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Introduction

**Smith Pachter McWhorter PLC** is pleased to present the 2020 edition of its False Claims Act Practice Guide. This Guide is intended to serve as a practical reference tool, providing general guidance about False Claims Act (“FCA”) legal standards, required elements of proof, common issues that give rise to FCA liability, and recent legal and enforcement developments.

**Part One**, beginning at page 1, reviews the FCA statute, explains the elements that must be proven to find a violation, reviews typical types of enforcement actions, and discusses how damages are calculated.

**Part Two**, beginning at page 9, describes common risk areas and theories of liability that the U.S. Department of Justice (“DOJ”) and *qui tam* relators have pursued. We also describe how and where these issues often arise for government contractors.

**Part Three**, beginning at page 18, provides an update on DOJ guidance or policy statements provided during the past year, recent enforcement activity, and notable case law developments.

We hope you find this Guide useful in considering potential FCA issues for your organization. We also hope that readers will be able to use the material and analysis in the Guide to anticipate and, hopefully, to avoid the many FCA risk areas that can arise in the federal contracting environment.

Please feel free to contact the authors of this Guide or any of the members of our Firm with questions or comments. Brief biographical and contact information for our attorneys is provided at the end of this Guide.

Thank you and best wishes for the coming year.

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Part One: FCA Statutory Framework and Legal Elements

The False Claims Act ("FCA"), codified at 31 U.S.C. §§ 3729 – 3733, is the federal government’s “primary litigative tool for combatting fraud.” Olson v. Fairview Health Servs. of Minnesota, 831 F.3d 1063, 1069 (8th Cir. 2016). The FCA, however, is “not an all-purpose antifraud statute,”... or a vehicle for punishing garden-variety breaches of contract or regulatory violations.” Universal Health Servs., Inc. v. United States ex rel. Escobar, 136 S. Ct. 1989, 2003 (2016) (citation omitted). Rather, the FCA applies to those who knowingly submit false or fraudulent claims for payment to the federal government or knowingly fail to return funds that are owed to the government.1 In this Part of the Guide, we review the statute, elements of proof in FCA cases, common enforcement action procedure, and damage calculations.2

A. FCA Statute and Elements of Proof

Under 31 U.S.C. § 3729(a)(1), civil liability attaches when any person:

(A) knowingly presents, or causes to be presented, a false or fraudulent claim for payment or approval;

(B) knowingly makes, uses, or causes to be made or used, a false record or statement material to a false or fraudulent claim;

(C) conspires to commit [an FCA violation];

(D) has possession, custody, or control of property or money used, or to be used, by the Government and knowingly delivers, or causes to be delivered, less than all of that money or property;

(E) is authorized to make or deliver a document certifying receipt of property used, or to be used, by the Government and knowing that the information on the receipt is true;

(F) knowingly buys, or receives as a pledge of an obligation or debt, public property from an officer or employee of the Government, or a member of the Armed Forces, who lawfully may not sell or pledge property; or

(G) knowingly makes, uses, or causes to be made or used, a false record or statement material to an obligation to pay or transmit money or property to the Government, or knowingly conceals or knowingly and improperly avoids or decreases an obligation to pay or transmit money or property to the Government.

1 The FCA does not apply to claims, records, or statements made under the Internal Revenue Code of 1986. 31 U.S.C. § 3729(d).

2 There is also a criminal statute, 18 U.S.C. § 287, that covers fraud against the United States. In United States v. Maher, 582 F.2d 842, 848 (4th Cir. 1978), cert. denied, 439 U.S. 1115 (1979), the Fourth Circuit summarized the distinction between the civil and criminal aspects of these statutes: “Under § 287, the government must prove beyond a reasonable doubt that the defendant performed forbidden acts with a criminal intent. The prohibition of the statute is absolute in that the defendant’s liberty is at stake. Under [the Civil FCA], the government is empowered to enforce the underlying civil duty to submit to the government only valid claims for payment by bringing an action for imposition of civil penalties. The nature of the proceedings, the standards of proof, and the defendant’s interests at stake are wholly different under these two statutes.” (Emphasis added.) This Guide focuses on the civil FCA, but readers should be aware that the criminal penalties exist for egregious cases.

3 Italicized terms are defined by the statute and are discussed below.
Section 3729 also defines certain terms that are used in the FCA:

- **Knowing or Knowingly** means that person: (i) has actual knowledge of about the falsity of a claim, (ii) acts in deliberate ignorance of the truth or falsity of the claim, or (iii) acts with reckless disregard of the truth or falsity of the claim. Notably, the FCA does not require proof that the person specifically intended to defraud the Government. 31 U.S.C. § 3729(b)(1).

- **Claim** means any request or demand for money or property (regardless of whether or not the United States has title to the money or property) that: (i) is presented to an officer, employee, or agent of the United States; (ii) or is made to a contractor, grantee, or other recipient, if the money or property is to be spent or used on the Government's behalf or to advance a Government program or interest, and if the United States Government either provides, or has provided, any portion of the money or property requested or demanded; (iii) or will reimburse such contractor, grantee, or other recipient for any portion of the money or property which is requested or demanded. § 3729(b)(2)(A).

- **Obligation** means an established duty arising from: (i) an express or implied contractual, grantor-grantee, or licensor-licensee relationship; (ii) a fee-based or similar relationship; (iii) a statute or regulation; or (iv) the retention of any overpayment. § 3729(b)(3).

- **Material** is defined as having a natural tendency to influence, or be capable of influencing, the payment or receipt of money or property. § 3729(b)(4).

### B. Elements of Proof and Judicial Interpretations of Terms

To prevail on an FCA allegation, a party must prove that: (i) a defendant presented a claim to the government, (ii) the claim was false, and (iii) the defendant knew that the claim was false. Proof of materiality is also a required element in many (but not all) FCA claims. However, because litigants typically assert FCA claims based on multiple theories under § 3729(a)(1), one or more of which require proof of materiality, we will evaluate the materiality element below as a required element of proof.

#### 1. Presentation of a Claim to the Government

To violate the FCA, the false or fraudulent statement must be associated with a **claim** (as defined above) that was presented (or submitted) to the government. United States ex rel. Prather v. Brookdale Senior Living Communities, Inc., 838 F.3d 750, 768 (6th Cir. 2016). Courts have equated the term “presentment” with any submission of a claim resulting in a “call upon the government fisc.” United States ex rel. Grant v. United Airlines Inc., 912 F.3d 190, 196 (4th Cir. 2019) (quoting Harrison v. Westinghouse Savannah River Co., 176 F.3d 776, 785-86 (4th Cir. 1999)). The FCA “attaches liability, not to the underlying fraudulent activity or to the government’s wrongful payment, but to the ‘claim for payment.’” United States v. Lang, 251 F. Supp. 3d 971, 975 (E.D.N.C. 2017); see also United States ex rel. Clausen v. Lab. Corp. of Am., 290 F.3d 1301, 1311 (11th Cir. 2002) (holding FCA “does not create liability merely for a... disregard

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4 Claims do not include requests or demands for money or property that the Government has paid to an individual as compensation for Federal employment or as an income subsidy with no restrictions on that individual’s use of the money or property. 31 U.S.C. § 3729(b)(2)(B).

5 See, e.g., United States ex rel. Purcell v. MWI Corp., 807 F.3d 281, 287 (D.C. Cir. 2015); United States ex rel Lemon v. Nurses To Go, Inc., 924 F.3d 155, (5th Cir. 2019) (also including materiality as required element).

6 The term “material” appears only in the text of § 3729(a)(1)(B) (making or using false statements or records in support of a claim) and § 3729(a)(1)(G) (false statements or records used to reduce payment owed to the Government, known as “reverse false claims”). Materiality also is required element in implied false certification theories, which are discussed in greater detail in Part One, Section B(4).
of Government regulations or improper internal policies unless, as a result of such acts, the provider knowingly asks the Government to pay amounts it does not owe”). Thus, a person need not have successfully defrauded the government for liability to attach. See, e.g., Lamb Eng’g & Constr. Co. v. United States, 58 Fed. Cl. 106, 111 (2003). A contractor who submits a false claim may still be liable under the FCA for statutory penalties, “even if it did not actually induce the government to pay out funds or to suffer any loss.” Id., at 111 (noting “the government need not prove actual damages” to recover under FCA).

A typical false claim “involves an incorrect description of goods or services provided or a request for reimbursement for goods or services never provided.” United States ex rel. Scott v. Pac. Architects & Engineers (PAE), Inc., 270 F. Supp. 3d 146, 153 (D.D.C. 2017). However, courts construe the FCA broadly and will interpret the term “false claims” to apply to demands for government funds, such as false applications for government loans or fraudulent claims for federal assistance. See, e.g., States v. Neifert–White, 390 U.S. 228, 233 (1968).

In broadly construing the FCA, courts have held the “causes to be made” or “presented” prong of the FCA extends liability beyond a prime contractor, reaching any person knowingly assisting in causing the Government to pay claims grounded in fraud. United States ex rel. Tran v. Computer Sciences Corp., 53 F. Supp. 3d 104, 126-27 (D.D.C. 2014). The “causes to be presented” prong will attach liability to a defendant whose conduct was “at least a substantial factor in causing, if not the but-for cause of, submission of false claims.” Id., at 126 (citing United States v. Toyobo Co., 811 F. Supp. 2d 37, 48 (D.D.C. 2011)). Thus, a prime contractor that submits false subcontractor claims to the federal government will be liable if the prime contractor knew of the falsity or acted with reckless disregard or deliberate ignorance of the falsity.

2. **Falsity of the Claim - Factual and Legal**

Although falsity is a required element of proof, the FCA does not define the term. Thus, courts have determined that a “false” claim is one that is “aimed at extracting money the government otherwise would not have paid.” United States ex rel. Kester v. Novartis Pharm. Corp., 41 F. Supp. 3d 323, 328–29 (S.D.N.Y. 2014) (quoting Mikes v. Straus, 274 F.3d 687, 696 (2d Cir. 2001)). Courts have further defined two categories of falsity: factual falsity and legal falsity. United States ex rel. Petratos v. Genentech Inc., 855 F.3d 481, 486 n.1 (3d Cir. 2017) (citing United States ex rel. Wilkins v. United Health Group, Inc., 659 F.3d 295, 305 (3d Cir. 2011)). Both types are described in greater detail below.

**Factual falsity** (also known as literal falsity) occurs when a contractor makes a claim or request for reimbursement with “an incorrect description of goods or services provided or a request for reimbursement for goods or services never provided.” United States ex rel. Conner v. Salina Regional Health Center, Inc., 543 F.3d 1211 (10th Cir. 2008); see United States ex rel. Hendow v. Univ. of Phoenix, 461 F.3d 1166, 1170 (9th Cir. 2006) (finding that a literally false FCA theory may lie where “the claim for payment is itself literally false or fraudulent”).

**Legal falsity** is “[m]ore difficult to assess” and occurs in cases where a “contractor falsely represents that it is in compliance with a particular federal statute or regulation.” United States ex rel. Perverz v. Beth Israel Medical Center, 736 F. Supp. 2d 804 (S.D.N.Y. 2010). Courts have identified two types of legal falsity cases: those where a contractor has (i) expressly or (ii) impliedly certified compliance with some statutory, regulatory or contractual requirement. United States ex rel. Conner v. Salina Regional Health Center, Inc., 543 F.3d 1211 (10th Cir. 2008); United States ex rel. Kester v. Novartis Pharm. Corp., 41 F. Supp. 3d 323, 329 (S.D.N.Y. 2014) (“a ‘legally false’ claim is ‘false’ because it has been tainted by some underlying statutory, regulatory, or contractual violation made in connection with that claim, which renders the claim ineligible for reimbursement”).

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7 The express and implied certification theories of liability are described in more detail in Part Two, Section F(3).
3. **Knowledge of Falsity**

As noted above, under the FCA, a person acts “knowingly,” if he or she: “(1) has actual knowledge of the [falsity]; (2) acts in deliberate ignorance of the truth or falsity of the information; or (3) acts in reckless disregard of the truth or falsity of the information, and no proof of specific intent to defraud is required.” *United States ex rel. Bartlett v. Ashcroft*, 39 F. Supp. 3d 656, 665 (W.D. Pa. 2014) (emphasis added). “Accordingly, unless the circumstances of a case show that a defendant knows of, or ‘acts in deliberate ignorance’ or ‘reckless disregard’ of, the fact that he is involved in conduct that violates a legal obligation to the United States, the defendant cannot be held liable under the FCA.” *United States ex rel. Harper v. Muskingum Watershed Conservancy Dist.*, 842 F.3d 430, 437 (6th Cir. 2016).

The “knowledge” component is “designed to address the problem of the ‘ostrich-like’ refusal to learn of information which an individual, in the exercise of prudent judgment, had reason to know.” *Horn & Assocs., Inc. v. United States*, 123 Fed. Cl. 728, 763 (2015) (emphasis added). For example:


- “Where a defendant has an ongoing business relationship with a repeated false claimant, and the defendant knows of the false claims, yet does not cease doing business with the claimant or disclose the false claims to the United States, the defendant's ostrich-like behavior itself becomes a course of conduct that allowed fraudulent claims to be presented to the government.” *United States v. President & Fellows of Harvard College*, 323 F. Supp. 2d 151, 187 (D. Mass. 2004) (internal quotation marks and citations omitted).

That said, “the statute’s language makes plain that liability does not attach to innocent mistakes or simple negligence.” *United States ex rel. Phalp v. Lincare Holdings, Inc.*, 857 F.3d 1148, 1155 (11th Cir. 2017). Courts have also recognized that, even if wrong, a contractor’s objectively reasonable interpretation of a regulation or statute can be a viable defense to an FCA allegation: “Consistent with the need for a knowing violation, the FCA does not reach an innocent, good-faith mistake about the meaning of an applicable rule or regulation. Nor does it reach those claims made based on reasonable but erroneous interpretations of a defendant’s legal obligations.” *United States ex rel. Purcell v. MWI Corp.*, 807 F.3d 281, 287-88 (D.C. Cir. 2015) (internal citations omitted).

4. **Materiality**

As noted above, the term *material* appears only in subsections (B) and (G) of FCA’s § 3729(a)(1). However, as discussed below, questions of materiality have taken on greater significance in the review of FCA claims after the Supreme Court’s decision in *Escobar*.

The statute defines *material* as “having a natural tendency to influence, or be capable of influencing, the payment or receipt of money or property.” 31 U.S.C. § 3729(b)(4). In its seminal *Escobar* decision, the Supreme Court explained that materiality under the FCA involves a “fact-specific inquiry,” and the standard is demanding. *Escobar*, 136 S. Ct. at 2002-03 (“materiality cannot rest on a single fact or occurrence as always determinative”). The Court elaborated that “materiality looks to the effect on the likely or actual behavior of the recipient of the alleged misrepresentation.” *Id.*

Materiality is often evaluated in cases involving allegations of legally false claims (i.e., express or implied false certification theories), when the government or relator must demonstrate that the standard or fact to which a contractor falsely certified was material to the government’s payment decision. *Escobar* teaches that the Government’s “decision to expressly identify a provision as a condition of payment is relevant, but not automatically dispositive.” *Id.*, at 2003
Proof of materiality may include evidence the Government “consistently refuses to pay claims… based on noncompliance with the particular statutory, regulatory, or contractual requirement.” *Id.* “Conversely, if the Government pays a particular claim in full despite its actual knowledge that certain requirements were violated, that is *very strong evidence that those requirements are not material.*” *Id.* (emphasis added).

C. Qui Tam Provision

Under the FCA, civil cases may be initiated either by the United States Department of Justice ("DOJ") or by private parties, known as *qui tam* relators. 31 U.S.C. §§ 3730(a) and (b). Section 3730(b) enables *qui tam* relators to recover damages on behalf of the United States. Any person or entity with knowledge of fraudulent activity against the government may file a claim as the plaintiff; the relator need not have personally been harmed by the defendant to bring a *qui tam* suit. Successful *qui tam* cases enable to the relator to receive a percentage of any award, including a settlement.

The FCA requires the DOJ to be substantially involved in a *qui tam* relator’s suit from the outset. FCA complaints in cases initiated by *qui tam* relators must be filed under seal in a federal court, with a copy provided to DOJ for review. § 3731(b)(2). DOJ has at least 60 days to review the allegations in the complaint, during which the complaint remains sealed.8 *Qui tam* cases are typically sealed well beyond the 60-day window, however, because DOJ is permitted to seek extensions of time for its review, upon showing of good cause, under § 3730(b)(3), and these extension requests—often for six months at a time—are commonly granted. The sealed review period can therefore last many months or even years.

After investigating the allegations in a relator’s complaint, DOJ generally has three options, other than settlement: (i) *intervene* in the case and take over as the plaintiff; (ii) *decline* to intervene, meaning the relator may choose to litigate the matter on its own; or (iii) *move to dismiss* the relator’s complaint.

- **Intervention:** If DOJ intervenes in one or more counts of the *qui tam* action, this signals greater potential liability for the defendant, as intervention means the federal government finds the relator's claims to be meritorious and that DOJ will bring to bear its tremendous resources on the case. If DOJ prevails or settles, then the relator receives between 15% and 25% of the proceeds of the action or settlement. 31 U.S.C. § 3730(d)(1).
- **Declination:** If DOJ declines to intervene, the relator may continue to prosecute the action on behalf of the United States. DOJ would continue to receive pleadings throughout the case but is not considered a party for the purposes of discovery. DOJ also retains the right to intervene at a later date (upon showing of good cause) and to collect the majority of the proceeds of any recovery: in a non-intervention case, the relator receives 25% to 30% of proceeds of the action or settlement. 31 U.S.C. § 3730(d)(2).
- **Dismissal:** Although relatively infrequent, the DOJ may affirmatively move to dismiss the relator’s complaint. 31 U.S.C. § 3730(c)(2)(A). As set forth in a 2018 memorandum by DOJ's Director of the Civil Fraud Section, Michael Granston (the “Granston Memo”), dismissal decisions occur when DOJ determines that, among other things, the relator’s case lacks merit, the costs imposed by the litigation case are excessive or that the litigation would conflict with significant statutory or policy interests of the United States.9

The FCA also details several circumstances in which a relator **cannot** file or pursue a *qui tam* action:

- The relator was convicted of criminal conduct arising from his or her role in the FCA violation. 31 U.S.C. § 3730(d)(3).
- Another *qui tam* concerning the same conduct already has been filed (the “first to file bar”). § 3730(b)(5).

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8 Once the complaint is filed, copies are provided to the judge, DOJ and the local United States Attorney’s Office. The relator also must provide DOJ with a “disclosure statement,” which must contain “substantially all” of the evidence in his or her possession that relates to the complaint's allegations. 31 U.S.C. § 3730(b)(2).

9 Developments related to the Granston Memo are discussed further in Part 3, Section B.
• The government already is a party to a civil suit or administrative money proceeding concerning the same conduct. § 3730(e)(3).

• The *qui tam* action is based on information that has already been disclosed to the public by some other means, such as criminal, civil, or administrative hearings in which the government is a party, government hearings, audits, reports, or investigations, or through the media (the “public disclosure bar”). § 3730(e)(4)(A). Note, however, that relator may proceed despite public disclosure if the relator was the *original source* of the publicly disclosed information.

These restrictions seek to prevent “parasitic” *qui tam* actions, where the relator has not helped the government uncover fraud (or have themselves benefitted from the fraud), but attempts to profit from misconduct already known to the government. *United States ex rel. Shea v. Cellco P’ship*, 863 F.3d 923, 926 (D.C. Cir. 2017).

**D. FCA’s Statute of Limitations**

At 31 U.S.C. § 3731(b), the FCA’s statute of limitations provides:

A civil action under section 3730 may **not** be brought—

1. more than 6 years after the date on which the violation of section 3729 is committed, or

2. more than 3 years after the date when facts material to the right of action are known or reasonably should have been known by the official of the United States charged with responsibility to act in the circumstances, but in no event more than 10 years after the date on which the violation is committed,

whichever occurs last.

Courts and litigants have long struggled to apply the terms of § 3731(b), such that litigants should check the standards in their jurisdiction. Regarding the six-year limitation set forth in § 3731(b)(1), courts are split as to when to the violation is deemed to have occurred, i.e., when the limitation clock would start ticking. Some jurisdictions look to the date on which the defendant submitted the false claim. See, e.g., *United States v. Vanoosterhout*, 898 F. Supp. 25, 30 (D.D.C. 1995); *Woodbury v. United States*, 232 F. Supp. 49, 59 (D. Or. 1964) *aff’d in part, rev’d in part on other grounds* 359 F.2d 370; *United States ex rel. Jackson v. Univ. N. Tex.*, 673 Fed. Appx. 384, 387 (5th Cir. 2016) (*per curiam*). Other courts start the limitations period when the government issues payment on the false claim. See, e.g., *United States v. Wells Fargo Bank, N.A.*, 972 F. Supp. 2d 593, 609 n.8 (S.D.N.Y. 2013) (citing *Kreindler & Kreindler*, 985 F.2d 1148, 1157 (2d Cir. 1993)).

Section 3731(b)(2) addresses circumstances where the defendant’s fraudulent activity is concealed at the time of the actual violation and thus delays the government’s knowledge of the wrongdoing. Under this scenario, the FCA allows an FCA suit to be initiated within the **later of ten years** from the date of the violation or **within three years** from when a government official knew or had reason to know of the violation. 31 U.S.C. § 3731(b)(2).

Notably, in FCA cases brought by *qui tam* relators where the Government chooses not to intervene, the Supreme Court recently resolved a circuit split and held that, because a *qui tam* relator is not a Government official, the three-year limitation period does not apply to the relator. *Cochise Consultancy, Inc. v. United States ex rel. Hunt*, 139 S.Ct. 1507, 1510 (2019). In making this determination, the Court recognized that, for example, “if the Government discovers the fraud on the day it occurred, it would have 6 years to bring suit, but if a relator instead discovers the fraud on the day it
occurred and the Government does not discover it, the *relator could have as many as 10 years* to bring suit.” *Id.*, at 1513 (emphasis added). The Court acknowledged that its holding might seem “odd” or “counterintuitive,” but the Court could find no other plausible interpretation of the FCA’s text. *Id.*, at 1513.

In sum, if the Government initiates or intervenes in an FCA case, it must do so within the later of (i) six years from the date of the violation or (ii) three years from date on which a Government official knew or should have known of the violation. If a relator initiates an FCA case and the Government does not intervene, then the case must be filed no more than 10 years after the date of the violation.

**E. Damages**

FCA damages assessments can be astronomical, falling into three general categories. First, FCA violators are liable for a civil penalty of between $11,181 and $22,363 per false claim. 31 U.S.C. § 3729(a)(1). Second, in addition to the per-claim penalties, defendants are liable for *treble damages*, or three times the amount of damages sustained by the Government. *Id.* Third, FCA violators are liable for the government's costs for bringing a civil action to recover any penalty or damages. § 3729(a)(3). Given its potentially existential effect on defendants, we will focus on the treble damages provision.

1. **Treble Damages**

Calculating – and then trebling – actual damages can be complicated when an FCA violation is based on a theory of liability that *every claim* submitted in connection with a particular contract is false or fraudulent. In such cases, courts must determine (i) what value was received and (ii) when to apply the trebling factor. Treble damages calculation methods vary by Circuit.

**Net Trebling.** Using a net trebling method, courts first calculate the difference between the actual price paid by the Government for the false claims and the price the Government would have paid had the claims not been false. The resulting difference is then trebled. *See United States v. Anchor Mortg. Corp.*, 711 F.3d 745, 749 (7th Cir. 2013) (using same net trebling method that applies to antitrust cases under the Sherman Act and to ordinary contract cases in civil litigation) (analyzing and rejecting gross trebling method and distinguishing *United States v. Bornstein*, 423 U.S. 303, 314 n. 10 (1976)).

**Benefit-of-the-Bargain.** Similar to the net trebling method, the D.C. Circuit has adopted what it described as a “benefit-of-the-bargain framework” for evaluating FCA damages and, in doing so, rejected arguments that a government contractor found to have violated the FCA must pay a penalty equal to three times the amount of the entire contract. *United States v. Science Applications International Corp.*, 626 F.3d 1257, 1278-79 (D.C. Cir. 2010) (“SAIC”). The SAIC court found that the court must calculate the market value of the products or services the government received and the market value of the products or services it *would have* received if they had been of the specified quality and treble only the difference between those amounts.

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10 The relator in *Cochise* “conceded that the 6-year limitations period in § 3731(b)(1) had elapsed before he filed suit....” *Cochise*, 139 S.Ct. at 1511. However, the relator “argued that his complaint was timely under § 3731(b)(2) because it was filed within 3 years of the interview in which he informed federal agents about the alleged fraud (and within 10 years after the violation occurred).” *Id.*

11 *See 28 C.F.R. § 85.5* (2018) (adjusting the per-claim range upward, pursuant to the Federal Civil Penalties Inflation Adjustment Act).

12 The SAIC court recognized that trebled damages might be calculated differently if the U.S. government did not receive any benefit from the goods or services provided. *Id.*, at 1279 (referencing *United States ex rel. Longhi v. Lithium Power Techs., Inc.*, 575 F.3d 458, 473 (5th Cir. 2009) (calculating damages as the amount the government paid to the defendants...
Gross Trebling. Courts that use the gross trebling method first determine the actual price that the government paid for the false claims and then treble that amount. After trebling, courts using this method subtract the price the Government would have paid, but for the false claim. See United States v. Eghbal, 548 F.3d 1281, 1283, 1285 (9th Cir. 2008) (relying on Bornstein and finding that the “FCA speaks of multiplying damages, not ‘net damages’ or ‘uncompensated damages’”).

2. Cooperation May Result in Double (Not Treble) Damages

The FCA provides an incentive to self-report potential FCA violations. If a party self-reports, the court may assess two times (rather than three times), the amount of damages sustained by the government because of the FCA violation, provided that the following additional factors exist:

(A) the person committing the violation furnished government officials investigating the false claims violations with all information known about the violation within 30 days after the date on which the person first obtained the information;

(B) such person fully cooperated with any government investigation of such violation; and

(C) at the time such person furnished the United States with the information about the violation, no criminal prosecution, civil action, or administrative action had commenced under this title with respect to such violation, and the person did not have actual knowledge of the existence of an investigation into such violation.


where “[t]he contracts entered ... did not produce a tangible benefit” to the government and were instead part of a grant program designed to award money to deserving small businesses) and United States v. Rogan, 517 F.3d 449, 453 (7th Cir. 2008) (concluding that the defendant, who submitted false claims for Medicare and Medicaid payments, was required to repay the full amount of the claims as damages because the defendant “did not furnish any medical service to the United States,” and instead effectively sought a government subsidy to which it was not entitled).
Part Two: Risk Areas and Enforcement

Some situations present higher risk that the elements required for FCA liability – false statements, made with knowledge, that are material to the government’s payment decision – may arise. Below we detail common theories of liability pursued by the government, followed by typical fact patterns through which those theories of liability can be proven.

A. Theories of Liability

Below are several theories of liability commonly pursued by relators or the government.

1. Improper Performance or Deliverables

A typical claim “under the FCA alleges that a person or company submitted a bill to the government for work that was not performed or was performed improperly, resulting in an undeserved payment flowing to that person or company.” United States ex rel. Customs Fraud Investigations, LLC. v. Victaulic Co., 839 F.3d 242, 247 (3d Cir. 2016). For example, FCA liability arises when contractors provide goods to the government but knowingly use inferior or defective parts or materials. See, e.g., United States ex rel. Westrick v. Second Chance Body Armor Inc., 128 F. Supp. 3d 1 (D.D.C. 2015) (involving FCA complaint related to allegedly defective body armor material made or sold by the defendants); United States ex rel. Roby v. Boeing Co., 100 F. Supp. 2d 619 (S.D. Ohio 2000) (involving allegations that a contractor violated the FCA by knowingly “manufacturing and selling defective transmission gears to the United States”).

FCA liability also may arise when contractors knowingly provide deficient services. See, e.g., United States v. Triple Canopy, Inc., 857 F.3d 174 (4th Cir. 2017). Triple Canopy involved a contract for security services in Iraq that required the contractor to provide guards who had received weapons training and passed tests demonstrating marksmanship competency. Id., at 175-76. Relators alleged the contractor invoiced for guards that the contractor knew had failed to satisfy the contract’s marksmanship requirements. Id.

2. Truth in Negotiations Act Violations

In 1962, Congress passed the Truth in Negotiations Act (“TINA”), 10 U.S.C. § 2306a et seq., to counter what Congress perceived as an imbalance between the negotiating strength of the government and potential contractors.13 Aerojet Solid Propulsion Co. v. White, 291 F.3d 1328, 1330 (Fed. Cir. 2002). Congress believed contractors were failing to disclose important facts regarding the probable cost of non-competitive contracts when negotiating with the government, and that the government lacked adequate negotiating tools to address the nondisclosures. Unisys Corp. v. United States, 888 F.2d 841, 844 (Fed. Cir. 1989). Contractors, according to Congress, overstated costs of future contract performance, resulting in frequent, excessively priced fixed price contracts. Lockheed Martin Corp., ASBCA No. 50464, 02-1 BCA ¶ 31,784, at 156,942.

TINA attempts to redress the purported imbalance between the government and contractors by requiring contractors to divulge significant detail concerning the various elements determining the ultimate price. United States v. United Techs. Corp., 255 F. Supp. 2d 787, 788 (S.D. Ohio 2003). Although potential contractors are free to negotiate whatever prices and terms the government will accept, TINA requires that disclosures during the negotiation process be current, accurate, and complete. United States ex rel. Campbell v. Lockheed Martin Corp., 282 F. Supp. 2d 1324, 1332 (M.D. Fla. 2003)

Because TINA requires disclosures to the government, FCA liability can attach when the disclosures relate to false claims.

13 TINA has been renamed the Truthful Cost or Pricing Data Act but is still commonly referred to as TINA. 10 U.S.C. § 2306a, 41 U.S.C. § 3306, FAR 15.403.
Specifically, FCA charges can arise when a contractor invoices the government after knowingly violating TINA during the negotiation process. See, e.g., United States v. BAE Sys. Tactical Vehicle Sys., LP, 2016 WL 894567 (E.D. Mich. Mar. 9, 2016) (government brought FCA charges alleging contractor violated TINA by failing “to meet its obligation to provide cost or pricing data that was accurate, complete, and current”); Sanders v. Allison Engine Co., 703 F.3d 930 (6th Cir. 2012) (involving “allegations that the defendants withheld cost and pricing data during their negotiations with the government’s agent in violation of the Truth in Negotiations Act and the FCA”).

3. False Certification (Express or Implied)

As noted above, federal courts have determined that legally false claims can create FCA liability. Legally false claims are premised on a “certification theory” of liability; that is, the claims involve “a false representation of compliance with a federal statute or regulation or a prescribed contractual term.” Mikes v. Straus, 274 F.3d 687, 696 (2d Cir. 2001); U.S. ex rel. Wood v. Allergan, Inc., 246 F. Supp. 3d 772, 783 (S.D.N.Y. 2017). Legally false certification claims “can rest [on] one of two theories—express false certification, and implied false certification,” United States ex rel. Conner v. Salina Reg’l Health Ctr., Inc., 543 F.3d 1211, 1217 (10th Cir. 2008), which are described below:

- Under an express false certification theory, the defendant is alleged to have signed or otherwise certified to compliance with some law or regulation on the face of the claim submitted.” United States ex rel. Hobbs v. Med-Quest Assocs., Inc., 711 F.3d 707, 714 (6th Cir. 2013). “The payee’s ‘certification’ need not be a literal certification, but can be any false statement that relates to a claim.” United States ex rel. Lemmon v. Envirocure of Utah, Inc., 614 F.3d 1163, 1168 (10th Cir. 2010). See also United States ex rel. Sloan v. Waukegan Steel, LLC, 2018 WL 1087642 (N.D. Ill. Feb. 28, 2018) (holding qui tam relator’s allegation that subcontractor submitted false steel weld inspection certifications to prime contractor was sufficiently detailed and material to survive motion to dismiss).

- In contrast, an implied false certification claim, is “based on the notion that the act of submitting a claim for reimbursement itself implies compliance with governing federal rules that are a precondition to payment.” Mikes, 274 F.3d at 699 (emphasis added). In Escobar, the Supreme Court recognized implied false certification as a viable theory of liability, provided that two conditions are met: “first, the claim does not merely request payment, but also makes specific representations about the goods or services provided; and second, the defendant’s failure to disclose noncompliance with material statutory, regulatory, or contractual requirements makes those representations misleading half-truth.” Escobar, 136 S.Ct. at 2001. Compliance need not be an express requirement for payment under the contract, but compliance with the particular regulation or statute must be material to the government’s decision to pay claims under the contract. Id., at 2004.

4. Fraud in the Inducement

B. Common FCA Risk Areas

Below we review several common factual circumstances that create heightened FCA liability risk.

1. **Prime Contractor Liability for Pass-through Claims**

Prime contractors and subcontractors are subject to FCA liability when presenting pass-through claims to the government: “[i]n False Claims Act actions, statements of the subcontractor, when submitted by the general contractor, may serve as a basis for liability against the general contractor.” United States ex rel. Ervin & Assocs., Inc. v. Hamilton Sec. Grp., Inc., 370 F. Supp. 2d 18, 41 (D.D.C. 2005). “[W]here the prime contractor allegedly knows that a material certification by a subcontractor was false,” courts hold “as a matter of law that the prime contractor has adopted the subcontractor’s certification by submitting it to the government.” Harrison v. Westinghouse Savannah River Co., 176 F.3d 776, 793 (4th Cir. 1999); see also Blake Constr. Co. v. United States, 28 Fed. Cl. 672, 681 (1993) (pass-through claim requires that the prime “considers there are good grounds for the claim, and that [the prime] intends for it (not [the subcontractor]) to be held liable for any possible fraud attributable to assertion of the claim”); Hanover Ins. Co. v. United States, 134 Fed. Cl. 51, 58 (2017) (government alleged fraud and FCA violations stemming in part from the contractor’s efforts to recover $1.1 million in pass-through subcontractor claims despite having settled those claims for $370,000).

Subcontractors may be liable under the FCA even if they cause a false claim to be presented to the government. See 31 U.S.C. § 3729(a)(1)(A); United States v. Carell, 782 F. Supp. 2d 553 (M.D. Tenn. 2011) (involving allegations that defendants submitted fraudulent claims through intermediaries who passed claims to the federal government). Liability attaches “if the subcontractor caused the presentation of false claims by the prime contractor,” even if the subcontractor did not actually submit a false claim to the prime contractor. United States ex rel. Smith v. Boeing Co., 505 F. Supp. 2d 974, 984 (D. Kan. 2007). FCA liability may also attach regardless of whether a subcontractor knows the prime contractor will submit its claim to the government. United States v. Sequel Contractors, Inc., 402 F. Supp. 2d 1142, 1151 (C.D. Cal. 2005).

2. **Performance Deficiencies**

Liability under the FCA can arise through a contractor’s deficient or otherwise inadequate performance of contract work. In Commercial Contractors, Inc. v. United States, the Federal Circuit affirmed that a contractor was liable for FCA violations based on submission of false claims for additional compensation related to its contract work. 154 F.3d 1357 (Fed. Cir. 1998). In that case, the contract required Commercial Contractors, Inc. (“CCI”) to excavate per contract drawings, but the trial court found that CCI submitted false cross-sections and quantity surveys indicating that it excavated up to the contract lines. Id., at 1363. The Federal Circuit affirmed the trial court’s holding that “CCI either knew or acted in reckless disregard of whether the... surveys it submitted in support of its claims were false.” Id., at 1363.

3. **Calculation and Certification of Claims**

Contractors can violate the FCA when submitting contract claims that “drastically” inflate the amount owed. Daewoo Eng’g and Constr. Co. v. United States, 557 F.3d 1332 (Fed. Cir. 2009). In Daewoo, the contractor submitted a $64 million claim, but was found to have inflated the amount by $50 million. See id., at 1338-41; Daewoo Eng’g and Constr. Co. v. United States, 73 Fed. Cl. 547, 585 (Fed. Cl. 2006). The contractor asserted that the government was responsible for each day of its additional performance period beyond the original performance period, “without even considering whether there was any contractor-caused delay or delay for which the government was not responsible.” Id., at 1338. The court found that the inflated claim was “negotiating ploy” built on a “baseless calculation.” Id., at 1339. The Federal Circuit affirmed the trial court’s determination that the claim was fraudulent. See id. at 1338-41. The trial court had determined the contractor’s case was “wholly without merit.” Daewoo Eng’g, 73 Fed. Cl. at 550. According to the trial
court, “the certified claim itself was false or fraudulent and plaintiff knew that it was false or fraudulent.” Id., at 585. The contractor “did not honestly believe that the Government owed it the various amounts stated when it certified the claim.” Id., at 590.

In contrast, the court in MW Builders, Inc. v. United States, 134 Fed. Cl. 469 (2017) held that a construction contractor did not violate the FCA in a case where the on-site project manager who prepared the claim was “very comfortable” about the costs claimed and believed they were “accurate.” Id., at 522. The claim was signed by MW Builders’ president, “an experienced contractor, who previously performed hundreds of millions of dollars worth of construction work for the Government over… nineteen years.” Id. Although the president’s review of the claim “was not as thorough as it could have been,” the contractor did not submit the claim with reckless disregard. The estimated costs in the claim were similar to actual costs recorded in contractor’s accounting system. Id., at 522-53.

4. Davis-Bacon Act Compliance


Under Davis-Bacon, all contractors and subcontractors performing work on federally funded or federally assisted contracts for the construction, alteration, or repair of public buildings or public works in excess of $2,000 must pay their laborers and mechanics not less than the prevailing wage rates and fringe benefits, as determined by the Department of Labor. To ensure compliance, contractors and subcontractors subject to Davis-Bacon must submit weekly wage payroll certifications for to each employee, and prime contractors are responsible for submitting copies of payrolls by all subcontractors and ensuring compliance by subcontractors. See 40 U.S.C. § 3145(a); 29 C.F.R. §§ 5.5(a)(3)(ii)(A), (a)(6).

In United States ex rel. Wall v. Circle Constr., LLC, 700 F. Supp. 2d 926, 932 (M.D. Tenn. 2010), aff’d in part, rev’d in part sub nom. United States ex rel. Wall v. Circle C Constr., L.L.C., 697 F.3d 345 (6th Cir. 2012), Circle C contracted with the Army to construct buildings at a military base. Circle C subcontracted 98% of the electrical work to a subcontractor, Phase Tech. In Circle C’s submission of payroll certifications to the government, Circle C failed to include any of Phase Tech’s employees, nor did Circle C ensure that Phase Tech complied with the Davis-Bacon prevailing wage requirements. Because Phase Tech did not pay the prevailing wage, the trial court found that the Army would not have paid Circle C the entire amount of electrical work under the contract – $553,807.71 – if the government had known about the false certifications. Accordingly, the trial court concluded that pursuant to the FCA, Circle C was liable for $1,661,423.13 (three times the amount of the government’s alleged damages).

On appeal, the Sixth Circuit affirmed and found Circle C liable for FCA violations, but reduced the damages award after finding that the government’s actual damages calculation should have been the difference between what Phase Tech was required to pay its workers and the amounts actually paid:

[A]ctual damages are the difference in value between what the government bargained for and what the government received. Here, the government bargained for two things: the buildings, and payment of Davis-Bacon wages. It got the buildings but not quite all of the wages. The shortfall was $9,916. That amount is the government’s actual damages.

United States ex rel. Wall v. Circle C Constr., LLC, 813 F.3d 616, 617 (6th Cir. 2016).
5. **Service Contract Act Compliance**

Contractors can also face FCA liability for violations of the McNamara-O’Hara Service Contract Act of 1965 (“SCA”), 41 U.S.C. §§ 6701, *et seq.*, which requires that applicable contracts with the federal government “include provisions specifying the contract’s ‘wage determination,’ which sets the wage rates and fringe benefits that must be paid to various classes of covered service employees.” *Call Henry, Inc. v. United States*, 855 F.3d 1348, 1350 (Fed. Cir. 2017). “The SCA insures that service employees who were protected by a collective bargaining agreement with one contractor are not deprived of the wages and benefits negotiated in that collective bargaining agreement when the contract they work on is competitively awarded to a new contractor.” *Id.*, at 1350.

While the SCA was intended to restrict employee remedies for violations of the SCA to administrative channels, at least one court has determined that *qui tam* relators can bring FCA claims alleging an employer “fraudulently reported to the United States that it was in compliance with the Service Contract Act.” *United States ex rel. Sutton v. Double Day Office Servs., Inc.*, 121 F.3d 531, 532 (9th Cir. 1997). Under this theory, an employer can be held to have “violated the FCA when it submitted a claim for payment to the United States falsely stating that it had complied with the SCA.” *Id.*, at 534. See also *United States ex rel. Contech v. IKON Office Sols., Inc.*, 27 F. Supp. 3d 80 (D.D.C. 2014) (“[b]ecause it is not the alleged violation of the [SCA], but rather the defendant’s alleged presentment of a false claim and false certification of compliance to the government for payment that implicates the [FCA], the plaintiff/relator has standing to bring a *qui tam* claim under the [FCA]”).

6. **Statements Made in Relation to Requests for Payment**

The submission of requests for payment to the government are a common administrative function on government contracts. The Federal Acquisition Regulation (“FAR”) provides requirements for the submission of payment requests, which are largely governed by the type of contract (e.g., fixed price, time and materials, etc.). Inherent in the payment process are certifications made by contractors to the government. These certifications, where containing false or fraudulent information “knowingly” made, may result in violations of the FCA.

   a. **Bond Premiums**

   FAR 52.232-5(g) (Payments Under Fixed-Price Construction Contracts), provides for reimbursement of bond premiums “after the contractor has furnished evidence of full payment to the surety.” In *Morse Diesel International, Inc. v. United States*, 74 Fed. Cl. 601 (2007), the contractor submitted progress payment applications seeking reimbursement for performance and payment bonds procured for the subject project. Those payment requests, however, included rebates that the surety reimbursed to the parent company of the contractor. Therefore, the requests for payment containing amounts that were reimbursed by the surety “were false and knowingly used by Plaintiff to get a fraudulent claim paid by the Government in violation of the False Claims Act.” *Id.*, at 625.

   b. **Payments to Subcontractors and Suppliers**

   FAR 52.232-5(c) provides a certification requirement for fixed-price construction contracts requiring contractors to certify that “[a]ll payments due to subcontractors and suppliers from previous payments received under the contract have been made, and timely payments will be made from the proceeds of the payment covered by this certification.... This request for progress payments does not include any amounts which the prime contractor intends to withhold or retain from a subcontractor or supplier in accordance with the terms and conditions of the subcontract.” Falsely certifying compliance with this clause in order to receive payment from the government can result in liability under the FCA.

   In *Lamb Engineering & Construction Co. v. United States*, 58 Fed. Cl. 106 (2003), the contractor (“Lamb”) entered into a fixed price construction contract. During performance, Lamb submitted five progress billings and certified that payments
had been made to its subcontractors and suppliers. With respect to its fifth invoice, Lamb requested $1,121,073.03, certified that all subcontractors had been paid from previous progress payments, and that Lamb was not withholding any amounts. However, Lamb had not fully paid its subcontractors from funds provided under previous progress payments. The court found that Lamb’s inclusion of clauses in its subcontracts “providing for it to retain funds in violation of the FAR and [Prompt Payment Act] PPA, which require that subcontractors be paid within seven days,” satisfied the FCA scietnter requirement. *Id.*, at 110–11. In addition, the court held that Lamb’s submission of a certified invoice, despite having failed to pay its suppliers and subcontractors, convinced the court that Lamb “acted knowingly, or in deliberate ignorance with reckless disregard of falsehoods, when it certified this final progress billing.” *Id.* The court held that each request for payment containing the false certification was a separate claim for which civil penalties under the FCA should be assessed.

### 7. Failure to Disclose Organizational Conflict of Interest

The FAR requires agency officials to “identify and evaluate potential organizational conflicts of interest as early in the acquisition process as possible.” FAR 9.504(a)(1). Organizational conflicts of interest (“OCI”) fall into three main categories: (a) impaired objectivity; (b) biased ground rules; or (c) unequal access to information. FAR 9.505; see also *L-3 Servs., Inc.*, B-400134.11, B-400134.12, Sept. 3, 2009, 2009 CPD ¶ 171; *Aetna Gov’t Health Plans*, B-254397 et al., July 27, 1995, 95-2 CPD ¶ 129. Most solicitations require offerors to certify no OCI exists or include a provision requiring the offeror to identify potential OCIs. Failure to meet these requirements can trigger FCA liability through the express certification theory and, even if such requirements are not incorporated into a solicitation, disclose OCIs may constitute an implied false certification under the FCA. *United States v. Sci. Applications Int’l Corp.*, 555 F. Supp. 2d 40, 51 (D.D.C. 2008); see also *United States ex rel. Ervin & Assocs., Inc. v. Hamilton Sec. Grp., Inc.*, 370 F. Supp. 2d 18, 51-52 (D.D.C. 2005) (“A government contractor’s failure to disclose an organizational conflict of interest constitutes a false claim under the False Claims Act”).

In some circumstances, FCA liability can attach when a contractor inadvertently but incorrectly certifies no OCIs exist. *United States ex rel. Harrison v. Westinghouse Savannah River Co.*, 352 F.3d 908 (4th Cir. 2003). In *Harrison*, just one of a contractor’s employees knew of the OCI, and that employee did not know that a different employee with no knowledge of the OCI had certified no OCI existed. According to the court, the single employee’s knowledge of the OCI inaccuracy was imputed to the contractor, causing the court to find that the contractor knew “that the substance of the no-OCI certification was false” when the contractor submitted the certification to the government. *Id.*, at 120.

On December 17, 2018, DOJ announced a $100,000 settlement with an offeror that falsely certified no OCI existed when bidding on a defense contract.14 The company did not admit fault, but the settlement confirms DOJ’s interest in FCA claims arising from OCIs and provides a reminder that contractors should implement processes to screen for OCIs.

### 8. Buy American Act Compliance

The Buy American Act (“BAA”), 41 U.S.C. § 8301, et seq., creates a preference for domestic construction material and products and applies to goods and services on supply and construction contracts with the federal government. Since 2016, and for the foreseeable future, compliance with the BAA and other domestic preference laws and regulations will likely be an area of increased emphasis. On April 18, 2017, President Trump issued an executive order seeking to “maximize” use of domestic preference laws such as the BAA for all Federal procurements. Exec. Order No. 13788, 82 Fed. Reg. 18837 (Apr. 18, 2017). The order requires agencies to “scrupulously” monitor and enforce these laws.


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Masonry Solutions, Inc. ("MSI") violated the FCA by seeking payment for products furnished to a federally funded construction project that were not compliant with the BAA. In its motion for summary judgment, MSI was able to convince the court that the materials were BAA compliant and the FCA case was dismissed.

9. **Contracting Set-Aside Issues**

Federal small business procurement goals are set by Congress, which requires that the government direct a portion of spending dollars – currently 23 percent – to small businesses. Additional goals for certain categories of small business include minority-owned businesses involved in the 8(a) program, women-owned small businesses, and service-disabled veteran-owned small businesses. The Small Business Administration administers programs in support of these goals and agencies can set aside contracts for participation only by small businesses or particular socio-economic categories of small businesses. Contractors found to have falsely certified compliance with SBA programs and regulations may be subject to FCA penalties and suspension or debarment from government contracting.

Liability can arise if a small business serves as a mere “pass-through” entity for a large business, as alleged by the relator in *United States ex rel. Tran v. Computer Scis. Corp.*, 53 F. Supp. 3d 104, 111 (D.D.C. 2014). In that case, the relator alleged that the large business prime contractor, Computer Sciences Corporation (“CSC”) falsely certified that it was in compliance with the Small Business Contracting Plan that had been incorporated into the prime contract when in fact large business subcontractors of the small businesses were performing the substantive work under the contract.

In March 2015, the Gilbane Building Company agreed to pay more than $1.1 million to settle false claims allegations that a company with which it merged, W.G. Mills Incorporated (“WGM”), violated the FCA by creating a front company, Veteran Constructors Incorporated (“VCI”), to receive a Coast Guard contract that was set aside for service disabled veteran-owned small businesses (“SDVOSBs”). The government alleged VCI did not perform the work required under the Coast Guard contract and instead the work was performed by WGM. Further, the government alleged that if the Coast Guard was aware WGM would be performing the work, it would not have awarded the contract to VCI. *See also LW Construction of Charleston, LLC v. United States*, 139 Fed. Cl. 254, 287-92 (2018) (holding government’s allegation of contractor’s misrepresentation regarding contractor’s SDVOSB status at bid and contract award sufficient to meet materiality requirement necessary to proceed with prosecution of government FCA counterclaim); *United States v. Strock*, 2018 WL 647471 at *6-*10 (W.D.N.Y. Jan. 31, 2018) (dismissing government FCA counts due to failure to plead materiality of contractor’s alleged false certifications of SDVOSB qualification to government’s decision to pay; granting government leave to amend complaint to adequately plead materiality).

In another matter that resulted in a settlement, Commonwealth Technologies and the companies’ owners were alleged to have made false certifications to the SBA representing that it was a small business within a Historically Underutilized Business Zone (“HUBZone”) and then used such certification to obtain Army contracts to build a courthouse in Fort Knox, Kentucky. According to the government’s allegations, Commonwealth applied for status as a HUBZone contractor but operated out of Lusk Mechanical Contractors’ offices, which were not located in a HUBZone. Further, the government noted that Commonwealth did not disclose on its SBA application that it shared facilities, equipment, personnel, insurance and bonding with Lusk. To settle the allegations, Lusk, Commonwealth and their owners agreed to pay $3.7 million and forfeit another $2.5 million seized by federal agents.


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WL 2881350 (E.D. Va. July 5, 2017) (analyzing *qui tam* allegations that defendant made false claims to the SBA as to its eligibility for the 8(a) Business Development Program).

10. **Multiple Award Schedule Compliance Issues**

The General Services Administration (“GSA”) “negotiates, awards, and manages Multiple Award Schedule (‘MAS’) contracts, which provide federal agencies with a simplified process for obtaining commercial supplies and services at fair and reasonable prices.” *United States ex rel. Frascella v. Oracle Corp.*, 751 F. Supp. 2d 842, 844 (E.D. Va. 2010) (citing 48 C.F.R. § 8.402). Through the MAS program, which encompasses GSA’s massive Federal Supply Schedule (“FSS”) program, “GSA negotiates and administers long-term, government-wide contracts, ensuring at the time of negotiation that these contract prices are fair and reasonable.” *K-Lak Corp. v. United States*, 98 Fed. Cl. 1, 2 n.3 (2011). Participating contractors agree to provide supplies and services “at stated prices for given periods of time,” 48 C.F.R. 8.402(a), and to publish a listing of the items offered with “pricing, terms, and conditions applicable to each item.” *Sharp Elecs. Corp. v. McHugh*, 707 F.3d 1367, 1369 (Fed. Cir. 2013).

Contractors who participate in the MAS program can face liability under the FCA as a result of the pricing information they must provide to GSA during the negotiation or performance of MAS contracts. See, e.g., *United States ex rel. Ubl v. IIIF Data Sols.*, 650 F.3d 445, 449 (4th Cir. 2011) (*qui tam* action alleging material false representations about prior pricing and discounting practices when applying for MAS contract); *United States ex rel. Shemesh v. CA, Inc.*, 89 F. Supp. 3d 36, 42 (D.D.C. 2015) (*qui tam* action alleging false statements in the process of negotiating the GSA MAS contract, which allegedly caused all claims submitted by the contractor under the contract to be false).

*a. Commercial Sales Practices Submissions*


*b. Price Reduction Clause Compliance*

GSA contracts also typically include a Price Reductions Clause (“PRC”), GSAR 552.238-81, “which requires GSA contractors to maintain a static relationship between GSA’s negotiated discounts or prices and those for a designated customer or category of customers.” *United States ex rel. Frascella v. Oracle Corp.*, 751 F. Supp. 2d 842, 845 (E.D. Va. 2010). Designated customers are known as Basis of Award (“BOA”) customers and are identified and agreed upon during contract negotiations. *Id.* “If the relationship between the prices charged to the government and those charged to the BOA customer changes during the life of a MAS contract, the contractor must disclose the change to GSA and offer discounts or prices that restore the static relationship.” *Id.*

FCA charges can arise if a contractor knowingly fails to comply with the Price Reduction Clause. *Id.*, at 847; see also *United States ex rel. Morsell v. Symantec Corp.*, 130 F. Supp. 3d 106 (D.D.C. 2015) (alleging contractor violated PRC by failing to disclose discounts larger than those extended to GSA). For example, in *Frascella*, the government brought FCA charges alleging “Oracle breached the PRC in its Contract by failing to report or offer to GSA certain software license discounts that Oracle purportedly gave to its commercial customers.” *Frascella*, 751 F. Supp. 2d at 846-47. According to the government, Oracle “routinely” granted its commercial customers discounts exceeding the discounts disclosed to GSA, and knowingly submitted false certifications that its commercial discount and pricing practices had remained consistent. *Id.* Additionally, the government alleged Oracle “consistently manipulated its sales of software licenses to Commercial
End Users” to evade PRC reporting obligations. *Id.*, at 847.

c. *Buy American Act / Trade Agreements Act Compliance*

GSA schedule contract holders are prohibited from selling products that fail to comply with the Buy American Act (“BAA”), discussed above, or Trade Agreements Act (“TAA”), 19 U.S.C. § 2501 *et seq.*, which requires contractors to provide country of origin information when selling products to the U.S. government and prohibits the acquisition of products made in certain countries. See, e.g., *United States ex rel. Scutellaro v. Capitol Supply, Inc.*, No. 10-1094 (BAH), 2017 WL 1422364 (D.D.C. Apr. 19, 2017). Additionally, a supplier that does not sell directly to the U.S. government faces FCA liability if the supplier causes a GSA schedule contract holder to submit false claims. *United States v. Toyobo Co.*, 811 F. Supp. 2d 37 (D.D.C. 2011). FCA liability can result when a GSA schedule contract holder knowingly and falsely certifies its products are BAA- or TAA-compliant or makes misrepresentations causing another party to sell non-compliant products and thus submit false claims. See *Scutellaro*, 2017 WL 1422364. That said, sales must occur; merely listing non-compliant product for sale under a GSA schedule contract will not create FCA liability. *United States ex rel. Folliard v. Govplace*, 930 F. Supp. 2d 123, 127 (D.D.C. 2013); *Scutellaro*, 2017 WL 1422364, at *23 (same). TAA or BAA non-compliance FCA allegations must include specific evidence that non-compliant products were sold, thus creating false claims. This can be a difficult standard to meet, particularly for *qui tam* relators who often base claims on internet research regarding country of origin data for listed goods. Lack of specificity can result in dismissal under Rule 9(b) of the Federal Rules of Civil Procedure for failure to plead fraud with particularity:

What the complaint fails to allege are any specific facts demonstrating what occurred at the individualized transactional level for each defendant. […] The fact that the defendants may have sold non-compliant products during a certain time period in violation of the TAA does not equate to the defendants making a knowingly false statement in order to receive money from the government.


Finally, without more, the mere failure to comply with TAA or BAA requirements is not deemed to be *per se* material to the government’s payment decision under the *Escobar* standard. To state a viable FCA claim, the plaintiff “must also show that… TAA compliance was material to the government’s decision to pay.” *Scutellaro*, 2017 WL 1422364, at *19; see *United States v. Comstor Corp.*, No. 11–731 (BAH), 2018 WL 1567620, at *19 (D.D.C. Mar. 31, 2018).

11. *False Estimates*

The act of underbidding a job does not by itself create liability under the FCA. However, where a contractor “knowingly” underbids a contract solicitation to increase the chances of winning an award while intending to charge more than bid, the contractor may be liable for FCA violations. In *Hooper v. Lockheed Martin Corp.*, 688 F.3d 1037 (9th Cir. 2012), a relator brought an action against Lockheed alleging, *inter alia*, that Lockheed “submit[ted] a fraudulently low bid, based on knowing underestimates of its costs, to improve its chances of winning the Air Force RSA IIA contract.” *Id.*, at 1047. Relying on First and Fourth Circuit precedents, the Ninth Circuit held “that false estimates, defined to include fraudulent underbidding in which the bid is not what the defendant actually intends to charge, can be a source of liability under the FCA…. ” *Id.*, at 1049. The discrepancy between what the contractor actually intends to charge the government and what it bids is what triggers potential FCA liability since “buying-in” to government contracts (intentionally offering the goods or services below cost in order to win the contract) is generally permitted for fixed price contracts. See *CC Distributors, Inc. v. United States*, 69 Fed. Cl. 277, 283 (2006) (“the fact that an offer [for a fixed-price contract] may not include any profit or may be an attempted buy-in (below cost) does not, in itself, render an otherwise responsible firm ineligible for award”) (internal citations omitted).
Part Three: Enforcement Trends and Notable Cases

Each year, DOJ publishes statistics regarding its FCA caseload. In Part Three, we provide an overview of DOJ’s published statistics, plus a review of enforcement trends and recent case developments.

A. DOJ Enforcement Statistics

In fiscal year 2019, DOJ recovered over $3 billion in FCA settlements and judgments. DOJ’s 2019 recovery was slightly higher than its $2.8 billion recovery in fiscal year 2018. From 1986 to the end of fiscal year 2018, FCA recoveries totaled more than $62 billion. Since 2009, DOJ has recovered at least $2 billion each year under the FCA. DOJ’s recovery in fiscal year 2019 was the ninth highest recovery in the previous 30 years.

DOJ and qui tam relators combined to file 782 FCA actions in fiscal 2019, a slight increase from 769 FCA actions filed in fiscal year 2018. DOJ initiated 146 FCA actions, an increase of almost 20% from fiscal year 2018. The number of qui tam actions fell to its lowest level in almost a decade.

Since 2009, DOJ and qui tam relators combined have filed at least 700 FCA actions each year. In the decade before 2009, the combined number of FCA actions each year was never above 700.

1. Targeted Industries

For the more than $3 billion recovered in fiscal year 2019, almost 90% related to FCA actions involving the health care industry. The government recovered $2.6 billion from participants in the industry, including drug and medical device manufacturers, managed care providers, hospitals, pharmacies, hospice organizations, laboratories, and physicians. The amount included millions of dollars for state Medicaid programs. Fiscal year 2019 is the tenth consecutive year health care fraud settlements and judgments exceeded $2 billion. Reflecting DOJ’s emphasis on combating the opioid crisis, two of DOJ’s largest recoveries involved opioid manufacturers: (1) a $195 million settlement with a company that allegedly paid kickbacks to induce physicians and nurse practitioners to prescribe opioids; and (2) a $1.4 billion settlement with a company to resolve criminal and civil liability related to marketing an opioid addiction treatment drug.

The government recovered $252 million from defense contractors in fiscal 2019, about twice as much as fiscal year 2018. In 2018, DOJ recovered $107 million related to military procurement fraud, a significant drop from 2017. DOJ’s $252 million in defense-related recovery in 2019 was slightly more than the $220 million DOJ recovered in 2017.

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18 See footnote 17.

19 See footnote 17.


2. **Qui Tam Statistics**

From 2017 to 2018, total *qui tam* recoveries fell by 34%, and *qui tam* recoveries were a lower percentage of the 2018 total (73%) compared to 2017 (92%). In fiscal year 2018, 645 *qui tam* lawsuits were filed, an average of more than 12 new cases each week. In 2019, a similar number of *qui tam* suits were filed: 633 *qui tam* lawsuits. The number of *qui tam* actions in fiscal year 2019 was the lowest since 2011. Of the $3 billion recovered by DOJ in 2019, over $2.1 billion was the result of *qui tam* matters, and the government paid $271 million to *qui tam* relators, the lowest since 2009.

**B. 2019 Developments**

The developments discussed below are relevant to FCA practitioners and show how issues may be taking shape for the coming year.

1. **DOJ Guidance for Obtaining Cooperation Credit**

On May 7, 2019, DOJ released formal guidance for DOJ litigators who handle FCA investigations identifying factors DOJ will consider, and credit DOJ will provide, when entities or individuals voluntarily self-disclose misconduct that could serve as the basis for FCA liability.22 The guidance also applies to entities and individuals that take other steps to cooperate with FCA investigations or take adequate and effective remedial measures. In addition to voluntary self-disclosure, the guidance provides a non-exclusive list of activities for which DOJ may provide credit:

1. Identifying individuals substantially involved in or responsible for misconduct;
2. Disclosing relevant facts and identifying opportunities for the government to obtain evidence;
3. Preserving, collecting, and disclosing relevant documents and information;
4. Identifying individuals aware of relevant information or conduct;
5. Making available for meetings, interviews, examinations, or depositions officers and employees with relevant information;
6. Disclosing facts relevant to the investigation gathered during the entity’s independent investigation;
7. Providing facts relevant to potential misconduct by third-party entities and third-party individuals;
8. Providing information in native format and facilitating review and evaluation of the information if special or proprietary technologies are required;
9. Admitting liability or accepting responsibility for wrongdoing; and
10. Assisting in the determination or recovery of losses.

To obtain maximum cooperation credit, a company or entity must voluntarily self-report misconduct that may be actionable under the FCA. DOJ’s guidance also provides a monetary “cap” limiting the extent to which cooperation reduces damages. Entities receiving maximum cooperation credit must still pay at least single damages (as opposed to treble damages recoverable under the FCA). The guidance includes few details regarding actions necessary to receive maximum cooperation credit. Regarding the “value” of voluntary disclosure or cooperation, DOJ will consider: (1)

timeliness and voluntariness of the assistance; (2) truthfulness, completeness, and reliability of information or testimony; (3) nature and extent of the assistance; and (4) significance and usefulness of cooperation to the government.

DOJ retains discretion to award cooperation credit, stating it “takes into account many considerations when evaluating the appropriate resolution of FCA matters, including the nature and seriousness of the violation, the scope of the violation, the extent of any damages, the defendant’s history of recidivism, the harm or risk of harm from the violation, whether the United States’ interests will be adequately served by a compromise, the ability of a wrongdoer to satisfy an eventual judgment, and litigation risks presented if the matter proceeds to trial.” The guidance reinforces existing DOJ statements regarding its expectation of cooperation, such as the September 9, 2015 policy memorandum issued by Deputy Attorney General Sally Q. Yates (“Yates Memo”). DOJ’s guidance for FCA defendants is in Section 4-4.112 of DOJ’s Justice Manual.23

2. Developments in Response to Granston Memorandum

In our 2017 and 2018 guides, we discussed the “Granston Memo,” issued January 10, 2018 by Michael Granston, Director of DOJ’s Commercial Litigation Branch, Fraud Section. The Granston Memo identified factors DOJ uses to evaluate whether to seek dismissal of meritless FCA cases under 31 U.S.C. § 3730(c)(2)(A), and the memo has remained a frequent topic of analysis among FCA practitioners.24

The principles of the Granston Memo have been formalized in the Justice Manual, which is used by DOJ prosecutors and trial attorneys nationwide. Consistent with the Granston Memo, § 4-4.111 of the Justice Manual lists factors that DOJ considers when evaluating whether to dismiss qui tam actions, including: (1) curbing meritless qui tam actions that facially lack merit; (2) preventing parasitic or opportunistic qui tam actions that duplicate a pre-existing government investigation and add no useful information to the investigation; (3) preventing interference with an agency’s policies or the administration of its programs; (4) controlling litigation brought on behalf of the United States, to protect the Department’s litigation prerogatives; (5) safeguarding classified information and national security interests; (6) preserving government resources, particularly where the government’s costs (including the opportunity costs of expending resources on other matters) are likely to exceed any expected gain; and (7) addressing egregious procedural errors that could frustrate the government’s efforts to conduct a proper investigation.

In a January 27, 2020 speech at the 2020 Advanced Forum on False Claims and Qui Tam Enforcement, Deputy Associate Attorney General Stephen Cox noted DOJ has used its authority to seek dismissal of qui tam actions “sparingly.”25 However, Cox also stated that before issuing the Granston Memo, DOJ identified approximately 45 cases for which it had sought dismissal in the previous thirty years since the 1986 FCA amendments. In just the two years since DOJ issued the memo, DOJ has moved to dismiss approximately 45-50 cases.

As we also noted in previous years, courts disagree regarding the standard for reviewing requests by DOJ to dismiss a qui tam action. Some courts recognize DOJ has full, unfettered discretion to seek dismissal. See, e.g., Swift v. United States, 318 F.3d 250, 252 (D.C. Cir. 2003) (provision gives “the government an unfettered right to dismiss an action,” meaning the government’s decision is “unreviewable”); Hoyte v. Am. Nat. Red Cross, 518 F.3d 61, 65 (D.C. Cir. 2008) (discussing

23 https://www.justice.gov/jm/jm-4-4000-commercial-litigation#4-4.112.
24 The Government may dismiss the action notwithstanding the objections of the person initiating the action if the person has been notified by the Government of the filing of the motion and the court has provided the person with an opportunity for a hearing on the motion.” 31 U.S.C. § 3730(c)(2)(A). See also U.S. Dep’t of Justice, Factors for Evaluating Dismissal Pursuant to 31 U.S.C. 3730(c)(2)(A) (Jan. 10, 2018), https://assets.documentcloud.org/documents/4358602/Memo-for-Evaluating-Dismissal-Pursuant-to-31-U-S.pdf.
“the Government’s virtually ‘unfettered’ discretion to dismiss the qui tam claim”; Riley v. St. Luke’s Episcopal Hosp., 252 F.3d 749, 753 (5th Cir. 2001) (“the government retains the unilateral power to dismiss an action notwithstanding the objections” of the relator). Other courts apply a two-step process, requiring DOJ to demonstrate a valid purpose for seeking dismissal. United States ex rel. Sequoia Orange Co. v. Baird-Neece Packing Corp., 151 F.3d 1139 (9th Cir. 1998); United States v. Academy Mortgage Corp., 2018 WL 3208157 (N.D. Cal. June 29, 2018) (denying government motion to dismiss because “the complaint ha[d] not been fully investigated,” and holding the “criteria for granting the Government’s motion to dismiss” is similar to a “‘good cause’ requirement”).

Federal courts in 2019 continued to wrestle with issues arising from DOJ motions to dismiss pending qui tam cases:

- In Chang v. Children’s Advocacy Ctr. of Delaware, 938 F.3d 384 (3d Cir. 2019), the Third Circuit held relators are not entitled to automatic in-person hearings if DOJ requests dismissal, even though § 3730(c)(2)(A) gives relators “an opportunity for a hearing” if DOJ moves to dismiss. The court held that an “opportunity” does not guarantee a hearing “unless the relator expressly requests a hearing or makes a colorable threshold showing of arbitrary government action.”

- In United States ex rel. Schneider v. J.P. Morgan Chase Bank, N.A., 2019 WL 1060876 (D.D.C. Mar. 6, 2019), the court granted DOJ’s request for dismissal after five years litigating before the trial and appellate court. Following D.C. Circuit’s decision in Swift, the court held DOJ has the “unfettered right to dismiss” a qui tam complaint.

- Two different cases applied the Ninth Circuit’s test in Sequoia, which requires DOJ to demonstrate a valid purpose for dismissal, but reached different results. In United States v. EMD Serono, Inc., 370 F. Supp. 3d 483 (E.D. Pa. 2019), the court noted that the “rational relationship standard … is consistent with the constitutional scheme of checks and balances” and that, if DOJ’s authority is unfettered, “a hearing would be superfluous, rendering the requirement of a hearing a nullity. Reducing the hearing requirement to insignificance violates a basic canon of statutory construction.” The court nonetheless held relator’s allegations lacked merit and agreed with DOJ that the case would be burdensome and contrary to the public interest. In contrast, in United States ex rel. CMZN-HCA, LLC v. UCB, INC., 2019 WL 1598109 (S.D. Ill. Apr. 15, 2019), the court denied DOJ’s motion to dismiss after applying the Sequoia test and finding that DOJ’s investigation was insufficient. The court rejected DOJ’s arguments that the case lacked merit, was contrary to important policy prerogatives of the federal government’s healthcare programs and that the case would impose disproportionate litigation costs.


- Finally, many FCA practitioners watched United States ex rel. Campie v. Gilead Sciences., Inc., 862 F.3d 890 (9th Cir. 2017) for potential implications on materiality issues, but it ended up implicating dismissal standards. At the end of 2017, Gilead petitioned the Supreme Court for certiorari, asking the Court to review whether an FCA allegation fails if the government continues to provide its approval and pay defendant after learning of alleged regulatory infractions. In November 2018, the government filed its amicus curiae brief urging the Court to decline to grant certiorari. The government argued the case was a “poor vehicle” for reviewing Escobar materiality requirements but also informed the Court that DOJ would move to dismiss relators’ complaint upon remand to the district court. The Supreme Court declined certiorari and, when the case was remanded, DOJ moved to dismiss, arguing (per the Sequoia test) that dismissal would: (1) prevent relators from undermining agency decisions regarding how to address defendant’s conduct; and (2) preserve government resources given the agency
“fully investigated” relators’ allegations and had taken actions the agency deemed appropriate. Relators argued DOJ failed to provide facts to support its arguments, but the court disagreed and granted dismissal, holding DOJ presented evidence of a “substantial” investigation into relators’ allegations and accepting the government’s argument regarding preservation of resources, agreeing that “extensive” discovery would be necessary due to relators’ allegations.

3. **Senate Judiciary Committee’s Inquiry re Granston Memo**

In last year’s guide, we discussed comments by Senator Charles Grassley (R-Iowa), Judiciary Committee chairman, criticizing what he described as “troubling developments in the courts’ interpretation of the False Claims Act.” In his 2018 comments, Senator Grassley noted his disagreement with how lower courts have interpreted and applied Escobar’s materiality standard. On September 4, 2019, Senator Grassley sent a letter to Attorney General William Barr expressing concerns that DOJ’s policy would encourage fraudsters to engage in abusive litigation tactics in an effort to persuade DOJ to dismiss *qui tam* cases. Senator Grassley sought details on the effect of the Granston Memo in DOJ efforts to dismiss *qui tam* actions.

On December 19, 2019, DOJ responded to Senator Grassley’s letter, stating DOJ’s support for the FCA and its *qui tam* provisions as “the government’s single most important tool in combating fraud.” According to DOJ, from January 2018 to December 2019, relators filed 1,170 *qui tam* actions. DOJ moved to dismiss only 45 of those cases, amounting to less than 4% of the total. Of the 45 cases, 10 involved the same for-profit relator who filed complaints that, according to DOJ, lacked merit. DOJ noted other reasons for requesting dismissal:

- 12 cases were filed by relators unrepresented by counsel and every circuit court to address the issue has held *qui tam* relators must be represented by counsel;
- In two cases, relator allegedly shorted stock in the defendant against which relator filed the *qui tam* action;
- In several cases, relator failed to allege a legally cognizable FCA claim;
- In 10 cases, agencies expressed valid concerns that enforcement could undermine patient care; and
- In one case, DOJ moved to dismiss based on concerns that classified information could be inadvertently disclosed.

DOJ noted courts issued decisions in 26 cases, granting DOJ’s motion in 25 cases while denying DOJ’s motion in one case. See *United States ex rel. CIMZNHCA, LLC v. UCB, Inc.*, 2019 WL 1598109 (S.D. Ill. Apr. 15, 2019) (discussed above). DOJ is appealing the court’s decision denying DOJ’s motion.

The long-term impact of the Granston Memo remains to be seen. However, especially now that its framework has been merged into the Justice Manual, the Memo provides litigants better insight into factors that DOJ will use in evaluating whether to affirmatively move to dismiss a *qui tam* case and, at least so far, it has led to an increase in dismissals.

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F. Notable Cases

In addition to the matters discussed above, the following cases decided in the past year are noteworthy.

1. Supreme Court Clarifies FCA Statute of Limitations

_Cochise Consultancy, Inc., et al. v. United States ex rel. Hunt_, 139 S. Ct. 1507 (2019). The Supreme Court resolved a circuit split related to the FCA’s statute of limitations. As noted above in Part 1, Section D, the government or _qui tam_ relators can file suit within six years of an alleged violation. 31 U.S.C. § 3731(b)(1). However, federal courts had split over how to apply the tolling provision in § 3731(b)(2) in _qui tam_ cases where DOJ did not intervene.

Billy Joe Hunt, the relator, alleged two contractors violated the FCA by engaging in a kickback scheme while performing a contract in Iraq. Hunt alleged the scheme took place from February 2006 through September 2006. On November 30, 2010, the FBI interviewed Hunt about his role in a separate kickback scheme. During that interview, Hunt informed the FBI of the alleged fraud. Hunt filed a complaint on November 27, 2013, more than six years after the alleged fraud but within three years after he had disclosed the fraud to the FBI. The district court held the three-year tolling period in Section 3731(b)(2), based on government knowledge, does not apply if the government declines to intervene. The district court dismissed Hunt’s complaint as time barred.

The FCA’s statute of limitations includes a tolling provision if defendant conceals an FCA violation, resulting in a delay in the government’s discovery of the wrongdoing. § 3731(b)(2). The Supreme Court held that (1) the tolling provision in § 3731(b)(2) applies even if the government declines to intervene, and (2) a _qui tam_ relator is not an “official of the United States” under the tolling provision. As a result, even if the ordinary six-year statute of limitation has expired, a _qui tam_ relator may now benefit from the extra three years under the tolling provision if the relator can show that a government official “charged with responsibility to act in the circumstances” knew or should have known the relevant facts within the limitations period but failed to act. In all cases, however, the FCA case must be brought within 10 years.

As the facts in _Cochise Consultancy_ demonstrate, for purposes of the statute of limitations, the date on which a relator learns of an alleged false claim may be irrelevant if the relator can prove that the government learned of the same alleged false claim within three years of the relator’s complaint. The Court’s decision could potentially allow relators with knowledge of fraud to sit on that knowledge for more than six years and still be able to bring a _qui tam_ suit if they can show that an “official of the United States charged with responsibility to act in the circumstances” knew or should have been aware of the allegations. Defendants in non-intervened _qui tam_ actions filed more than six years after the alleged false claim occurred will likely seek discovery to determine when and how the government first knew of the fraud if the date that triggered the statute of limitations is in dispute.

2. Government Contractor’s Failure to Disclose Inability to Meet Federal Cybersecurity Regulations is Actionable under the FCA

_United States v. Aerojet Rocketdyne Holdings, Inc._, 381 F. Supp. 3d 1240 (E.D. Cal. 2019). In May 2019, a federal court ruled for the first time that the failure by a government contractor to disclose its inability to meet U.S. government cybersecurity regulations can be actionable under the FCA. In denying a motion to dismiss, the district court held that a _qui tam_ relator adequately pleaded that Aerojet Rocketdyne’s knowing failure to comply with cybersecurity regulations met the Supreme Court’s test for materiality under _Escobar_.

Defendant Aerojet Rocketdyne manufactures aerospace and defense industry products for government agencies, including DOD and NASA. In October 2015, its former senior director of Cyber Security, Compliance and Controls,
filed a *qui tam* complaint alleging the company knowingly failed to meet the DOD rules requiring defense contractors to guard unclassified controlled technical information. According to the relator, Aerojet Rocketdyne’s computer systems failed to meet minimum cybersecurity requirements imposed by DOD and NASA, and defendant knew its systems were noncompliant based on a third-party audit. The relator alleged company officials knowingly and repeatedly misrepresented compliance with cybersecurity requirements to government officials, and the government awarded at least one contract based on the misrepresentations. The relator asserted two theories of FCA liability: false certification and promissory fraud (a/k/a fraud in the inducement). After investigating the allegations for almost three years, DOJ declined to intervene.

After DOJ declined to intervene, Aerojet Rocketdyne filed a motion to dismiss, arguing it disclosed its noncompliance with cybersecurity requirements to government customers. Because Aerojet Rocketdyne disclosed its noncompliance, it argued the relator could not meet the FCA’s “demanding” materiality standard as articulated in *Escobar*. Aerojet Rocketdyne argued that the government’s payment of claims despite its knowledge of Aerojet Rocketdyne’s purported noncompliance was proof that the noncompliance was not material. The district court disagreed, noting relator’s specific allegations that Aerojet Rocketdyne had failed to disclose the full extent of its noncompliance. The purported misrepresentations, according to the relator, persisted over time, and Aerojet Rocketdyne knowingly and falsely certified compliance with security requirements in submitting invoices.

According to the court, Aerojet Rocketdyne’s alleged failure to “fully disclose” its noncompliance was sufficiently alleged as a misleading “half-truth.” Taking relator’s allegations as true, Aerojet Rocketdyne made “partial disclosures” that could result in liability for its failure to “disclose noncompliance with material statutory, regulatory, or contractual requirements.” Thus, the court observed “the government may not have awarded these contracts if it knew the full extent of the company’s noncompliance, because how close [defendant] was to full compliance was a factor in the government’s decision to enter into some contracts.” The court also rejected Aerojet Rocketdyne’s materiality argument, which asserted that DOJ investigated the allegations and declined to intervene. According to the court, no evidence existed that “the decision not to intervene is a comment on the merits of this case.”

The court also rejected Aerojet Rocketdyne’s argument that the alleged noncompliance with cybersecurity regulations did not go to the “central purpose” of its contracts because it provides missile defense and rocket engine technology services. Under *Escobar*, material misrepresentations go to the “essence of the bargain.” The court noted that the contracts incorporated DOD and NASA cybersecurity clauses requiring Aerojet Rocketdyne to undertake specific measures before it could handle certain technical information.

3. **Fifth Circuit Addressed Whether Government Knowledge is Sufficient to Show Relator Failed to Sufficiently Plead Materiality**

*United States ex rel. Lemon v. Nurses To Go, Inc.*, 924 F.3d 155 (5th Cir. 2019). In *Lemon*, the Fifth Circuit reversed dismissal of a *qui tam* action, holding the district court erred in its materiality analysis. The case involved allegations that hospice providers fraudulently billed Medicare. The Fifth Circuit analyzed each factor identified in *Escobar* and held relators sufficiently alleged defendant violated Medicare regulations that were conditions of payment. Although not dispositive, that the statutory and regulatory requirements allegedly violated were conditions of payment is “certainly probative evidence of materiality.”

Analyzing relators’ allegations regarding government enforcement, the court noted that relators “alleged that the U.S. Department of Health and Human Service’s Office of Inspector General has taken criminal and civil enforcement actions against other hospice providers that submitted bills for ineligible services or patients, including situations where the provider failed to conduct appropriate certifications.” Relators’ allegations were sufficient to raise “reasonable inference that the Government would deny payment if it knew about Defendants’ alleged violations.” Because the court determined relators sufficiently pled that the government would deny payment in the circumstances alleged, the court held defendants’
noncompliance, as alleged by relator, was not “minor or insubstantial.” According to the court, the government would “attach importance” to the alleged violations. The court thus held that relators sufficiently established materiality.

4. **D.C. Circuit Dismissed Complaint Alleging “Novel” FCA Theory**

*United States ex rel. Kasowitz Benson Torres LLP v. BASF Corp.*, 929 F.3d 721 (D.C. Cir. 2019). The D.C. Circuit affirmed dismissal of relator’s complaint alleging a “novel” FCA theory. Relator alleged chemical manufacturers knew of adverse health effects from chemicals but failed to disclose the information under the Toxic Substances Control Act (“TSCA”). Relator alleged defendant’s failure to disclose the information deprived the government of money (in the form of fines) and property (information regarding the chemicals’ health risks). The court found that defendant’s failure to voluntarily self-report TSCA violations is a “non-starter” under FCA because, even if a company violates the TSCA, the EPA can decline to impose a penalty and not every TSCA violation results in a civil penalty.

Although the TSCA required submission of information regarding health risks posed by chemicals, any obligation to inform the EPA was not an obligation to transmit property to the U.S. government. Instead, the EPA’s right to be informed of the information was a regulatory concern. Consistent with *Escobar* and its progeny, the court noted the FCA is not a vehicle for punishing “garden-variety” regulatory violations. The court found that government regulators, not *qui tam* relators, are responsible for enforcing reporting violations: “Regulatory reporting requirements, including TSCA’s requirement to report substantial risk information, are a mainstay of regulatory agencies.” The court also noted relator’s theory was “novel” and that “the government openly support[ed] the defendants.”

5. **Public Disclosure Bar and Original Source**

*United States ex rel. Reed v. KeyPoint Gov’t Solutions*, 923 F.3d 729 (10th Cir. 2019). The Tenth Circuit reversed the district court’s holding that relator’s *qui tam* complaint was barred by the public disclosure bar. The case involved allegations that a government contractor conducting background investigations for the federal government billed for work that was inadequate or incomplete. The district court dismissed the complaint because facts “substantially the same” to relator’s allegations had been publicly disclosed in (1) criminal investigations of individual investigators performing background checks; (2) news reports about fraud in the background-investigation industry, (3) congressional hearings and audits; and (4) a *qui tam* suit against a competitor.

Although the court did not credit relator as being the original source of all allegations, the court found that relator provided unique allegations regarding defendant’s responses to internal reports of fraud, providing first-hand evidence of scienter. Given her status as an insider, the court found that relator provided new allegations that defendant’s investigators and managers knowingly tried to cover up fraud in the program.

According to the Tenth Circuit, relator’s allegations were substantially the same as allegations available in public disclosures but, according to the Tenth Circuit, the district court erred in finding relator’s allegations did not materially add to the public disclosures. The Tenth Circuit held that the district court used the wrong standard to determine if relator was an original source, failing to address whether relator materially added to the public information. A relator is an original source if he or she discloses new information that is sufficiently significant or important so that the information is capable of influencing the government’s behavior.

6. **First Circuit Finds First-to-File Bar is Not Jurisdictional**

*United States ex rel. McGuire et al. v. Millennium Labs., Inc.*, 923 F.3d 240 (1st Cir. 2019). The FCA’s first-to-file bar states that when a relator files a *qui tam* action, “no person other than the Government may intervene or bring a related action based on the facts underlying the pending action.” 31 U.S.C. § 3730(b)(5). The rule prohibits subsequent relators from bringing *qui tam* actions based on facts in a previously filed case. In *McGuire*, the First Circuit reversed its prior
precedent and held the first-to-file bar is not jurisdictional. The court followed decisions from the D.C. Circuit and Second Circuit holding arguments for dismissal under the first-to-file bar do not implicate subject matter jurisdiction. Rather, the court focused on which complaint, regardless of when filed, contained the substantive allegations relevant to the alleged fraud.

The case arose from the government’s intervention in several qui tam suits filed against Millennium Health, which settled for $227 million. The First Circuit addressed (1) which relator filed the first action and (2) how to determine which of competing relators files first. In late 2009 and early 2010, Robert Cunningham filed qui tam actions against five companies, including Millennium. In February 2011, he filed an amended complaint against Millennium. In January 2012, a different relator, Mark McGuire, filed a qui tam complaint against Millennium, alleging a different fraud scheme. In December 2014, the government intervened in McGuire’s action but not the earlier action filed by Cunningham. The district court held the first-to-file bar applied to bar McGuire’s later-filed action. The district court looked beyond the allegations in each complaint and considered extrinsic evidence, including later investigations by the government.

The First Circuit reversed, holding the first-to-file bar is not jurisdictional. Following Supreme Court precedent, the court noted neither the statutory text nor legislative history clearly state that the provision is jurisdictional. Regarding whether Cunningham or McGuire was entitled to relator’s share of the settlement, the court analyzed whether Cunningham’s earlier complaint “contained all the essential facts of the fraud McGuire alleged.” Unlike the district court, the First Circuit limited its analysis to the four corners of each complaint, proceeding claim by claim. Although Cunningham filed the earlier complaint, he provided “general” allegations rather than the “essential facts” of the fraud. Thus, the First Circuit reversed the district court, which had awarded $34 million to Cunningham, who had filed the first qui tam complaint, and awarded the entire $34 million to McGuire.

7. Consideration of FCA Materiality Standard

In 2019, courts issued several important decisions interpreting Escobar’s materiality standard. As in previous years, courts continue to focus on the effect of government action – or inaction – after learning of allegations of fraud. Courts also continue to address whether relators failed to adequately plead or establish materiality and reached different conclusions based on how the government responded, including: (1) lack of government action, such as the failure to take contractual actions to remedy the violation; (2) whether DOJ’s decision not to intervene in an FCA case is a factor supporting a non-materiality finding; and (3) whether the government continued to pay claims.

DOJ’s Intervention Decision. Some courts consider DOJ’s intervention or declination decisions when analyzing materiality. A district court in the Fourth Circuit, as part of its materiality analysis in granting summary judgment to defendant, referenced DOJ’s declination decision. United States ex rel. Taylor v. Boyko, 2019 WL 2423283 (S.D.W. Va. June 7, 2019). In granting summary judgment to defendant, the court reviewed the materiality factors identified in Escobar and noted the government “declined to intervene in this matter.” Id. Conversely, the DOJ’s decision to intervene was treated by another court as being a factor that strongly militates in favor of materiality.” United States ex rel. Longo v. Wheeling Hosp., Inc., 2019 WL 4478843 (N.D.W. Va. Sept. 18, 2019).

Another court dismissed a qui tam complaint based on the government’s continued payment after learning of the alleged fraud and DOJ’s decision declining to intervene. Cimino v. Int’l Bus. Machines Corp., 2019 WL 4750259 (D.D.C. Sept. 30, 2019). The relator alleged IBM fraudulently induced the IRS to renew a software licensing agreement, but, after investigating the allegations for four years, DOJ declined to intervene. As part of its materiality analysis, the court noted DOJ’s declination decision: “Nor is it lost on the court that, after a multi-year investigation, the United States declined to intervene in this case. Although the decision to intervene is not ‘dispositive,’ it is entitled to some ‘respect,’ especially as here when the government conducted an extensive investigation spanning four years.” Id.; see also United States v. Teva Pharm. USA, Inc., 2019 WL 1245656, at *34 (S.D.N.Y. Feb. 27, 2019) (“Appellate decisions since Escobar confirm that
summary judgment is appropriate if the Defendant introduces evidence that the Government conducted a detailed investigation and subsequently declined to take any action against the defendant. In these cases, the Government’s inaction left no genuine issue of triable fact for the jury, because the only reasonable conclusion was that the Government believed the claims meritless or would not have changed its calculus even if the allegations were true.

Continued Payment After Learning of Fraud. Other courts analyzed government action after learning of fraud, considering continued payment an “important factor” but not dispositive of materiality. United States ex rel. Campbell v. KIC Dev., LLC, 2019 WL 6884485, at *10 (W.D. Tex. Dec. 10, 2019) (“the Government’s continued payment after discovery of fraud does not necessarily preclude a finding of materiality”). According to Campbell, “there is no per se rule; continued payment is only relevant to the extent that it is probative of materiality. Therefore, courts have held that “the Government may still maintain an FCA claim if it can muster allegations, taken as true, that explain why continued payments are not probative of immateriality in the circumstances presented by a specific case.” In contrast, at least one court, when analyzing materiality in ruling on a motion to dismiss, refused to consider whether the government continued paying defendant after learning of the alleged fraud. United States v. Andover Subacute & Rehab Ctr. Servs. One, Inc., 2019 WL 4686963, at *6 n.16 (D.N.J. Sept. 26, 2019) (“Whether the Government continued to pay [defendant] is a matter for [summary judgment or] trial. Accordingly, it does not factor into the materiality analysis at [the Rule 12(b)(6)] stage.”).

D. Settlements and Other Case Developments

There have been several FCA settlements in the past year that are worthy of note, as the settlements signal where DOJ prioritizes investigative and enforcement efforts.

Failure to Satisfy Labor Category Requirements. On January 28, 2019, DOJ announced that it reached a $5.2 million settlement with a contractor for the United States Postal Service ("USPS").28 According to DOJ, the contractor falsely billed labor under a USPS contract that required the contractor to provide qualified labor and management services to augment IT services at USPS data centers nationwide. The contract included requirements to bill for personnel performing services using hourly rates established for more than 100 labor billing categories. DOJ alleged the contractor knowingly billed for personnel without education or experience identified by the categories.

Overcharging and Deficient Performance. On March 25, 2019, DOJ announced a $25 million settlement arising from fraud and corruption related to subcontracts for supporting American troops in Afghanistan.29 A subcontractor allegedly billed more than $77 million for delivering supplies to U.S. services members, received a disproportionate number of subcontracts for transporting military supplies in Afghanistan and charged inflated prices to the United States. DOJ’s investigation revealed thousands of false documents submitted by different companies to the United States for payment and, as a result, the government paid for work never performed and for work other than that described in the documents. The subcontractor also charged rates well above its competitors’ average rates. The civil FCA settlement was part of a global settlement resolving a criminal case and FCA allegations.


Cybersecurity Non-compliance. On August 1, 2019, a government contractor reached the first-ever FCA settlement related to allegations involving violation of federal and state cybersecurity regulations. The contractor agreed to pay $8.6 million in response to allegations it sold surveillance equipment to the federal government and state governments even though, according to relator, the contractor knew the equipment was susceptible to cyberattacks. The suit involved the federal government, fifteen states, and the District of Columbia. The contractor will pay a total of $6 million to state governments.

Misrepresentation of SBA Compliance. On August 20, 2019, DOJ announced a $20 million settlement with the chief executive officer of a defense contractor who was alleged to have fraudulently obtained federal set-aside contracts reserved for small businesses. According to DOJ, the CEO knowingly caused his company to falsely represent its eligibility as a small business under federal regulations. As alleged, the CEO knowingly misrepresented that his company met eligibility criteria by falsely certifying a lack of affiliation with other entities. As a result, federal agencies awarded small business set-aside contracts for which the company was ineligible. Separately, DOJ resolved claims against the company for $16 million and against the company’s former general counsel for $225,000. DOJ also obtained recoveries and guilty pleas from other entities allegedly involved in the scheme. The combined settlements totaled over $36 million, the largest ever FCA recovery from small business contracting fraud.

Conclusion

FCA standards evolve throughout each year and we will continue to monitor these developments. Please feel free to contact any of the authors or other members of Smith Pachter McWhorter PLC with questions or comments. Our team’s biographical information is presented at the end of this Guide.

Thank you.

Mr. Connor is a trial lawyer and litigator with experience in a wide variety of criminal and civil litigation matters including allegations related to mail and wire fraud, the False Claims Act, embezzlement, accounting fraud, procurement fraud, criminal antitrust violations, obstruction of justice, income tax evasion, money laundering, import/export and custom violations. Cormac has assisted clients during or in anticipation of investigations by agencies including the Department of Justice, U.S. Attorneys’ Offices, Department of Homeland Security, Department of Defense, Office of Foreign Asset Control, Department of Veterans Affairs Office of Inspector General, the IRS, the National Credit Union Administration and several State investigative agencies.

Ms. Jochum’s practice focuses on government contracts and enforcement defense. She represents government contractors in bid protests, claims and appeals and other government contracts litigation, as well as in regulatory, investigative and trial matters – including U.S. Department of Justice and Inspector General investigations, False Claims Act and procurement fraud investigations, compliance counseling, mandatory and voluntary disclosure matters, and internal investigations.

Mr. Garland represents clients in government contracts, white collar, and construction litigation matters. He performs internal investigations, provides Foreign Corrupt Practices Act compliance counseling, helps clients address potential False Claims Act issues, and provides guidance on the Federal Acquisition Regulation (FAR) and other statutes and regulations governing federal government contractors. His government contracts experience includes responding to DCAA audits, counseling contractors on GSA federal supply schedule compliance, contract changes and claim preparation, and cost allowability issues.
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Ms. Bennett has deep experience counseling clients on the investigation, defense, and resolution of white collar matters, as well as FCPA and FCA compliance counseling. She has represented Fortune 100 corporate and individual clients in matters relating to potential violations of criminal or civil fraud statutes, including the False Claims Act (FCA), the Foreign Corrupt Practices Act (FCPA), the Anti-Kickback Act, and antitrust laws, as well as oversight on independent monitor engagements.

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Ms. Griffin focuses her practice on representing contractors in contract claims and disputes with the federal government and prime-subcontractor disputes on federal and federally-funded projects. Her experience includes government cost accounting issues, audits and investigations. Her experience also includes audits and compliance investigations, procurement fraud allegations, contractor debarment and suspension, ethics and compliance programs, and internal investigations.

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A practitioner of government contract law for more than 40 years, Mr. Pachter has represented and counseled clients on fraud and compliance investigations, audits, corporate governance and ethics, and defense of *qui tam* actions. He has extensive experience in areas of defective pricing, cost determination, requests for equitable adjustment, licensing of intellectual property, subcontractor performance issues, small and small disadvantaged business matters, terminations for default and convenience, GSA schedule contracts, task order contracting, multiple awards, commercial products and requests for government information.
Mr. Rounds provides counsel on a wide range of federal and state government contract, construction, and grant issues, including contract negotiation, contract changes and claim preparation, contract termination settlements, and regulatory compliance including Buy America and other domestic preference regulations. His regulatory compliance work has included advising clients on issues that create potential or actual False Claims Act liability.

Mr. Vadiee’s practice focus is government contracts, commercial contracts, compliance, white collar and construction matters, including contract negotiation, contract terms and conditions, bid protests, contract changes and claim preparation, contract termination settlements, regulatory audit and compliance litigation and oversight on independent monitor engagements. He provides regulatory compliance counseling related to export controls, subcontractor evaluations and mandatory reporting requirements.

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