995, a Massachusetts district court had dismissed this *qui tam* action alleging defects in the Patriot missile that the relator LeBlanc would not have known about "but for" public disclosures in congressional hearings and news articles. According to the district court, LeBlanc's added analysis that Raytheon must have violated quality control requirements was not sufficient to save the action from the public disclosure bar.**

*U.S. ex rel. Eitel v. Roy D. Reagan et al., Opinion and Order, Civ. No. 94-425-JO (D.Ore. Aug. 16, 1995)*

**A *qui tam* plaintiff who alleged fraud against the United States Forest Service by certain individuals and aviation contractors failed to demonstrate that he was an "original source" of the publicly disclosed information underlying his suit, an Oregon district court ruled. The court found that Eitel did not have "direct and independent" knowledge of the information on which his allegations were based and therefore did not meet his burden of establishing subject matter jurisdiction.**

The court based its holding exclusively on its "original source" determination, noting that Eitel had conceded that the allegations were publicly disclosed. However, the court proceeded with its "original source" analysis without first determining whether Eitel's complaint was "based upon" the public disclosures. Nevertheless, in considering whether Eitel possessed the requisite "direct and independent" knowledge, the court found that he had derived nearly all his information from public sources such as news articles, government investigations, and documents obtained through the Freedom of Information Act.

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## Relator Responsibility for Costs in Non-Frivolous Action

*U.S. ex rel. Lindenthal and Willis v. General Dynamics*, 61 F.3d 1402 (9th Cir. Aug. 2, 1995)

In a *qui tam* case lost on the merits but determined not to be frivolous or vexatious, the 9th Circuit upheld an order that relators pay \$50,000 in defendant's costs pursuant to F.R.C.P. 54(d), which permits courts to award costs to a prevailing party unless the operative statute contains an express provision relating to costs. While the FCA contains a provision that requires relators to pay defendants' attorneys' fees and expenses if a suit is clearly frivolous or vexatious, the appellate court found that this language was not an "express provision" under the FCA that would displace a court's authority to award Rule 54 costs. Acknowledging that the "question is close," the court declined to accept the statute's reference to "expenses" as incorporating "costs" since, in the court's view, the FCA treats fees, expenses, and costs as separate and distinct. On a separate issue, the court ruled that the 1986 public disclosure jurisdictional provision applied even though the defendant's conduct occurred prior to 1986.

The relators filed suit in connection with a contract between Aydin Corporation and the Air Force for the production of MUTES, a system for training pilots that simulates enemy radar. Under the contract, Aydin was to produce MUTES based on engineering drawings prepared by General Dynamics (GD) under a previous contract with the Air Force. However, Aydin encountered difficulty reproducing the MUTES system from GD's drawings and was forced to make changes. These problems ultimately led to a renegotiation of the contract between Aydin and the Air Force for an additional \$22 million. Soon afterwards, Lindenthal and Willis, employees

of Aydin, filed a *qui tam* suit alleging GD defrauded the Government in the amount of \$22 million. The relators alleged that GD knowingly provided inadequate drawings and then submitted claims for payment that were false because the claims were based on work that did not meet the contract requirements. The district court ruled against the relators on the merits and ordered them to pay \$50,000 in costs to GD under Rule 54(d).

### Decision on the Merits Not Clearly Erroneous

The district court ruled that GD's claims were not "false" because its contract did not require that the drawings be error free or suitable for a "build to print" follow-on contract with another contractor. In reaching this finding, the district court concluded that the contract terms were ambiguous and admitted extrinsic evidence to determine the parties' expectations. Air Force representatives testified that the Air Force had not expected GD's drawings to be suitable for a build to print follow-on contract and that the Air Force was "very happy with the drawings." Based on the evidence, the district court found that the Air Force intended to procure from GD drawings that were suitable for GD-built equipment, not necessarily equipment and systems that would be produced by another contractor. As a result, any claims for payment based on work that satisfied GD's contractual obligations could not have been "false or fraudulent" within the meaning of the FCA.

The 9th Circuit agreed that the contract requirements were ambiguous and that therefore the district court did not err in admitting extrinsic evidence. The appellate court also ruled that it was not clearly erroneous for the district court to find that GD's drawings satisfied the contractual obligations and, as a result, affirmed the district court's holding that no false claims were submitted.

### District Court Had Authority to Award Costs Against Relators

The relators appealed the award of costs against them, contending that the district court lacked authority to award Rule 54(d) costs because the FCA contains an express provision at §3730(d)(4)

which supersedes the rule. (By the terms of Rule 54(d), the rule does not apply when “express provision” for awarding costs is otherwise made by the operative statute.) Under §3730(d)(4), relators may be assessed “attorneys’ fees and expenses” if the action is determined to be “clearly frivolous, clearly vexatious, or brought primarily for purposes of harassment.” In this case, the district court had ruled that the *qui tam* action was not “clearly frivolous, clearly vexatious, or brought primarily for purposes of harassment.” According to the relators, while §3730(d)(4) does not include the term “costs,” its reference to “expenses” includes costs.

The 9th Circuit disagreed, finding that on its face §3730(d)(4) does not constitute an “express provision” regarding “costs” because the term “costs” is not specifically mentioned. The court reasoned that “expenses” does not incorporate costs because other provisions in the FCA treat fees, expenses, and costs as three distinct categories. Specifically, §3730(d)(2) allows a prevailing relator an award of “reasonable expenses necessarily incurred, plus reasonable attorneys’ fees and costs.” Additionally, §3730(g) applies 28 U.S.C. §2412(d) when the Government intervenes but does not prevail. Under the latter provision, a court has authority to award certain prevailing parties “fees, and other expenses, in addition to any costs.” The 9th Circuit concluded that it would be “incongruous” to find that §3730(d)(4), which refers only to “fees” and “expenses,” is an express provision regarding “costs” given its silence regarding “costs.”

### **District Court Did Not Abuse Its Discretion in Awarding Costs**

The 9th Circuit also rejected the relators’ argument that the district court had abused its discretion in awarding costs. Just prior to issuing its decision in this case, the 9th Circuit had held in another case that, in order to show abuse of discretion in the awarding of Rule 54(d) costs, the unsuccessful litigant must show some impropriety on the part of the prevailing party worthy of punishment. National Info. Servs. v. TRW, Inc., 51 F.3d 1470 (9th Cir.), amended, 52 F.3d 334 (1995). The court read Rule 54(d) to create a presumption in favor of awarding costs to the prevailing party absent a showing of impropriety. Although relators

Lindenthal and Willis put forth 12 reasons supporting their abuse of discretion argument, the court found that none of those reasons related to misconduct by GD. Accordingly, the 9th Circuit ruled that the relators did not overcome the presumption and the district court did not abuse its discretion in awarding costs.

### **1986 Jurisdictional Provision Applies Retrospectively**

The 9th Circuit, as it has in other recent cases, followed the Supreme Court’s retroactivity analysis in Landgraf v. USA Film Products, 114 S.Ct. 1483 (1994), in addressing whether the FCA’s 1986 jurisdictional provision at §3730(e)(4) applied in this case. Under Landgraf, the court must first determine whether Congress has “expressly prescribed the statute’s proper reach.” If Congress has not demonstrated its intent, then the court must focus on the conduct affected and determine whether the amendment will have “retroactive effect,” i.e., impair substantive rights existing at the time of the conduct, increase liability for past conduct, or impose new duties upon completed transactions. If so, there is a presumption against retroactive application “absent clear congressional intent favoring such a result.” The 9th Circuit clarified Landgraf terminology by using the term “retrospective” to describe application of a new statute to events that occurred before its enactment and “retroactive” to describe a statute that, if applied, would attach new legal consequences to past conduct.

While the 9th Circuit acknowledged that in U.S. ex rel. Anderson v. Northern Telecom, Inc., 52 F.3d 810 (9th Cir. Apr. 20, 1995), it had applied the 1986 jurisdictional provision to a suit involving alleged false claims that occurred prior to the 1986 amendments, it noted that the panel expressly declined to decide whether the provision was “retroactive.” In that case the relator had both revealed his information to the Government and filed suit after 1986. Since the jurisdictional provision only changed the consequences of the relator’s conduct, the Anderson panel “avoided the key inquiry under Landgraf because application of the new law to the case at hand did not constitute application [to pre-1986 conduct].”

By contrast, in this case the relators had revealed their information to the Government prior to the 1986 amendments. If the pre-1986 rule applied, the court would not have subject matter jurisdiction over the action because the Government was in possession of the information prior to the filing of the *qui tam* suit. The court, then, necessarily faced the question of whether the new jurisdictional provision applied retrospectively.

### **Amendment Did Not Alter GD's Obligation Not To Commit Fraud**

As in Anderson, the 9th Circuit found that the new jurisdictional provision did not attach any new legal consequences to GD's past actions. The provision only affects a relator's right to bring a *qui tam* suit. If GD submitted false claims prior to 1986, "it became liable and remained liable to the government." The appellate court rejected GD's argument that the amendment has retroactive effect because it eliminated an "absolute defense" GD had in the pre-1986 government notice jurisdictional bar. According to the court, the provision was "simply a jurisdictional defense" to a *qui tam* action, as opposed to one brought directly by the Government. Moreover, as the Landgraf court stated, "present law governs . . . because jurisdictional statutes speak to the power of the court rather than to the rights and obligations of the parties." In contrast to the pre-1986 bar, under the 1986 provision the court has authority to hear a claim where the Government already possessed the information, provided the new public disclosure bar does not apply. "The amendment simply did not alter GD's underlying obligation not to commit fraud upon the government." Therefore, the 9th Circuit affirmed the district court's retrospective application of the 1986 jurisdictional provision in this case.

### **Public Disclosure Bar Not Triggered Because All Elements Not Present**

GD argued that the relators' suit should be barred even under the 1986 jurisdictional provision because seven different documents constituted public disclosures. In rejecting this contention, the 9th Circuit recognized that the Act creates a four-part test for determining whether the §3730(e)(4)(A) public disclosure bar applies. First,

there must be a "public disclosure." Second, it must be a disclosure of "allegations or transactions." Third, the disclosure must be in an enumerated method or manner (e.g., an "administrative hearing"). Finally, the suit must be "based upon" the public disclosure. A *qui tam* action is barred only if each and every element of the test is satisfied.

Applying this test, the court found that each of the seven documents either did not constitute an "allegation or transaction" of fraud, was not disclosed publicly, or failed on both counts. Consequently, the 9th Circuit held that "none of the alleged disclosures GD presented to the district court triggers the jurisdictional bar."

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## **False Progress Reports**

*U.S. ex rel. Schwedt v. Planning Research Corporation, 59 F.3d 196 (D.C. Cir. July 7, 1995)*

**The knowing submission of false progress reports -- even though the reports are not invoices -- triggers FCA liability, according to the D.C. Circuit. In reversing the district court's dismissal of a *qui tam* case involving a software development contract, the appellate court also ruled that if the Government relied on false progress reports in deciding to pay for certain individual items (such as manuals), those payments may constitute damages under the Act even if the delivered items were in fact compliant. The relator, a former government employee responsible for overseeing the contract, had alleged that the Government paid for certain items only because of the defendant's false representations that the entire software project was nearing successful completion.**

In 1992, Schwedt, Director of the Office of Information Management at the Department of Labor's Pension Welfare Benefits Administration (PWBA), filed this *qui tam* action against Planning

Research Corporation (PRC). The district court dismissed most of Schwedt's claims under F.R.C.P. 9(b) for not meeting the heightened pleading requirements for fraud and granted summary judgment for PRC on the one remaining claim.

In 1989, the PWBA contracted with PRC to design and implement a computer software system to link the PWBA's national and field offices. PRC was to complete seven sequential "milestones," running from initial system design through production of software to presentation of a final report. A series of individual "deliverables" (e.g., a training manual) was also called for, each of which was due at a particular stage and was to be paid for upon acceptance by the Government. The contract included an acceptance and payment system for each deliverable. No payment could be requested or made before government acceptance.

Schwedt was responsible for overseeing the contract. PRC made four deliveries of the software and submitted three progress reports which represented that the software was either "99%" or "100%" complete. The Government rejected the software after testing on each occasion. In short, Schwedt alleged that PRC unlawfully and knowingly "presented and caused to be presented non-functional and non-compliant software to representatives of the United States while wrongfully and knowingly misrepresenting that said software was compliant and functional." He maintained that PRC submitted false progress reports about the status and success of the software system in order to induce the Government to pay for various components.

### **False Progress Reports Are "False Claims"**

The D.C. Circuit pointed out that, in dismissing the bulk of Schwedt's complaint, the district court failed to consider whether progress reports themselves, although not invoices, might constitute "false claims" or "statements" under §3729 of the FCA. In fact, the appellate court emphasized, a submission need not be an actual invoice to be a "claim" or "statement." The court then found that Schwedt's complaint sufficiently stated a claim based on the three allegedly false progress reports submitted by PRC.

Specifically, the court held that if PRC knowingly submitted false progress reports stating that the software delivered was complete when in fact it was not, then the reports constituted false statements in support of false claims. That the reports were not invoices was immaterial. The reports were submitted during the same period the software was, and "[t]hough PRC did not submit a bill for the software, its goal of receiving payment was implicit in the submission of the goods, and the accompanying progress reports had the purpose of 'get[ting] ... [the] claim ... approved.' 31 U.S.C. §3729(a)(2)."

### **Losses Resulting "Because Of" False Progress Reports May Constitute FCA Damages**

Schwedt alleged that he made on behalf of the Government approximately \$500,000 in payments for various deliverables because of PRC's progress report representations that the project was nearing successful completion: "But for the progress reports and representations by PRC, I would not have accepted and paid for the milestone products which are worthless without contractually compliant software." The court held that if Schwedt could prove that he relied on PRC's false representations in deciding to pay for the individual components, those payments may constitute damages under the Act.

PRC argued that, because the contract allowed for payment only upon the Government's inspection and acceptance of the deliverables, the payments could not possibly have been made "because of" the alleged false statements and thus could not be claimed as FCA damages. Rejecting this argument, the court emphasized that under Schwedt's damages theory it was immaterial that the Government found the individual components to be contractually compliant. Even if, for example, the manual was in perfect form, it was useless without an entire working software package. The Government "would not have paid for it if not for PRC's representations that the whole package was imminently available."

The court clarified that it was not adopting the broad "but for" causation standard rejected in several decisions cited by PRC. Rather, Schwedt's claim "survives under the more restrictive standard" adopted by the 3rd and 5th Circuits -- "that

the submitter of a false claim should be liable only for those damages that arise because of the falsity of the claim, i.e., only for those damages that would not have come about if the defendant's misrepresentations had been true." In the case at hand, if PRC's representations had been true (i.e., that the software was at or near completion), then the Government's payments for the compliant deliverables would not have constituted damages (i.e., "money spent on useless goods").

Lastly, the court noted that its conclusion might have been different if the contract had been structured so that the Government was required to pay for all contractually compliant components regardless of misrepresentations concerning PRC's ability to perform the rest of the project. Then, PRC's alleged false representations "would not have caused any damages at all; they would simply be irrelevant." However, the contract in fact permitted the Government to terminate for default if PRC's performance was defective. Therefore, explained the court, absent PRC's false assurances that the software was nearly complete and workable, the Government could have avoided making payment to PRC (thereby incurring damages) by terminating the contract prior to accepting the deliverables that were ultimately determined to be compliant.

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## Knowledge Standard

*Covington, Sidicane, U.S. v. Sisters of the Third Order of St. Dominic of Hanford, California, d/b/a Sacred Heart Hospital et al., 61 F.3d 909, Unpublished Disposition (9th Cir. July 13, 1995)*

In a *qui tam* case involving Medicare overpayments mistakenly made to a rural hospital for several years both before and after 1986, the 9th Circuit held that the district court erred in applying an "actual knowledge" standard to the hospital's conduct regarding the overpayment instead of the 1986 FCA amendments' "gross negligence" standard of liability. However, the appellate

court held that it could not grant summary judgment for the relators on the record before it and remanded for further proceedings. Disagreeing with this latter holding, a strongly worded dissent maintained that the undisputed facts before the court clearly established that the hospital's conduct satisfied the "gross negligence standard of deliberate indifference to the truth." Earlier in the litigation, the Government had accepted restitution from the hospital in an administrative settlement but would not agree that the relators were entitled to a share. The appellate court rejected the Government's argument that the relators could not recover a share because the Government had accepted "restitution" as opposed to "damages."

In November 1987, relators Covington and Sidicane filed this *qui tam* action alleging two types of wrongdoing under the federal Medicare program. First, they claimed that Sacred Heart had fraudulently recorded diagnoses to receive higher reimbursement. This "upcoding" claim was not at issue on appeal. Second, they alleged that Sacred Heart knowingly submitted false claims for payment based on an inflated reimbursement rate. This "overpayment" claim was at issue.

The overpayment began in January 1984 when Blue Cross of California, Medicare's state fiscal administrator, applied an incorrect geographical factor in computing Medicare reimbursement to Sacred Heart. Although a rural hospital, Sacred Heart was reimbursed at the higher rate of an urban hospital. The relators alleged that Sacred Heart knew of the incorrect overpayment for several years yet continued to accept and use the payments.

After investigations and negotiations, the Government attempted to settle both the overpayment and upcoding claims. With respect to the overpayment, the Government entered into an administrative settlement with Sacred Heart which required the hospital to make restitution for the amount of the overpayment. The relators asserted a right under the FCA to a percentage of the Government's recovery. The Government, howev-

er, responded that the relators were not entitled to any share because it had accepted restitution for the overpayment after concluding that Sacred Heart's conduct was not fraudulent.

The relators continued to assert their entitlement to a portion of the overpayment recovery as part of the settlement negotiations for the upcoding violations. In January 1991, the relators, Sacred Heart, and the Government executed a settlement agreement which granted the relators 20 percent of the upcoding recovery. The agreement also provided that the relators' claim to a portion of the overpayment recovery would be resolved through an expedited procedure before the district court. The issue was to be presented via "motion and stipulated facts with no discovery permitted." If the parties were unable to agree on undisputed facts, then they were to proceed "as if a motion for summary judgment had been filed under the provisions of the [Federal Rules of Civil Procedure]."

Subsequently, the expedited procedure called for in the agreement ended with the district court's determination that it could not grant summary judgment to either party because the undisputed facts did "not establish the extent of the knowledge of the Hospital, [or] whether knowingly false claims were being submitted to the U.S. Government." The court interpreted the agreement to constitute a waiver of the relators' right to proceed to trial for determination of the issue and ordered the case concluded, effectively extinguishing the relators' claim. The relators appealed.

### **Government's Acceptance of Restitution Does Not Preclude Recovery by Relators**

As an initial matter, in a succinct footnote the 9th Circuit stated: "We reject the United States' argument that the Relators could not recover because the government accepted a restitution payment as a recovery. This argument would allow the government to eliminate recovery for relators by simply characterizing the nature of the conduct."

### **Funds Paid by Mistake Can Result in FCA Liability if Recipient Knows Payments Are Improper**

The 9th Circuit therefore addressed Sacred Heart's

conduct and whether the district court applied the correct liability standard to that conduct. The appellate court clarified: "Whether Sacred Heart personnel caused the improper rate calculation is immaterial because the mere receipt and deposit of government funds known to have been paid by mistake is a false claim under the Act." Sacred Heart's liability thus depended on whether it knew that it was receiving improper overpayments.

### **District Court Applied Wrong Standard of Liability**

According to the appellate court, in finding a genuine issue of material fact regarding whether Sacred Heart satisfied the FCA's knowledge requirement, the district court "apparently considered it necessary for the relators to establish actual knowledge or fraud." However, the FCA, as amended in 1986, explicitly states that "deliberate ignorance" or "reckless disregard" of the truth satisfies the knowledge requirement.

The relators' complaint was filed after the effective date of the 1986 amendments but covered conduct that occurred both before and after that date. According to the 9th Circuit, "[t]he earlier conduct comes within the 1986 amendments if 'the nature of the [offense] involved is such that Congress must assuredly have intended that it be treated as a continuing one.'" The court concluded that Sacred Heart's acceptance of the overpayments, if proven to be reckless or deliberately ignorant, constituted a "continuing" offense under the FCA; therefore, the prospective application of the 1986 amendments' "gross negligence" standard was appropriate.

### **Majority Holds That Relators Are Not Entitled to Summary Judgment Based On Constructive Knowledge Standard**

Because the district court had applied an incorrect standard, the 9th Circuit next addressed whether the relators were entitled to summary judgment under the lower constructive knowledge liability standard. A majority of the appellate panel concluded: "[W]e are unable to determine as a matter of law that Sacred Heart acted with deliberate ignorance or with reckless disregard for the truth." According to the majority, while the relators pre-

sented evidence suggesting that hospital personnel knew they were receiving overpayments and failed to take sufficient action, this evidence was not undisputed. On the other hand, it was undisputed that the hospital's Chief Executive Officer, Wallace Flemming, undertook efforts in 1984 to inform Blue Cross that the reimbursement rate was incorrect, the hospital's Chief Financial Officer, Mario Rocha, kept track of the improper payments, and Sacred Heart wrote a series of letters to Blue Cross in 1987 regarding the incorrect payment rate -- all actions which supported the Government's argument that Sacred Heart did not act with reckless disregard for the truth. The relators "dispute whether the hospital did all that it could to deal with the overpayments," but, concluded the majority, "[t]hat determination would involve fact-based interpretations of all the events, a process that is not appropriate in deciding a motion for summary judgment."

Moreover, the majority was "concerned by important evidence" not in the record. Specifically, they did not know "how extensive the overpayments were compared to the hospital's total budget." If the overpayment was substantial, as opposed to "relatively steady but small," Sacred Heart "should perhaps have taken dramatic action quickly" as compared to the actions that were taken.

### **Strong Dissent Supports Summary Judgment for Relators**

A strongly worded dissent favored summary judgment for the relators. It maintained that the majority omitted "key portions of the factual record" and presented "an incomplete perspective on the hospital's actions." According to the dissent, the evidence showed that hospital administrators knew from the beginning about the overpayments and "were at least reasonably certain that there was an urban coding error." Despite this knowledge, "the hospital did not set the funds aside in escrow: it continued to receive, use, and earn interest on the overpayments."

The dissent pointed out that in 1984 Flemming merely called and informed Blue Cross that Sacred Heart's rate calculations differed from the fiscal intermediary's, not that the hospital was receiving overpayments. The same was true of Flemming's January 1987 letter to Blue Cross, the first written

inquiry by Sacred Heart regarding the rate problem. Yet, a year earlier Flemming had been advised by the hospital's own accountants and attorneys that the overpayment amount was significant and that Blue Cross should be informed of this in writing. Only in December 1987, after four more letters had been exchanged between Sacred Heart and Blue Cross regarding the incorrect payment rate, and shortly after the Government's *qui tam* investigation enabled Blue Cross to correct the coding error, did Sacred Heart specify to Blue Cross that the incorrect rate had resulted in inflated payments. The Government's own final investigative reports concluded that "the hospital failed to properly disclose" and "concealed the proper information from the fiscal intermediary."

The dissent noted that the district court had concluded that, under the actual knowledge liability standard, affirmative actions of concealment were required: "The court, applying the incorrect actual knowledge or fraud standard, thus refused to grant summary judgment to the relators because of a factual dispute regarding whether the hospital defendants committed actual fraud by affirmatively concealing the urban-rural coding error and resulting overpayments." However, the dissent asserted, "[t]he factual issues that create a dispute regarding actual fraud are not sufficient to create a dispute regarding the much lower liability standard of 'gross negligence' required under the Act."

The dissent disagreed with the majority's view that further fact finding was necessary. Instead, the dissent concluded that the facts were sufficient to show that Sacred Heart did not commit an "innocent mistake" or "mere negligence," but rather "knowingly refrained from advising their fiscal intermediary of significant overpayment." In short, "[t]his behavior clearly satisfies the gross negligence standard of deliberate indifference to the truth."

### **District Court Erred in Interpretation of Settlement Agreement**

With regard to the settlement agreement, the 9th Circuit panel unanimously held that the district court had erred in interpreting the agreement to preclude further consideration of the relators' claim on the merits. The appellate court was

“unwilling to cut off traditional resolution of factual disputes through some type of trial in the absence of clear indication that the parties did not necessarily desire to resolve the dispute on the merits.” The court did not consider general language in the settlement agreement indicating that the parties wished to avoid litigation to mean that they had agreed that the Government would prevail if the relators could not obtain summary judgment. While the parties wanted to minimize litigation, “they did not expressly preclude further proceedings if their efforts at an expedited resolution failed.” Added the court: “Such a result is grossly unfair to the Relators, and we discern no reason to attribute such an intention to their Agreement.” In conclusion, the court stated: “Because we have declined to decide the issues in this case as a matter of law, we remand so that they may be resolved by a factfinder at trial.”

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## Dischargeability of Fraud Settlement in Bankruptcy

*U.S. v. Spicer, 57 F.3d 1152 (D.C. Cir. June 30, 1995)*

**A real estate broker who admitted to making false statements in order to obtain FHA-insured mortgages for otherwise ineligible home buyers could not discharge in bankruptcy the \$339,000 he agreed to pay the Government in settlement of civil fraud claims. While the broker argued that his settlement agreement with the Government represented an ordinary contractual obligation, the D.C. Circuit held that the agreement did not transform the debt, which was obtained by fraud and otherwise nondischargeable under the bankruptcy code, into an ordinary dischargeable debt.**

In October 1989, Spicer admitted as part of a guilty plea to having intentionally overstated to the Department of Housing and Urban Development (HUD) the down payment made by a home buyer seeking an FHA-insured mortgage. Although convicted of only one count, Spicer stipulated to simi-

lar misrepresentations on 81 mortgage applications. Buyers of 43 of the 81 properties ultimately defaulted, resulting in a HUD loss of \$1.8 million. Consequently, the district court ordered Spicer to pay \$340,000 in restitution, an amount equal to the profits he earned from the misrepresentations. Subsequently, Spicer reached a settlement agreement on civil FCA claims and promised to pay the Government \$339,000 plus interest over a 10 year period.

In July 1992, Spicer filed a voluntary Chapter 7 bankruptcy petition seeking to discharge the debt he owed to the Government. In response, the Government sought from the court a determination that the \$339,000 debt was nondischargeable under 11 U.S.C. §523(a)(2)(A) as “debt for money [or] property . . . obtained by . . . fraud.” The bankruptcy court granted the Government’s motion for summary judgment, and the district court affirmed.

## Debt Obtained by Fraud Remains Nondischargeable Despite Settlement Agreement

On appeal, Spicer argued that the district court had erred in characterizing his debt as one “for money or property obtained by fraud,” relying on the 7th Circuit decisions Maryland Casualty Co. v. Cushing, 171 F.2d 257 (7th Cir. 1948), and Matter of West, 22 F.3d 775 (7th Cir. 1994). Under the 7th Circuit view, the settlement agreement releases the underlying tort claim for fraud, thereby replacing the parties’ original rights and obligations with new ones. The post-settlement debt is merely an ordinary contractual obligation involving a promise to pay in exchange for a promise to forego certain legal claims.

The D.C. Circuit expressly rejected the 7th Circuit view, finding that it “improperly elevates legal form over substance.” The D.C. Circuit instead followed the 11th Circuit approach articulated in Greenberg v. Schools, 711 F.2d 152 (11th Cir. 1983), by which a court looks behind the legal form of the debt and ascertains whether the debt originated in fraud. According to the D.C. Circuit, the weight of recent authority follows Greenberg and rejects the 7th Circuit approach as being contrary to the public policy embodied in the bankruptcy code. That pol-

icy seeks to prevent fraudulent debtors from escaping their obligations at the expense of innocent defrauded creditors. In short, the appellate court stated, “[a] fraudulent debtor remains a fraudulent debtor, and debt originating in fraud remains nondischargeable even if its legal form changes under a settlement agreement.”

### **Defendant’s Fraud Proximately Caused Financial Losses to HUD**

Spicer also argued that the bankruptcy court and district court improperly applied an incidental “but for” causation test to find his misrepresentations responsible for HUD’s \$1.8 million loss due to defaults on the fraudulently obtained mortgages. He argued that the defaults were “proximately caused” by a variety of factors, such as the homeowners’ financial problems, that were beyond his control. Although the court agreed that the standard for nondischargeability is that the debt is “proximately caused” by the debtor’s fraud, it found that Spicer’s misrepresentations were more than an incidental “but for” cause of the losses. Rather, the defaults were a foreseeable consequence of Spicer’s conduct. As long as Spicer’s misrepresentations were a material and proximate cause, they need not have been the sole factor causing HUD’s losses. Summarizing, the court stated:

It is undisputed that Spicer intentionally misrepresented buyers’ downpayments in order to induce HUD to approve FHA-insured mortgages for parties who otherwise would not qualify; without evidence of adequate down payments, HUD would have rejected the applications, calculating the risk of default too high. HUD went for Spicer’s bait, and suffered massive losses when the buyers subsequently defaulted.

Accordingly, the D.C. Circuit affirmed the lower court’s ruling that Spicer’s misrepresentations proximately caused HUD’s losses.

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## **Filing and Service Requirements**

*U.S. ex rel. Pilon et al. v. Martin Marietta Corporation and General Electric Company*, 60 F.3d 995 (2nd Cir. July 25, 1995)

**Failure to comply with the filing and service requirements of the FCA warrants dismissal of *qui tam* claims with prejudice, according to the 2nd Circuit. Because the plaintiffs’ failure to comply “incurably frustrated” the statutory objectives underlying these provisions, the appellate court modified the district court’s previous dismissal without prejudice. The plaintiffs were not barred, however, from pursuing a §3730(h) retaliatory discharge claim, which is not subject to the same procedural requirements.**

Pilon, a former General Electric (GE) employee, and his wife alleged the submission of false claims by GE in connection with the production and delivery of radar systems and technical services to Egypt, as well as false claims for non-military specified components. (Martin Marietta is GE’s successor in interest for purposes of this action.) The plaintiffs also alleged that Mr. Pilon’s employment with GE was terminated in violation of §3730(h) of the FCA and New York labor laws.

Under §3730(b)(2) of the FCA, a copy of the complaint and written disclosure of substantially all material evidence and information the relator possesses must be served on the Government. The complaint must be filed in camera, remain under seal for at least 60 days, and not be served on the defendant until the court so orders.

In this case, the Pilon did not mark the complaint as sealed, and it was filed on the open docket. The Pilon also did not serve a copy of the complaint or written disclosure on the Government. Shortly after the complaint was filed, a reporter contacted the Pilon’s counsel, and an interview with the Pilon was arranged. The substance of the complaint was revealed in a newspaper article pub-

lished two days after the case was filed. Following the article's publication, Martin Marietta received a faxed copy of the complaint.

Given the noncompliance with the filing requirements, the defendants moved to dismiss the *qui tam* claims with prejudice for lack of subject matter jurisdiction. The defendants also moved to dismiss with prejudice the §3730(h) claim since Pilon had not alleged that he acted in furtherance of filing an FCA action prior to his discharge. Dismissal with prejudice as to the state law claim was sought on the theory of preemption by §3730(h). The New York district court dismissed the complaint without prejudice, and defendants appealed.

### **Plaintiffs' Failure to Satisfy Filing and Service Requirements Frustrated Interests Underlying Provisions**

The *qui tam* plaintiffs did not dispute their failure to comply with the Act's procedural requirements. Rather, they pointed to their counsel's assertion that he had tried to tell the court clerk that certain sealing requirements applied. They further maintained that not serving the Government was excusable because the Government was already aware of their allegations.

Citing legislative history of the 1986 FCA amendments, the 2nd Circuit noted that the seal and service provisions were intended to give the Government an adequate opportunity to evaluate the private action, determine if the suit involved matters the Government was already investigating, and decide whether to join and take over the litigation. Another objective was to prevent defendants from having to respond to complaints without knowing whether the Government would pursue the action. In addition to legislative history, the court cited other interests, including providing a certain degree of protection for the defendant's reputation until the Government has had the chance to review the claims and the possibility that a defendant might agree to a quick and valuable settlement with the Government to avoid the unsealing.

Siding with the defendants, the 2nd Circuit stated that the Pilons' failure to comply with the service and filing provisions "incurably frustrated all of

these interests." Added the court: "That the government and Defendants may have been aware of the substance of the Pilons' allegations does not diminish the consequences of the Pilons' failure to comply with the statutory requirements."

Finding the district court's dismissal of the *qui tam* claims without prejudice to be an abuse of discretion, the 2nd Circuit modified the lower court's ruling to specify dismissal with prejudice. In affirming the judgment as modified, the court noted that it did not need to address whether the filing and service requirements were jurisdictional in order to resolve the matter.

### **Plaintiffs Barred Only from Further Pursuit of *Qui Tam* Claims, Not Retaliatory Discharge Claim**

With respect to the retaliatory discharge claim, the 2nd Circuit let stand the district court's dismissal without prejudice. The court observed that §3730(h) claims (as well as state law claims) are not subject to the procedural requirements of §3730(b)(2). Moreover, the lower court had not addressed the merits of Mr. Pilon's retaliatory discharge claim. Therefore, the 2nd Circuit ruled that the plaintiffs were barred only from pursuing their *qui tam* claims, not the §3730(h) retaliation claim.

***U.S. ex rel. Windsor v. DynCorp, Inc. et al.*, 1995 WL 475811 (E.D.Va. Aug. 9, 1995)**

See "*Davis-Bacon Act Violations*" below in this section.

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## Limitation by Relator of Government Communication with Defendant

*U.S. ex rel. Pentagen Technologies International Limited v. CACI International Inc. et al., 1995 WL 404857 (S.D.N.Y. July 6, 1995)*

A relator cannot prevent the Government from communicating with a defendant in a *qui tam* suit in which the Government has declined to intervene, ruled a New York district court. According to the court, while a *qui tam* relator is empowered as a private prosecutor, it is not empowered to replace the Government. Allowing the relator Pentagen to limit communication between the Government and the defendants would unconstitutionally expand a relator's power beyond that authorized in the FCA. Pentagen's motion to enjoin such communication was therefore denied. In addition, the court denied Pentagen's motion to enjoin further performance of the defendants' government contract.

Pentagen Technologies International Inc. (Pentagen) brought a *qui tam* suit alleging FCA violations in connection with a U.S. Army contract for the modernization of installation information management systems under the Sustaining Base Information System (SBIS) Program. The Government did not intervene in the action.

Pentagen alleged that the defendants violated the FCA by entering into the SBIS contract and submitting claims for payment even though they knew or should have known that they did not have suitable software to perform the contract services or to achieve the contract targets. The defendants responded that the provisions Pentagen claimed were breached were not part of the final SBIS contract but instead merely statements made during the "request for proposal" process.

Pentagen further maintained that the Army should have modified or rebid the contract because the defendants were unable to perform, and that the defendants were knowingly presenting false claims since they knowingly were not performing. The defendants countered that the Government was the administrator of its own contracts and, because the Army had decided not to modify the SBIS contract, they were obligated to continue performance and thus entitled to receive payment.

Before the district court were several motions by Pentagen for injunctive relief. Specifically, Pentagen moved to enjoin: (1) the Department of Defense and its counsel from communicating with the defendants regarding issues raised in the lawsuit; and (2) the defendants from receiving payments under the SBIS Program, or (3) all further activities under the SBIS Program, pending final resolution of the litigation.

### Injunction Against Communication Denied

The district court found "absolutely no basis" for enjoining communication between the Government and the defendants. Pentagen had argued that as a relator it had replaced the Government's counsel; therefore, under the rules of ethical conduct, direct communication between the defendants and the Government should be prohibited. The court, however, agreed with the defendants that the Government was not "Pentagen's client" and that Pentagen could not "expropriate the government's power or prohibit communications." The court explained: "While Congress has made it clear that *qui tam* relators should be able to effectively bring civil suits under the FCA, it does not follow that once the government has decided it will not intervene, it is relegated to the position of the relator's client."

According to the court, "[w]hile the *qui tam* relator is empowered as a private prosecutor, it is not empowered to replace the government." Nothing in the FCA prohibits the Government from communicating with the defendants or gives the relator power over the conduct of government officials. Further, Pentagen failed to show how such communication "would interfere with Pentagen's right to conduct the lawsuit or limit Pentagen's status."

Also, the court noted, such communication is common in FCA actions where the Government has not intervened.

Moreover, the court asserted that limiting the Government's right to communicate with defendants "would raise serious constitutional issues." Where the constitutionality of the *qui tam* provisions has been challenged, "the courts have concluded that the relator's power is permissible because it does not trump that of the executive branch." Allowing the relator to control government communication "would be expanding the relator's power beyond that specifically authorized by the FCA, and would therefore be unconstitutional."

### **Injunction Against Payments and Performance Under SBIS Contract Denied**

Pentagen claimed that, without an injunction against future payments or performance under the SBIS contract, there would be an irreparable injury to the public not remediable through monetary damages alone. In particular, Pentagen contended that, if an injunction were not granted, the FCA's purposes of punishing wrongdoers and deterring fraud would be undermined.

The district court acknowledged that the 2nd Circuit "recognizes that '[a] significant risk of irreparable harm to the public' may justify a preliminary injunction." However, the court found that Pentagen had failed to prove such harm. If the defendants were indeed defrauding the Government, the substantial remedies under the FCA would serve to punish them and deter others. Moreover, Pentagen's contention that an injunction was necessary to prevent the defendants from continuing to benefit from their false claims was "purely speculative." Pentagen had not proven that violation of the FCA by the defendants was likely, and "[i]nstead of preventing FCA violations, the injunction may in fact prevent defendants from making progress in their modernization of the Army's computer system."

The court also rejected the argument that Pentagen would suffer without an injunction because the defendants could use the SBIS contract proceeds to defend against Pentagen, which had fewer assets.

The court asserted that the defendants' alleged combined net worth of \$142 billion "render[ed] it extremely unlikely that without the contract money they would not be able to finance this litigation. Furthermore, it is difficult to see how the defendants' ability to defend themselves results in harm to Pentagen."

In short, the court concluded, without proof of irreparable injury to the public (the first requirement for a preliminary injunction), it was not necessary to analyze the other requisite factors (i.e., the likelihood of success on the merits, or the existence of sufficiently serious meritorious questions and the balance of hardships). Nevertheless, the court stated that it was clear that "the contentions on which plaintiff would rely to establish likelihood of success on the merits are too speculative for the court to make a reasoned judgment."

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### **Section 3730(h) Retaliation Claims**

*Childree v. UAP/GA Ag-Chem et al.*,  
No. 1:94-CV-1312 (N.D.Ga. June 20,  
1995)

**A contractor employee who had copied documents relating to possible fraud and stored them at home for four years, but who took no other action in furtherance of a False Claims Act lawsuit, could not recover for alleged retaliation under §3730(h), according to a Georgia district court. "The language of Section 3730(h), even broadly construed, clearly provides that Plaintiff, at a minimum, must show some nexus between her conduct and the furtherance of a potential False Claims Act action," the court stated.**

Childree's §3730(h) suit alleged that her employer fired her in retaliation for her testimony at a Department of Agriculture administrative hearing regarding efforts by agricultural companies to evade certain subsidy limitations. The defendants argued that Childree's conduct was not protected by

§3730(h) because there was no nexus between her conduct and furthering an FCA suit. No FCA action was ever filed against the defendants. Moreover, while Childree claimed that in 1989 she had questioned defendant managers about allegedly illegal practices and had copied certain documents, which she stored at home, she reportedly conceded that she did not know about the FCA nor did she disclose her information to the Government. She also conceded that she did not intend to initiate any FCA action, nor did she conduct an internal investigation. Years later, Childree's stored documents were subpoenaed by the Department of Agriculture, and she was called upon to testify in the hearing. Based on these facts, the court found that Childree failed to show any nexus between her conduct and a potential FCA lawsuit.

According to the court, Congress intended §3730(h) to help foster whistleblowing by protecting employees who engage in a broad range of conduct, as long as that conduct is in some way related to an FCA action. Moreover, §3730(h) is intended to protect those who come forward with evidence of fraud against the Government. Childree did not perform any affirmative act to expose the alleged fraud. Rather, "[a]ll Plaintiff did was copy the documents she believed to be fraudulent, took the documents home, and stored them there for four years." Finally, while the court agreed that §3730(h) should be broadly construed, it found that every case to consider the issue required some nexus between the employee's conduct and the filing or potential filing of an FCA action.

***U.S. ex rel. Lamar v. Burke and Arsenal Credit Union, 1995 WL 496983 (E.D.Mo. Aug. 21, 1995)***

**Liability for retaliatory acts under §3730(h) of the False Claims Act does not extend beyond the corporate entity to individual corporate officers, according to a Missouri district court. The court interpreted the ordinary and natural meaning of "employer" as not encompassing corporate supervisors. As a result, the retaliation count against the relator's supervisor (but not the corporation) was dismissed.**

The relator, Norman Lamar, was hired by the president of Arsenal Credit Union (ACU), William Burke, to work as a loan manager. Lamar was responsible for preparing reports to the Government, including Forms 799 for payments of interest and special allowances on guaranteed student loans. According to Lamar, he discovered that ACU was improperly seeking payments for interest and special allowances. He then informed Burke and others at the credit organization that corrected Forms 799 had to be filed to notify the Government. While corrected forms were prepared, Lamar alleged that Burke instructed him to dispose of the corrected forms. Lamar told Burke that he would not sign any more 799s unless the Government was notified of the false billings. Burke then fired Lamar for failing to sign the forms.

The FCA count was settled by the parties. On the remaining §3730(h) count against both ACU and Burke, the latter filed a motion to dismiss or, in the alternative, for summary judgment.

**Meaning of "Employer" Does Not Extend to Corporate Supervisors**

Under §3730(h), an employee is entitled to relief if he or she is discharged, demoted, or in any other manner discriminated against "by his or her employer" because of the employee's acts in furtherance of a *qui tam* action. Burke argued that he was not an "employer" within §3730(h). Rather, Lamar was employed by the business, and Burke was merely an officer, and another employee, of ACU. Calling for a liberal interpretation of remedial statutes, Lamar argued that "employer" should cover Burke because he actually fired the relator. (Yet, according to a footnote in the opinion, Lamar admitted in his deposition that he considered ACU, not Burke, to be his "employer.")

While interpretation of a statute normally begins with its plain language, the court noted that the FCA does not define "employer." Accordingly, the court looked to construe the term "in accord with its ordinary and natural meaning." By dictionary definition, an "employer" is the "owner of any enterprise (as a business or manufacturing firm)," "such an enterprise," and "an agent acting for such enterprise in employing persons." While §3730(h)

case law and other federal “whistleblower” provisions did not provide guidance as to whether “agent” or “employer” should be interpreted to include an officer of a corporation, case law relating to Title VII of the Civil Rights Act of 1964, 42 U.S.C. §2000e et seq., did provide some instruction. The court pointed out that that statute includes language similar to §3730(h) and both laws have a remedial purpose.

Unlike the FCA, Title VII does define “employer” -- as “a person [including individuals and corporations] engaged in an industry affecting commerce who has fifteen or more employees ...and any agent of such person.” Although courts are divided regarding whether corporate supervisors are subject to individual liability under the Title VII definition of “employer,” the instant court and others in the district “consistently have found persuasive those decisions rejecting the personal liability of individual supervisors under Title VII.” Additionally, the 8th Circuit, in construing analogous provisions in the Missouri Human Rights Act, had recently looked with approval to those courts ruling that supervisors and other employees cannot be liable under Title VII in their individual capacities. The Burke court concluded:

This Court finds persuasive the reasoning of those courts holding that Title VII does not impose individual liability on corporate supervisors. The definition of ‘employer’ under Title VII is broader than that word’s ordinary and natural meaning: Title VII extends to ‘any agent’ while the dictionary definition of ‘employer’ includes only those agents ‘acting for such enterprise in employing persons.’ Yet, the cases cited ... interpret the Title VII definition as not extending to corporate supervisors. As such and in light of the similar remedial purposes behind Title VII and ‘whistleblower’ provisions generally, this Court will interpret the ordinary and natural meaning of ‘employer’ as not extending to corporate supervisors.

Accordingly, the court granted Burke’s motion, and the complaint was dismissed as against him with prejudice.

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## Third Party Indemnification Claims

*U.S. ex rel. Public Integrity v. Therapeutic Technology Inc. et al.; Therapeutic Technology Inc. et al., Third-Party Plaintiffs v. HNE Healthcare, Inc., Third-Party Defendant, 1995 WL 480594 (S.D. Ala. Aug. 7, 1995)*

***Qui tam* defendants Therapeutic Technology Inc. (TTI), a medical equipment provider, and its president, Charles Moody, were not allowed to bring a third party claim for indemnification against HNE Healthcare, Inc. (HNE), the manufacturer of lymphedema pumps at issue in the suit. TTI and Moody sought to have the court exercise supplemental jurisdiction over their indemnification claim based on state law causes of action. Finding that Congress did not intend to create a right to bring claims that would have the effect of offsetting FCA liability, an Alabama district court held that supplemental jurisdiction was not warranted.**

In February 1993, Public Integrity filed a *qui tam* suit alleging that TTI and its president, Charles Moody, knowingly made claims for lymphedema pumps and related equipment that were not qualified for coverage under Medicare or Medicaid and were not medically necessary. After more than a year of investigation, the Government intervened in the suit and filed an amended complaint. Defendants TTI and Moody then filed a third party complaint against HNE, the pump manufacturer. The third party claims were based solely on state law causes of action, including breach of contract, breach of warranty, and fraud. Essentially, TTI and Moody sought indemnification from HNE for any FCA damages they had to pay the Government. The Government moved to dismiss the third party complaint.

## No Right of Action for Indemnification Under FCA

In granting the Government's motion, the court noted that it maintains discretion to reject supplemental jurisdiction if "there are other compelling reasons for declining jurisdiction" and that it should be guided by considerations of "judicial economy, convenience, and fairness to the litigants." In reaching its conclusion, the court followed prior FCA cases holding that "Congress did not intend to create a right of action for contribution or indemnification under the FCA." The purpose of the FCA damages provision is to "deter future fraudulent claims, as well as recoup the government's losses due to fraud. The FCA is in no way intended to ameliorate the liability of wrongdoers by providing defendants with a remedy. . . ."

## Indemnification Contrary to Purposes of FCA

Moreover, the Government cited other important factors favoring dismissal of the third party claims. Allowing them to stand would interfere with the Government's efforts to recover against parties ultimately responsible for submission of false claims and would shift the focus of litigation to allocation of fault. Additionally, dismissal would not result in prejudice against the defendants. TTI and Moody, if found liable under the FCA, could still file an action against HNE in state court. If the defendants were not found liable, no indemnification claims would exist. Furthermore, the third party claims would unduly complicate and prolong the litigation, subverting the goals of efficiency and convenience which underlie supplemental jurisdiction. In sum, the court reasoned that "embroiling the Court and the government's case" in a state law dispute was "clearly contrary to the purposes of an FCA suit."

## Anti-Kickback and Self-Referral Violations

*U.S. ex rel. Pogue v. American Healthcorp, Inc. et al., Memorandum and Order, No. 3-94-0515 (M.D.Tenn. Sept. 14, 1995)*

**A *qui tam* relator who alleged that Medicare providers knowingly violated federal anti-kickback and self-referral statutes failed to state a claim under the False Claims Act, according to a Tennessee district court. While the court found that a general release previously executed between Pogue and two of the defendants did not prevent Pogue from pursuing a *qui tam* case, the court dismissed Pogue's suit which alleged that a group of physicians, treatment centers, and a hospital were involved in a scheme to refer Medicare and Medicaid patients in violation of anti-kickback and self-referral laws.**

The relator Pogue filed a *qui tam* suit against his former employer Diabetes Treatment Centers of America, Inc. (DTCA), its parent company American Healthcorp, Inc. (AHC), West Paces Medical Center (West Paces), five individual physicians, and a number of John Doe defendant hospitals and physicians. Pogue alleged that the claims submitted by the defendants were false because they were submitted in knowing violation of Medicare and Medicaid anti-kickback and self-referral statutes. Had the Government been aware of these violations, the defendants would not have been able to participate in Medicare and Medicaid programs. According to Pogue, by submitting claims to the Government, the defendants fraudulently implied that they had not violated federal laws so as to warrant program exclusion. In response, the defendants filed a motion to dismiss pursuant to F.R.C.P. 12(b)(6) for failure to state a claim upon which relief can be granted or, in the alternative, a motion for summary judgment, arguing that the general release of claims previously signed by Pogue prohibited him from bringing a *qui tam* action.

## **Court's Stated Elements for FCA Claim Appear at Odds with Precedent**

In considering the 12(b)(6) motion, the court articulated the standard for dismissal as twofold. First, the claim may be dismissed “only if it is clear that no relief could be granted under any set of facts that could be proved consistent with the allegations.” However, Rule 12(b)(6) also requires the “plaintiff to plead facts sufficient to establish all of the essential elements of the doctrine under which he seeks relief.”

According to the court, the elements necessary to establish a claim under the FCA were set forth by the Federal Circuit in Young-Montenay, Inc. v. United States, 15 F.3d 1040 (Fed. Cir. 1994), as follows: (1) the presentation or causing the presentation of a claim; (2) the falsity of the claim; (3) defendant's knowledge of its falsity; and (4) damages to the United States as a result of the false claim. (*The Young-Montenay court actually listed these four elements as necessary to recover damages for violation of the FCA. This position is consistent with the generally accepted rule that it is not necessary to show actual damages to establish liability under the Act. See U.S. ex rel. Hagood v. Sonoma County Water Agency*, 929 F.2d 1416, 1421 (9th Cir. 1991); *U.S. ex rel. Marcus v. Hess*, 63 S.Ct. 379 (1943).) The court found that Pogue “failed to allege facts that, even if true, would be sufficient to prove either the second or fourth element.”

## **Violation of Anti-Fraud and Abuse Statutes Not Necessarily a False Claim, Nor Does It Injure Government**

In the view of the court, Pogue had failed to allege that any of the submitted claims were themselves false. Nor had he alleged that the “services were unnecessary, not rendered, or that there was some other miscalculation with regard to the care provided to the patients.” Even if the claims were knowingly submitted in violation of the anti-kick-back and self-referral statutes, that would not make the claims themselves false, the court said. (*Pogue has filed a motion for reconsideration which points out that the Tennessee court's ruling is contrary to that previously reached by an Ohio district court in U.S. ex rel. Roy v. Anthony*, 1994 U.S. Dist. LEXIS 9768 (S.D. Ohio July 14, 1994).)

Moreover, the court found that, even if the claims were considered false or fraudulent, Pogue “failed to prove that the government was injured by the submission of these claims.” Assuming that the services rendered were necessary (Pogue did not allege otherwise), the patients would have been treated at some hospital, even if not the defendant hospital. By the court's reasoning, the Government suffered no injury because the Government pays the same amount for treatment regardless of where it is rendered. The court thus concluded that Pogue had failed to allege facts sufficient to support a claim under the FCA.

## **Enforceability of Release is Determined by Balancing Test**

On defendants' summary judgment motion, the district court addressed whether an agreement settling employment related issues, which also included a general release of claims, prohibited the relator from bringing a *qui tam* action. The court assumed that the release encompassed the relator's right to bring a *qui tam* suit but ruled that it was unenforceable as against public policy. In so doing, the court adopted the view recently expressed in U.S. ex rel. Green v. Northrop Corporation et al., 59 F.3d 953 (9th Cir. July 12, 1995). See “*Prefiling Release of Qui Tam Claim*” above in this section.

## **Public Interest in Protecting the Treasury Outweighs General Interest in Enforcing Agreements**

According to the district court, with the *qui tam* provisions, Congress intended to “set up incentives to supplement government enforcement of the Act.” This purpose would be subverted by upholding releases of *qui tam* claims. The court rejected the defendants' contention that the FCA's purposes would not be frustrated by upholding such a release because the Government could still bring an action of its own. Instead, the court reasoned, if the “prevailing rule were that pre-filed releases were enforceable, the government may not ever become aware of allegations of fraud in the first place.” Accordingly, such a precedent would frustrate the purposes of the FCA.

The balancing test for determining the enforceability of the release required the court to “weigh the

interest of the public in protecting the national treasury and deterring fraud against the public policy of enforcing agreements and encouraging settlements.” The court found that the “substantial interest” in preventing fraud outweighs the “general interest” in enforcing agreements, and thus “pre-filing releases of *qui tam* claims . . . cannot be enforced to bar a subsequent *qui tam* claim.” Accordingly, the agreement signed by Pogue could not be enforced to bar his *qui tam* claim.

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## Davis-Bacon Act Violations

*U.S. ex rel. Windsor v. DynCorp, Inc. et al.*, 1995 WL 475811 (E.D. Va. Aug. 9, 1995)

**Alleged misclassification of workers under the Davis-Bacon Act does not constitute “false claims” under the FCA, according to a Virginia district court. Rather, responsibility for resolving worker classification disputes rests with the Department of Labor, not with the courts. The district court also held that the failure to submit required payroll reports did not subject the delinquent contractor to FCA liability.**

In July 1994, Windsor filed a *qui tam* suit alleging various FCA violations by DynCorp in connection with its fixed price contract with the U.S. Army for general repair, preventive maintenance, and construction services at Fort Belvoir, a military base in Virginia. Windsor had been DynCorp’s electric shop foreman at Fort Belvoir until April 1993, when he was fired for “insubordination” after voicing concerns to DynCorp’s upper management about the issues that later formed the basis of his *qui tam* complaint.

Windsor’s complaint alleged that DynCorp: (1) falsely represented to the Government that it was paying wages in compliance with the Davis-Bacon Act, when in fact it was violating the Act’s reporting and wage requirements; (2) fraudulently billed the Government for preventive maintenance services never actually performed; and (3) failed to perform

certain quality control measures required under the contract. DynCorp sought summary judgment on all three counts.

DynCorp’s contract contained a Davis-Bacon Act wage rate provision that subjected it to the statute’s wage and reporting requirements. The Davis-Bacon Act “is a protective labor law” that requires certain federal contracts to incorporate government-determined minimum wages to be paid to various classes of laborers and mechanics. In addition to the specified wages, Department of Labor regulations require that the contractor maintain detailed payroll records. Copies of these records must be submitted to the contracting agency on a weekly basis, along with a statement certifying that the payroll information is correct and complete and the workers have been paid at least the applicable wage rate for the classification of work performed. Falsification of these certifications may subject the contractor to FCA liability.

It was undisputed that DynCorp did not submit the required certified payroll reports from 1991 to 1993, and the reports it submitted to the Army in 1994 were untimely. Further, while DynCorp’s records accurately reflected the wages paid to its workers, Windsor presented an expert affidavit stating that, in certain instances, DynCorp misclassified workers and therefore paid wages that were legally deficient. For example, Windsor’s expert concluded that certain employees classified as “Laborers” should have been classified as “Electricians” or “Carpenters” based on Department of Labor policy regarding the work they were performing. Classified as such, these workers would have been entitled to higher wages.

### **Failure to Submit Required Payroll Reports Alone Doesn’t Trigger FCA Liability**

The district court first concluded that DynCorp’s delinquency in submitting certified payroll reports, though violative of the Davis-Bacon Act and subject to that Act’s penalties, did not constitute a false claim under the FCA. The court reasoned that there was “simply no falsity, no misrepresentation” by DynCorp. After all, the Government was aware it was not receiving weekly reports from DynCorp

and could have taken steps to enforce compliance. Moreover, the court added, the failure to submit reports was not a “claim” within the meaning of the FCA. “There is simply no logical nexus between the failure to submit reports, by itself, and economic injury to the government.”

### **Allegation That Contractor Misclassified Workers Doesn’t State Claim Under FCA**

The court next addressed “[t]he more significant question” of “whether Windsor’s contention that DynCorp intentionally misclassified, and thereby underpaid, certain workers, combined with DynCorp’s continued billing of the Army for the full contract price (which incorporated Davis-Bacon wage rates), states a claim under the FCA.” The court noted that a statement by a contractor that it is paying Davis-Bacon wages, when it knows otherwise, is of course false. However, to be a “false claim” under the FCA, “the putative false statement must have the purpose and effect of ‘causing financial harm to the Government.’”

Therefore, according to the court, whether an intentional false statement regarding payment of Davis-Bacon wages constitutes a “claim” depends on the nature of the underlying contract and, specifically, “on whether the amount of the government’s payments under the contract is in some sense tied, or related, to the amount the contractor pays its workers.” Under the “fixed price” contract in this case, despite a somewhat “attenuated connection” between actual labor costs and contract price, “there would nonetheless be a loss to the government if DynCorp intentionally paid its workers lower wages than were due by misclassifying them.” This is so, explained the court, because in all Davis-Bacon Act contracts the Government pays the contractor more in order that the workers be paid more.

Nevertheless, the district court granted summary judgment for DynCorp because (1) whether DynCorp submitted a false claim could not be determined without first determining whether DynCorp actually misclassified its employees, and (2) the governing regulations place the responsibility for resolving worker classification disputes with the Department of Labor, not with the courts. The court clarified that “the Davis-Bacon Act by no means precludes or preempts all FCA suits for false claims that happen also to be Davis-Bacon Act vio-

lations.” Instead, “[w]here the contractor’s statement may be determined to be false without regard to complex Davis-Bacon Act classification regulations, then a Davis-Bacon Act violation may form the basis of an FCA suit.” For example, an FCA action may be viable if, unlike in this case, a contractor misrepresents the wages actually paid or lies about the frequency with which its employees receive paychecks.

### **Billing for Services Not Performed Not an FCA Violation in This Unusual Situation**

Windsor’s complaint also alleged that DynCorp billed the Government the full monthly contract price even though certain required preventive maintenance services were never performed or completed. DynCorp conceded that this was true. The district court found, however, that DynCorp “nonetheless offered substantial, unrefuted evidence that negates any FCA claim.”

Specifically, the evidence showed that over time the contract became outdated and did not accurately reflect existing conditions at Fort Belvoir. As such, it was impossible for DynCorp to provide some of the contractually required services. At the same time, new services not in the contract had to be performed. The Army was aware of these deficiencies in the contract, and, while contract modifications were being considered, the Army and DynCorp mutually agreed that (1) DynCorp would continue to bill the fully monthly contract price regardless of the work actually performed, and (2) payment would be adjusted based on reports from DynCorp regarding the services actually provided and subsequent negotiations regarding the value of these services.

In short, the court noted that “this case presents the somewhat unusual circumstance where a contractor’s submission of an invoice covering work not actually performed does not constitute a false claim.” The Army was “fully cognizant of the billing situation,” and Windsor did not produce any evidence that DynCorp ever misled the Government regarding the work it had performed.

## Summary Judgment Also Granted on Quality Control Count

Windsor also alleged that DynCorp defrauded the Government by not performing “quality control” random sampling and inspections of its preventive maintenance services. The court, however, found that there were no set requirements for inspections and the degree to which DynCorp was to perform quality control on preventive maintenance services “was fairly flexible.” Windsor did not provide any specific evidence regarding contractual requirements for random sampling or the manner in which DynCorp fell short of these requirements, or “that DynCorp misled the government into believing that it had performed quality control in a given instance, when in fact it had not.”

## Summary Judgment Inappropriate for Alleged Violation of Statutory Seal By Relator

As an initial matter, DynCorp had urged that the case be dismissed because Windsor had violated the statutorily mandated seal while it was in effect. Specifically, DynCorp alleged that Windsor had disclosed the allegations underlying his *qui tam* suit to at least three DynCorp employees. Windsor denied this allegation.

The court noted that the *qui tam* seal procedures “reflect Congress’ desire to permit the government to investigate the allegations without ‘tipping off’ the alleged wrongdoers while protecting defendants from damaging reputational injuries associated with possibly baseless public accusations.” Further, *Erickson v. American Institute of Bio. Sciences*, 716 F.Supp. 908, 912 (E.D.Va. 1989), held that dismissal was the appropriate remedy where the relator not only neglected to file the complaint in camera and under seal but also immediately served the defendant with a copy.

DynCorp contended that, as in *Erickson*, dismissal of this case was warranted. Windsor argued that, even assuming that he had disclosed certain information about the suit to some individuals, dismissal was inappropriate because no publicity resulted and the Government’s investigation was not obstructed.

The court concluded that whether Windsor’s disclosures actually occurred and, if so, whether they warranted dismissal were matters requiring further fact finding. The court clarified: “To be sure, not every technical or minor, remediable violation of the seal requires automatic dismissal of a *qui tam* action.” For example, disclosing merely the existence of the *qui tam* action “to a spouse or other disinterested party. . . may not justify the harsh remedy of dismissal. On the other hand, where, as here, the relator is alleged to have made improper disclosures to the defendant’s own employees, the severity of the dismissal remedy may well be warranted.”

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## Falsity of Claim

*U.S. ex rel. Hindo v. University of Health Sciences/The Chicago Medical School*, 1995 WL 527203 (7th Cir. Sept. 6, 1995)

**A university did not make a false claim by submitting an invoice to a medical center for reimbursement of radiology residents’ costs where the residencies ended up not being funded by the Veterans Administration as expected, the 7th Circuit ruled. The court found neither a false statement nor a purposeful scheme by the University to defraud the Medical Center and the Government.**

This case arose from false billing allegations by Walid Hindo, former Chairman of the Department of Radiology for the University of Health Sciences/The Chicago Medical School (University) and staff member at the North Chicago Veterans Administration Medical Center (Medical Center or Center). According to Hindo, the University defrauded the Government when it sought from the Medical Center reimbursement for the salaries and benefits paid by the University to radiology residents who worked at the Medical Center but for whom funding had not been approved by the Veterans Administration (VA). The Government declined intervention in the action.

After the *qui tam* complaint was served on the University, Hindo filed an amended complaint adding a new §3730(h) count alleging that the University threatened to terminate his tenure and discharged him as Department Chairman for reporting the fraudulent billing to the Medical Center. Following the discovery cut-off date and while the University's motion to dismiss was pending, Hindo sought leave to file his second amended complaint, which added allegations of harassment in "retaliation" for reporting the fraud. The district court denied Hindo's motion and subsequently granted the University's motion to dismiss the §3730(h) claim. The University had contended that Hindo's prior unsuccessful state retaliatory discharge action had preclusive effect. On the underlying claim, the district court granted a directed verdict and entered judgment for the University, which had argued that Hindo's evidence confirmed that the University had not made any false claims.

The 7th Circuit observed that this case was strongly dependent on the facts. To summarize: The University's medical school is affiliated with the Medical Center. While the University is privately run, the Medical Center is funded by the VA. During the relevant time period, the University and the Medical Center operated under a Disbursement Agreement whereby the University paid salaries and benefits directly to residents and the Medical Center reimbursed the University the cost of the residents. Part of the invoicing and payment process for residents involved verification by a Medical Center accountant that the VA had funded each residency position.

### **Circumstances of Hindo's Claim**

Having been granted temporary funding for two radiology residencies for the 1988-89 academic year, the Medical Center reapplied for the following academic year in mid-1988. Permanent funding was denied by the VA, and the Medical Center submitted its appeal after the deadline passed. The VA, however, placed the Center's request on a "waiting list for temporary resident positions" and promised funding if resources became available. According to the 7th Circuit, this missive gave the Medical Center "a certain degree of optimism for the 1989-

90 academic year which they were loathe to relinquish short of a definite and final denial of their plea for funding." The court also cited "other expressions of optimism for funding," including minutes of Medical Center committee meetings and a May 1989 VA letter to the Center indicating the possibility of temporary resident positions for the upcoming year.

In July 1989, two radiology residents began work at the Medical Center. When the University submitted its bills to the Center, no representation was made as to whether funding from the VA had been obtained for these residencies. Without verifying VA funding, the Center approved the invoices for the radiology residents, paying more than \$45,000. Subsequently, the Medical Center discovered that it had not received funding for radiology residencies and had improperly paid for those services. After determining it could not receive after-the-fact funding, the Center demanded a refund from the University by way of letter, and the University agreed to an offset of future payments.

### **University's Invoice for Reimbursement Not A False Claim**

In the central discussion of the opinion, the 7th Circuit addressed the elements of FCA liability and showed why they were not present on these facts. Under §3729(a), liability exists if one "knowingly presents" to the Government "a false or fraudulent claim for payment." "Knowingly," in turn, means the person or entity (1) had actual knowledge of the information; (2) acted in deliberate ignorance of the truth or falsity of the information; or (3) acted in reckless disregard of the truth or falsity of the information. In contrast, the 7th Circuit explained, innocent mistakes or negligence are not actionable under this section. Quoting *U.S. ex rel. Hagood v. Sonoma County Water Agency*, 929 F.2d 1416, 1420 (9th Cir. 1991), the court stated: "[W]hat constitutes the offense is not intent to deceive but knowing presentation of a claim that is either fraudulent or simply false. The requisite intent is the knowing presentation of what is known to be false."

Hindo argued that the invoice for the radiology residents constituted a false claim because the

University knew that the Medical Center had not obtained funding for the residencies. He contended that the falsity was an implied representation by the University in each invoice that the Medical Center had in fact obtained funding. The 7th Circuit found that such an argument “distorts the record produced at trial and misapprehends the law.” Rather, there was nothing false in the invoices -- the residents had performed the work listed there, and no one said otherwise. The court distinguished these invoices from those where a representation is made, for example, that a resident worked five days a week at a hospital when he worked only three.

In the absence of a false statement, the 7th Circuit looked for “some purposeful scheme” by the University to defraud the Medical Center and ultimately the Government. The court maintained that, even reading the scienter requirement at its broadest, it could not find that Hindo had set forth a claim. The court noted that the University and Medical Center shared a vested interest in obtaining funding and the Medical Center fought hard to secure funding from the VA as well as alternative sources. Moreover, throughout the process the VA expressed optimism to both the Medical Center and University that funding might come through. In sum, said the 7th Circuit: “No legitimate reading of the record can support an inference that any party involved here knew that the possibility of funding was foreclosed.”

In fact, added the court, “[f]ar from an instance of deceit and skullduggery, the handling of this situation by the University and the Medical Center evidences a spirit of compromise and accommodation that belies any fraudulent motive.” The University had based its decision to hire the residents on the VA’s statement that there was legitimate reason to believe funding would become available. The University knew there was a chance it would have to pay the residents out of its own pocket even though they would be working the entire academic year at the Medical Center. Still, the VA, through the Medical Center, led it to believe funding might come even after the residents started working full-time at the Center. Under the circumstances, according to the court, “[i]t was not unreasonable and certainly not fraudulent for the University to

include reimbursement for these residents’ costs in its invoice to the Medical Center.”

As for the Medical Center, the 7th Circuit pointed out that it actively worked to secure funding and through its efforts contributed to the University’s belief that funding might become available. Additionally, according to the court, when the University invoiced the residents’ costs, the Medical Center was in the best position to determine whether funding had been obtained. In fact, the Medical Center had procedures in place to verify that very information. In short, the court asserted: “Considering that the Medical Center had ready access to the necessary information and that the University assumed all the risk of securing the residents upon the Veterans Administration’s assurances, it is difficult to paint the University as a defrauder.”

The 7th Circuit further noted that the Government suffered no harm and the Medical Center benefited from the services of two full-time radiology residents at no cost. Once the \$45,000 “bookkeeping error” was discovered, it was quickly remedied. Given the Government’s decision not to pursue the action and the Medical Center’s apparent satisfaction with how the matter was resolved, it appeared to the court that no party involved believed any harm was done.

In concluding that there was no false claim or fraud, the court stated that, at most, the University was perhaps negligent in not determining whether funding had been approved before it invoiced the Medical Center. Because negligence is not actionable under the FCA, however, Hindo’s claim necessarily failed.

### **Letter Between Two Private Parties Not A Public Disclosure**

The 7th Circuit rejected the University’s argument that the district court lacked jurisdiction under §3730(e)(4)(A) of the Act. In raising the bar, the University claimed that the letter it received from the Medical Center was a public disclosure and that Hindo was not an original source of the disclosure.

Explaining that the Act seeks to encourage private individuals who are aware of fraud to bring infor-

mation forward, the 7th Circuit stated that §3730(e)(4)(A) must be “read conjunctively” and the bar is to be invoked “only when each and every component of this section is present.” According to the court, this suit was not based on a public disclosure of the alleged fraud. The only communication of the alleged false claim was by letter between the Medical Center and University. Because such a communication between two private parties was not a “public disclosure” within §3730(e)(4)(A), the 7th Circuit ruled that the district court had properly exercised jurisdiction.

ing the motion to amend would result in delay and burden the parties.

### **Hindo Moved to Amend Complaint Too Late**

The 7th Circuit further ruled that the district court did not abuse its discretion when it denied Hindo’s motion for leave to file a second amended complaint to include additional allegations of harassment and retaliation. Hindo had sought to appeal the district court’s dismissal of his third count of his amended complaint (regarding his discharge) on the basis of *res judicata*. While conceding that his original §3730(h) count was barred by the adverse state court decision regarding his discharge, Hindo argued that his new allegations of harassment, for which leave to file was denied, were not so precluded.

The 7th Circuit found that the circumstances of Hindo’s motion to amend supported the lower court’s denial. As recounted by the court, on September 22, 1993, the University filed a motion to dismiss Hindo’s §3730(h) count on the grounds of *res judicata*. The discovery deadline was October 31, 1993. On November 3, 1993, while the district court was considering the University’s motion to dismiss, Hindo filed a motion seeking leave to file a second amended complaint so that he could modify the §3730(h) count. Upholding the district court’s ruling, the 7th Circuit referred to “the litany of instances in which we affirmed a district court’s denial of leave to amend a complaint where discovery has ended and a motion is pending for dismissal of the count or for summary judgment.” The 7th Circuit added that a denial is especially warranted where, as here, the plaintiff has not provided an explanation as to why the amendment did not occur sooner and where the delay in grant-

## Qui Tam Statistics

### **Recoveries Top \$1 Billion, Filings Hit Record Level**

As of September 1995, *qui tam* recoveries have exceeded \$1 billion since the False Claims Act was amended in 1986. According to the Department of Justice (DOJ), more than 1,000 *qui tam* cases have been brought during this period, with a record 245 cases reported to have been filed in fiscal year 1995.

FY 1987: 33 cases	FY 1992: 119 cases
FY 1988: 60 cases	FY 1993: 131 cases
FY 1989: 95 cases	FY 1994: 220 cases
FY 1990: 82 cases	*FY 1995: 245 cases
FY 1991: 90 cases	

Total *qui tam* recoveries by fiscal year are approximated as follows:

FY 1987: -----	FY 1992: \$123.88 million
FY 1988: \$2.34 million	FY 1993: \$193.45 million
FY 1989: \$17.89 million	FY 1994: \$379.56 million
FY 1990: \$40.56 million	*FY 1995: \$200.43 million
FY 1991: \$70.45 million	

DOJ reported in August 1995 that it has intervened in 169 cases and obtained judgments or settlements in 115 matters. In cases where the relator's share has been finally determined, relators have received about \$153 million or an average of 18% of the total recovery. Based on DOJ's statistics, the average recovery for all resolved *qui tam* cases (including unsuccessful cases) is approximately \$1.76 million.

### **Intervention in Nearly A Quarter of Cases, with Many Actions Pending**

DOJ has intervened in *qui tam* cases at a rate of 24%. As of August 1995, DOJ reported that it was investigating 312 *qui tam* actions that are under seal and for which it has not yet made an intervention decision. Of the cases DOJ has declined to join, 380 have been dismissed or are not being pursued by the relator, while 83 cases are known to be in active litigation. Where the relator has proceeded after DOJ has declined, there have been recoveries in 26 cases for \$18 million, of which about 28% has been awarded to relators. According to DOJ, the status of the remaining cases that the Government has not joined is unclear.

\* *Statistics incomplete for fiscal year 1995.*

# DOJ INTERVENTIONS AND UNSEALED CASES

## **U.S. ex rel. Virgin Islands Housing Authority v. Coastal General Construction Services Corp. et al. (D VI No. \_\_)**

In August 1995, DOJ intervened in a *qui tam* suit alleging that a construction company and several of its officers defrauded the U.S. Department of Housing and Urban Development of \$800,000 by submitting false claims for the renovation and rehabilitation of two public housing projects in the Virgin Islands. The defendants allegedly fabricated documents and information to support inflated claims, causing the housing authority to submit false claims to HUD. Coastal General Construction Services Corp. had entered into contracts with the housing authority for building repair. After the contracts were terminated, Coastal submitted claims to the housing authority for work never performed. Relying on the accuracy of Coastal's information, the housing authority paid the claims and ultimately received reimbursement from HUD.

## **U.S. ex rel. Relator v. Healthwest Regional Medical Center et al. (WD WA No. \_\_)**

In August 1995, a *qui tam* lawsuit alleging improper Medicare and Medicaid billing for investigational medical devices was partially unsealed in connection with a countersuit by some of the defendant hospitals. According to the *qui tam* suit, filed in 1994, at least 21 major hospitals and research centers nationwide falsely billed for devices deemed experimental and not approved by the Food and Drug Administration. The hospitals allegedly received payments totaling at least \$800 million as a result of the false claims. Donald R. Warren of Monaghan & Warren (San Diego, CA) is the relator's counsel.

As part of a related government investigation into the billing practices of more than 130 hospitals, the HHS Office of Inspector General last year issued subpoenas concerning unapproved cardiac devices and approved devices used for unapproved purposes.

## **U.S. ex rel. Higby v. Data Chem Laboratories (D UT No. \_\_)**

In August 1995, a *qui tam* suit alleging that Data Chem Laboratories submitted erroneous test results was unsealed. The lawsuit was filed in February by Loren Higby, a former chemist at Data Chem. According to the lawsuit, the Army Toxic and Hazardous Waste Agency had contracted with the defendant to analyze water, soil, and other materials for traces of chemicals. Higby cited technical problems in analytical procedures that affected the testing results for hundreds of samples as well as employee inexperience in working with complicated analytical instruments. According to Higby, Data Chem refused to conduct necessary retesting to correct the problems. DOJ has declined intervention in this action. Representing the relator is Loren Lambert (Salt Lake City, UT).

## **U.S. ex rel. Chisholm v. Wolfe and Wolfe (SD CA No. 94-1063-H (BTM))**

In September 1995, a *qui tam* suit alleging false Medicare and Medi-Cal billing was unsealed. DOJ has joined the lawsuit, originally filed by Sharon Chisholm in 1994. According to the complaint, Dr. Gerald Wolfe, who operates the Alvarado Pain and Rehabilitation Center, billed for services that were not rendered or that were performed by unlicensed and unqualified assistants. The California osteopath allegedly instructed his staff to perform unnecessary procedures, including nerve study tests and physical therapy. He also allegedly made late night visits to nursing home patients and entered false notations on charts indicating he had examined them. Wolfe's license was previously revoked in New Jersey for similar abuses. The relator, who formerly worked for Dr. Wolfe, is represented by Linda Popejoy and Stephen Meagher of Phillips & Cohen (Washington, D.C.; San Francisco, CA). Assistant U.S. Attorney Donald F. Shanahan is handling the case for the Government.

**U.S. ex rel. O'Keefe v. McDonnell Douglas Corporation (ED MO No. \_\_\_ )**

In September 1995, DOJ announced that it intervened in a *qui tam* suit alleging that McDonnell Douglas Corporation defrauded the Government by routinely mischarging labor costs on several DOD airplane contracts, including those for A-12 and C-17 aircraft. According to the lawsuit, originally filed in 1993 by former McDonnell Douglas employee Daniel O'Keefe, company supervisors ordered assembly-line workers to shift millions of dollars of labor costs between various weapons programs. Specifically, employees were directed to charge work performed on certain overbudget programs to unrelated programs that were within budget. The mischarges are said to represent potentially one of the most costly defense fraud schemes to date. Mr. O'Keefe is represented by Daniel Conlisk of Dankenbring, Greiman, Osterholt & Hoffmann (St. Louis, MO).

According to DOJ, in a separate Court of Federal Claims suit, A-12 contractors McDonnell Douglas and General Dynamics are challenging the Navy's default termination of the A-12 contract.

# QUI TAM SETTLEMENTS

## ***U.S. ex rel. Fergusson v. GTE Government Systems Corporation et al.* (D MA No. 93-10348)**

In July 1995, GTE Government Systems Corporation and Canadian Marconi Corporation agreed to pay the Government **\$3.2 million** to settle a *qui tam* suit brought by Edward Fergusson in 1993. The firms allegedly sold the Army radios that did not meet the hot weather temperature performance requirements of the contract. The radios were intended for use under combat conditions that might be encountered in desert and tropical areas. Mr. Fergusson is a former GTE Government Systems employee. According to the lawsuit, after conducting internal testing, company engineers concluded that a number of the 2,500 radios delivered to the Army failed to perform properly at high temperatures. The Army was not fully informed of the testing results. As part of the settlement, GTE Government Systems and Canadian Marconi will conduct, at their own expense, a retesting and repair program for the affected units. Assistant U.S. Attorney Bunker Henderson II and Dennis L. Phillips of the DOJ Civil Division handled the case for the Government.

## ***U.S. ex rel. Wells v. Huntleigh Technology, PLC et al.* (D NJ No. 95-95)**

In July 1995, Huntleigh Technology, PLC agreed to pay the Government **\$4.9 million** to settle a *qui tam* suit brought by Ronald Wells in 1994. The lawsuit, originally filed in New York, alleged that Huntleigh Healthcare, a division of Huntleigh Technology, falsely represented to dealers and suppliers that a particular lymphedema pump it manufactured qualified for Medicare's highest reimbursement rate when, in fact, it qualified for a much lower rate. As a result of Huntleigh's fraudulent representations regarding the pump's specifications and billing code, dealers submitted false claims for reimbursement. Mr. Wells, a durable medical equipment supplier, was solicited by a Huntleigh representative to distribute the lymphedema pump,

which is used to treat swelling in limbs. The relator's share was 18 percent or \$882,000. The relator was represented by Neil V. Getnick of Getnick & Getnick (New York, NY). Assistant U.S. Attorney Joseph G. Braunreuther and Sara Strauss of the DOJ Civil Division represented the Government.

## ***U.S. ex rel. Johnson v. General Electric Company* (SD OH No. C-1-93-0846)**

In August 1995, General Electric Company agreed to pay the Government **\$7.18 million** to settle a *qui tam* suit filed by Ian Johnson in 1993. The lawsuit alleged that General Electric failed to satisfy electrical bonding requirements in its contracts, thereby creating a safety risk. The company allegedly sold 7,000 engines without proper testing for resistance to electrical interference. The engines at issue are used in commercial planes and military aircraft such as the F-16 fighter and B1-B bomber. While the Air Force and FAA found no safety problems, the company could still have been liable under the False Claims Act. In addition to the settlement payment, General Electric reportedly agreed to make a modification in the controls of one type of military engine and to negotiate new contract language with the Government concerning electrical bonding. The relator was formerly an electrical engineer at the company's Evendale, Ohio aircraft engine plant. The relator's share was \$1.7 million. James Helmer of Helmer, Luginbill, Martins & Neff (Cincinnati, OH) was the relator's counsel. Assistant U.S. Attorney Gerald F. Kaminski and Michael C. Theis of the DOJ Civil Division represented the Government.

## ***U.S. ex rel. Nelson v. CSX Transportation, Inc.* (MD FL No. 94-248-CIV-J-10)**

In September 1995, CSX Transportation, Inc. agreed to pay **\$5.9 million** to the U.S. Government and 11 state governments to settle a *qui tam* suit filed by A. David Nelson in conjunction with Taxpayers Against Fraud, The False Claims Act Legal Center. The relator, a former CSX employee, brought the suit in 1994. According to the lawsuit, CSX defraud-

ed federal and state governments by overcharging for materials used to maintain and repair railroad crossings. While working on an audit of certain transactions, Nelson discovered that CSX failed to obtain the lowest prices available for construction materials, as required by the U.S. Department of Transportation's Rail Highway Crossing Program. CSX did not obtain materials through competitive bidding, established "shell" companies through which materials could be marked up and resold at higher prices, and inflated the number of person-hours required to wire equipment. The relator's share was 20 percent or \$1.18 million. Mr. Nelson was represented by Mary Louise Cohen and Mitch Kreindler of Phillips & Cohen (Washington, D.C.). Representing the Government was Benjamin J. Vernia of the DOJ Civil Division.

**U.S. ex rel. Copeland v. Lucas Western Inc. et al. (D UT No. 93-C-831B)**

In September 1995, the British corporation Lucas Industries, plc and two of its U.S. subsidiaries agreed to pay the Government **\$88 million** to settle a *qui tam* suit brought by a former machinist for the company. The recovery is the largest to date for the sale of non-compliant parts to the Department of Defense. The suit, filed in 1993 by Frederick Copeland, alleged falsification of gear charts for a key component of the Navy's F/A-18 planes as well as major defects in gearboxes for the Army's Multiple Launch Rocket System. One of the U.S. subsidiaries, Lucas Western, pleaded guilty in January 1995 to 37 counts of making false certifications to DOD that gearboxes for Navy fighter jets and Army rocket launchers had been fully inspected in accordance with contractual requirements when, in fact, they had not. Investigators reportedly contended that the gearboxes supplied by Lucas were responsible for engine fires, aborted missions, and system failures. A record criminal fine of \$18.5 million was paid by Lucas Western, and Lucas Industries has been barred from receiving new government contracts. The relator's share was 21 percent or \$18.48 million. The relator was represented by Lon D. Packard of Packard, Packard & Johnson (Salt Lake City, UT). John A. Kolar of the DOJ Civil Division handled the case for the Government.

## Israel Aircraft Industries Ltd.

In July 1995, DOJ announced that Israel Aircraft Industries Ltd. (IAI) agreed to pay the Government **\$8.5 million** plus interest to settle False Claims Act and TINA allegations that it knowingly submitted false cost data while negotiating Navy contracts. The company had received contracts in 1984 and 1986 for maintenance and support of Kfir fighter planes leased to the Navy. According to government auditors, IAI did not provide the Navy with accurate, current, and complete data concerning equipment and aircraft parts costs as required under the Truth in Negotiations Act. The company did not reveal updated bills that showed its most current vendor quotes and purchase orders for necessary maintenance equipment. The company also allegedly withheld records relating to the dollar value of consumable aircraft parts used per flight hour, instead submitting an inflated estimate that it falsely stated reflected actual costs.

## B.F. Goodrich Company

In July 1995, DOJ announced that the B.F. Goodrich Company will pay the Government **\$552,500** to settle allegations that it knowingly manufactured defective 15-person assault rafts for the Army from 1986 to 1988. The settlement resolves the company's potential liability under the False Claims Act. According to the Government's investigation, B.F. Goodrich cut corners in the manufacturing process, including using an adhesive weaker than that required under the contract. The Government also cited incorrect bow height and warping which impaired the raft's capacity to function properly under all conditions. The Army issued two recall alerts for the rafts.

According to DOJ, a former government quality inspector who was stationed at the company's Engineered Rubber Products facility pleaded guilty in 1993 to a charge that he illegally received a gratuity for performing his job, which included inspecting rafts. B.F. Goodrich sold its Engineered Rubber Products Division in 1988.

## Rockwell International Corporation

In July 1995, Rockwell International Corporation agreed to pay the Government **\$27 million** to settle allegations that the company knowingly failed to provide accurate, complete, and current information in negotiating multi-billion dollar contracts in 1981 to develop the B1-B bomber and build the first nine bomber planes. Rockwell allegedly did not tell the Government that changes in its corporate costs and a change in California law reduced the company's costs of doing business. According to DOJ, these cost reductions were not passed on to the Government despite Rockwell's specific agreement with federal authorities to do so. The settlement resolves Rockwell's potential liability under the False Claims Act and Truth in Negotiations Act.

## Dana Corporation

In September 1995, DOJ announced that the Dana Corporation agreed to pay the Government **\$19.5 million** to partially settle a False Claims Act suit alleging that its former division, Beaver Precision Products Inc., overcharged the Army, Air Force, and Navy for missile and aircraft parts from 1981 to 1989. According to the 1992 lawsuit, the Government was overcharged on 18 sole-source, negotiated contracts for ball screw actuators, which are used as control mechanisms on Patriot and MLRS missile systems, B-1, C-5A, C-130 and F-14 aircraft, and the Air Force's F100 high-performance jet engine. The actuators control such parts as the landing gear and flaps of aircraft. Beaver Precision allegedly inflated prices by providing misleading cost data to government negotiators and withholding accurate data. According to DOJ, the partial settlement does not affect pending claims arising from Beaver's sales of F100 jet engine parts.

## **Acknowledgments**

TAF thanks the Department of Justice Office of Public Affairs and *qui tam* counsel for providing source materials.

## HHS Reports \$101 Million in Fraud Recoveries

- According to the Semiannual Report of the Department of Health and Human Services Office of Inspector General, the Government recouped approximately \$101 million through civil monetary penalties and False Claims Act settlements from October 1, 1994 to March 31, 1995. During this reporting period, the OIG imposed 801 sanctions in the form of exclusions or monetary penalties on individuals and entities for Medicare and Medicaid fraud or abuse. Overall, OIG's work resulted last year in \$8 billion in savings, fines, penalties, and recoveries -- the largest amount in the Department's history.

## New Health Care Fraud Alert Issued

- In August the HHS Office of Inspector General issued a "Special Fraud Alert" concerning the provision of medical supplies to nursing facilities. The Alert is the second in a series of fraud warnings that the OIG will issue over the next year as part of its "Operation Restore Trust" anti-fraud crackdown. Among the fraudulent practices identified by Inspector General June Gibbs Brown are claims for supplies and equipment that are not medically necessary, claims for items that are not provided or are double billed, and illegal kickbacks in exchange for Medicare or Medicaid referrals.

Besides illegal remuneration and waiver of copayments, the following factors may indicate improper nursing facility transactions according to the Alert: excessive volumes of supplies delivered to or solicited by nursing facilities and kept as inventory for lengthy periods; items provided directly to residents that are unordered, unnecessary, or unused; an unusually active presence in facilities of medical supply sales representatives who are given unlimited access to patient medical records; and questionable documentation for medical necessity of supplies.

## Previous Publications Available

- Back issues of the *Quarterly Review* as well as the *1994 Year in Review* are still available at no cost. Requests can be made by phone or mail.

## TAF on the Internet

- TAF has initiated an on-line service on the Global Internet designed to educate the public and legal community about *qui tam*. The Internet presence features information about the organization, frequently asked questions about *qui tam*, statistics, and an on-line version of the law. Look for an expanded presence in the coming months, including TAF publications. TAF's site is located at WWW: <http://www.taf.org/taf> or via e-mail at [taf-info@taf.org](mailto:taf-info@taf.org).

## Library Resources

- TAF has available in its library a variety of resources on the False Claims Act and *qui tam*. The library is open to the public during regular business hours. Please call in advance to schedule an appointment. Submissions of case-related materials such as complaints and settlement agreements are welcome.

## Qui Tam Attorney Network

- In conjunction with its library project, TAF is working to build and facilitate an information network for *qui tam* attorneys. For further details, please contact TAF Staff Attorney Gary W. Thompson.

## Quarterly Review Submissions

- TAF would like to include submissions by readers in future issues of the *Quarterly Review* (e.g., opinion pieces, legal analysis, practice tips). If you would like to discuss a potential article, please contact Associate Director Alan Shusterman.