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False Claims Act and *Qui Tam* Quarterly Review

INSIDE...

Also in this issue. . .

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

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

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

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QR Citation System

For ease of reference, TAF is establishing a *Quarterly Review* citation system: [Vol. #] TAF QR [Page #] ([Date]); e.g., 5 TAF QR 7 (Apr. 1996). We will refer to the first four issues of the *Quarterly Review* as follows: April 1995 as Vol. 1; July 1995 as Vol. 2; October 1995 as Vol. 3; and January 1996 as Vol. 4.

Public Disclosure Bar and Original Source Exception

U.S. ex rel. Burns v. A.D. Roe Company, Inc. et al., Memorandum Opinion and Order, No. 3:94CV-357-H (W.D.Ky. Mar. 19, 1996)

A *qui tam* suit filed by a government employee was dismissed for lack of jurisdiction under FCA §3730(e)(4) by a Kentucky district court which found that the allegations forming the basis of the action were publicly disclosed and the relator was not an "original source." According to the court, because the relator Burns acquired his information through the Freedom of Information Act (FOIA), the suit was based upon a public disclosure. The court further held that the relator's government employee status prevented him from satisfying the original source test. According to the court, Burns could not have "independent" knowledge of the information because the Government owned the "fruits of Burns' effort," and he could not have "voluntarily" provided the information because the nature of his employment compelled his actions. Notwithstanding dismissal of the relator, the court ruled that the Government, which had previously intervened in the matter, was entitled to proceed with the action.

Fred Burns alleged in his *qui tam* action that A.D. Roe Company, Inc., a prime contractor, and numerous subcontractors filed false claims on a contract with the U.S. Navy for the modernization of the Phalanx facility at the U.S. Naval Ordinance Station. Burns was the Navy's construction representative on the project. The defendants moved to dismiss and for summary judgment based on lack of subject matter jurisdiction under §3730(e)(4) of the FCA.

Information Obtained Through FOIA Prior to Filing Suit Is Publicly Disclosed

The district court first addressed whether the *qui tam* action was based upon a public disclosure as defined by §3730(e)(4)(A). Burns had claimed that he acquired the information that formed the basis of his complaint through FOIA requests during a five month period when he was not assigned to the Phalanx project. Following U.S. ex rel. Schumer v. Hughes Aircraft Co., 63 F.3d 1512 (9th Cir. 1995), 3 TAF QR 4 (Oct. 1995), the court asserted that information cannot be deemed to be publicly disclosed if it is only theoretically available through FOIA. In this case, however, because the relator based his claim on documents he received through FOIA before he filed suit, the court found that the allegations forming the basis of his action were publicly disclosed.

Government Employee Obligated To Report Fraud Not An Original Source

The court then addressed whether Burns was an "original source" under §3730(e)(4)(B). Noting that the 6th Circuit "has not addressed the 'original source' issue," the court followed the reasoning of 1st and 9th Circuit decisions involving Inspector General auditors as relators. Comparing the relator in this case (even though he was not an auditor) to those in U.S. ex rel. LeBlanc v. Raytheon Co., 913 F.2d 17 (1st Cir. 1990), and U.S. ex rel. Fine v. Chevron U.S.A., Inc., 72 F.3d 740 (9th Cir. 1995), 4 TAF QR 7 (Jan. 1996), the court found that the nature of Burns' employment precluded him from qualifying as an original source.

As in LeBlanc, the court found that Burns was obligated as part of his job to investigate and report fraud. As a result, the "fruits of Burns' effort" belonged to his employer, the Government. Burns therefore could not have the required "independent" knowledge of the information, according to the court. Moreover, addressing the second element of the original source test — whether the relator has "voluntarily provided the information to the Government" — the court relied on the reasoning of the en banc majority in Fine to conclude that the relator did not provide the information "voluntarily" because his actions were compelled by the nature of his employment. Accordingly, the court ruled that Burns was not an original source and that it lacked jurisdiction over his complaint.

Government Allowed To Pursue Claims Against Defendants

Notwithstanding the dismissal of the relator's complaint, the Government argued that it could still pursue the claims in this action. The defendants, on the other hand, contended that the court must dismiss the Government because the relator had been dismissed.

According to the court, neither side cited any authority that resolved this issue. While the Government relied on cases interpreting prior versions of the FCA, the defendants based their argument on an "unnecessarily stilted reading of the statute." Under §3730(e)(4)(A), a court does not have jurisdiction over an action based upon public disclosures "unless the action is brought by the Attorney General" or the relator is an original source. The defendants argued that the Government did not "bring" the action; rather, it had intervened and thus did not fit into the §3730(e)(4)(A) exception.

The court disagreed with the defendants' reading of the Act. According to the court, the purpose of the FCA is to help the Government remedy fraud, and "[t]he statute is not intended to make the United States' claim dependent on the Relator's claim in any way." Noting that even the defendants conceded that the Government could bring its own FCA action against them, the court found that neither the Act nor common sense called for dismissing the Government and requiring the filing of a new complaint. Accordingly, the court deemed the action as "being now 'brought' by the Attorney General" and rejected dismissal of the Government.

Anti-Kickback and Self-Referral Violations

U.S. ex rel. Pogue v. American Healthcorp, Inc. et al., Memorandum and Order, No. 3-94-0515 (M.D.Tenn. Jan. 5, 1996)

A Tennessee district court on reconsideration vacated its 1995 decision which held that a *qui tam* relator who alleged that Medicare providers knowingly violated federal anti-kickback and self-referral statutes failed to state a claim under the False Claims Act. In the reconsideration decision, the court held that the FCA "clearly prohibits fraudulent acts even if they do not cause a loss to the government." Moreover, the court found that the relator alleged an FCA violation by claiming that the defendants concealed their illegal activities from the Government in an effort to induce the Government to pay Medicare claims it would not otherwise have paid.

According to the court, its previous dismissal was based on two alternative grounds. First, it had found that the relator Pogue failed to allege that any of the claims submitted by the defendants were themselves false. Second, the court had found that Pogue failed to allege that the Government suffered damages as a result of the submission of these claims. Pogue's motion to reconsider argued that the Government need not suffer actual damages in order to prove a FCA violation and that his allegations that the claims were submitted in knowing violation of federal anti-kickback and self-referral statutes were sufficient to render the claims false or fraudulent within the meaning of the FCA.

Damages Need Not Be Shown To State Claim

In its reconsideration decision, the district court reversed itself on the damages issue after examining Supreme Court precedent. The court cited Rex

Trailer v. United States, 350 U.S. 148 (1956), which held that "there is no requirement, statutory or judicial, that specific damages be shown" to support a claim under the Surplus Property Act. There, the Supreme Court relied on its earlier opinion in U.S. ex rel. Marcus v. Hess, 317 U.S.537 (1943), which did not explicitly address the damages issue but did affirm the judgment of the lower court which had found that failure to show actual damages does not preclude recovery under the FCA. According to the Pogue court, although Rex Trailer did not involve the FCA, the Supreme Court in that case clearly stated that it had earlier recognized in Marcus that there was no requirement under the FCA to prove damages. As a result, the district court ruled that Pogue was not required to allege facts regarding actual damages.

Fraudulent Conduct To Induce Government Payment Is Actionable

According to Pogue, by submitting claims to Medicare,the defendant West Paces Medical Center implicitly agreed to comply with all statutes, rules, and regulations governing the program. Therefore, when it submitted claims without so complying, those claims were fraudulent within the meaning of the FCA. The district court agreed with Pogue that a violation of the Medicare anti-kickback and self-referral laws also constitutes a violation of the FCA, even if there is no allegation that the services billed for were not rendered or were unnecessary.

The district court noted that in U.S. ex rel. Roy v. Anthony, 1994 WL 376271 (S.D.Ohio 1994), an FCA case involving similar anti-kickback allegations, the Ohio district court found that the alleged kickbacks could have "tainted" the claims for Medicare reimbursement and thus rendered those claims "constructively false or fraudulent."

Furthermore, the court discussed several other cases where FCA violations were based upon violations of other statutes, rules, and regulations. The court concluded that these cases make it "clear that the False Claims Act was intended to cover not only those situations in which the claims themselves are false but also those situations in which a claimant engages in fraudulent conduct with the purpose of inducing payment by the government."

For example, in Ab-Tech Construction, Inc. v. United States, 31 Fed. Cl. 429 (1994), aff'd, 57 F.3d 1084 (Fed. Cir. 1995), the Government alleged that the contractor, who had obtained a contract pursuant to the Small Business Administration (SBA) program for minority-owned business,had entered into a financial arrangement with a non-minority-owned enterprise without obtaining SBA approval and thereby submitted false claims in the form of payment vouchers for services performed. According to the Ab-Tech court, "[t]he payment vouchers represented an implied certification by [the plaintiff] of its continuing adherence to the requirements for participation in the [SBA] program." Quoting the Supreme Court in U.S. v. Neifert-White Co., 390 U.S. 228 (1968), the court stated that the FCA extends "to all fraudulent attempts to cause the Government to pay out sums of money."

Similarly, in U.S. v. Incorporated Village of Island Park, 888 F. Supp. 419 (E.D.N.Y. 1995), 2 TAF QR 10 (July 1995), the New York district court held that the FCA is violated "by one who engages in a fraudulent course of conduct that causes the government to pay a claim for money." There, the court found the defendant liable for engaging in a scheme to give preferential treatment to white applicants for HUD subsidized housing in violation of the regulations governing the HUD program.

Pogue's FCA Claim Sufficiently Alleged

The Pogue court concluded that "the False Claims Act was intended to govern not only fraudulent acts that create a loss to the government but also those fraudulent acts that cause the government to pay out sums of money to claimants it did not intend to benefit." However, the court clarified that Pogue "may bring his claim under the False Claims Act only if he can show that Defendants engaged in the fraudulent course of conduct with the purpose of inducing payment from the government."

Applying this rule, the court noted that Pogue had alleged that the Government would not have paid the defendants' claims if it had been aware of the kickback and self-referral violations. "Thus," continued the court, "Pogue suggests that Defendants concealed their illegal activities from the government in an effort to defraud the government into paying Medicare claims it would not have otherwise paid." Therefore, the court found that Pogue had alleged facts upon which a claim under the FCA could be based.

False Claims Involving Compliance with Environmental Laws

U.S. ex rel. Pickens v. Kanawha River Towing et al., 1996 WL 56092 (S.D.Ohio Jan. 23, 1996)

Tugboat operators who allegedly dumped bilge and violated the Clean Water Act (CWA) while working on a government dam project may be liable under the False Claims Act, according to an Ohio district court. Moreover, the court found that the failure to keep records of environmental violations in order to avoid payment of CWA fines may constitute a "reverse false claim" under the FCA.

In 1993, Earl Pickens filed a two count *qui tam* complaint against the defendants, contractors for the construction and repair of the Gallipolis Lock and Dam, in connection with their pollution of the Ohio River. Pickens worked for one of the subcontractors on the project. He alleged that, in providing services on the Gallipolis project, the subcontractors' tugboat dumped its bilge containing hazardous substances into the river. Moreover, the subcontractors did not keep records of the discharges from their vessel as required by the Clean Water Act. The defendants moved to dismiss Pickens' complaint under F.R.C.P. 12(b)(6) for failure to state a claim.

Affirmative False Statement Not Required To State §3729(a)(1) Claim

Pickens' first count alleged that the contract with the Government, as well as the relevant subcontracts, required compliance with the CWA,and that the subcontractors violated the FCA by submitting their bills to the contractor without acknowledging that they were in violation of the CWA. Therefore, when the contractor submitted its invoice to the Government, it falsely certified that it was in compliance with the contract.

The defendants, relying upon U.S. ex rel. Stevens v. McGinnis, Inc. et al., 1994 WL 799421 (S.D.Ohio 1994), argued that a subcontractor does not violate the FCA by submitting a false invoice to a government contractor. The district court, however, clarified that the FCA is in fact violated when a subcontractor "causes" a general contractor to submit a false claim to the Government. The court explained that "[a]lthough McGinnis is factually similar to the case at bar, it supports a cause of action in this instance." Unlike here, in McGinnis the contractor did not bill the Government for the subcontractor's work, and thus the subcontractor did not cause a false claim to be made.

The defendants further argued that Pickens failed to allege that an affirmative false statement had been made to the Government, and that such an affirmative statement is necessary to state a claim under FCA §3729(a)(2) (the "false record or statement" liability provision). The court, however, responded that an affirmative statement is not necessary to state a claim under §3729(a)(1) (the "false or fraudulent claim" liability provision). The court cited U.S. ex rel. Fallon et al. v. Accudyne Corp. and Alliant Techsystems, Inc., 880 F. Supp. 636 (W.D.Wisc. 1995), 2 TAF QR 1 (July 1995), for the findings that "an allegation that a party sought payment from the government while in material noncompliance with a provision of the contract states a claim under §3729(a)(1)" and that "the standard government certification form might constitute an affirmative false statement under §3729(a)(2)." Accordingly, the court denied the defendants' motion to dismiss Count I.

"Reverse False Claim" Sufficiently Alleged

Pickens' second count alleged a "reverse false claim" under §3729(a)(7), which establishes liability for making or using false statements or records to conceal or decrease an obligation to pay money to the Government. According to Pickens,the defendants failed to report their discharge of bilge into the Ohio River, or to keep transfer records, as required by the CWA. By doing so, the defendants avoided payment of fines owed to the Government under the CWA.

The district court first determined that "a reverse false claim requires more than a mere failure to report a violation of another statute." According to the court, the language of §3729(a)(7) "mandates that the defendant prepare, create or submit some type of statement or record that is false," and "[a] failure to report does not count as a statement or record."

Nevertheless,the defendants here not only failed to report their bilge discharge but also failed to record their actions in the tugboat's log. And,asserted the court, the vessel's log "is clearly a record. If the log excludes a major event that it should ordinarily contain, the record is a false one." Moreover, "[i]f the government relies upon or otherwise reviews such logs as part of its regulatory role, then the Defendants would have submitted a false report in order to avoid an obligation to the government."

The defendants argued that they were not obligated to make the log. The court, however, stated that the FCA "does not require that the false record be one that the defendant is under an obligation by law to maintain."

The defendants further argued that, even if a CWA violation can give rise to a false claim, Pickens had not sufficiently alleged a CWA violation. The court responded that the defendants' reading of the CWA and the applicable regulations was incorrect. The CWA did apply to the discharge of the tugboat's bilge. Accordingly, the court found that Pickens had made sufficient allegations of a CWA violation and had stated a claim under §3729(a)(7) of the FCA.

CWA Does Not Preempt FCA

The defendants also argued that Pickens' FCA claims were preempted "by the more specific remedial provisions of the CWA." In rejecting this argument,the district court asserted that federal law disfavors preemption of one federal law by another absent express preemptive intent. Moreover, according to the court, the Supreme Court case relied upon by the defendants "appears to be limited to attempts to enforce a more specific federal statute by use of 42 U.S.C. s 1983" and stands for the proposition that "implied preemption is only appropriate for purely remedial acts when the statute to be enforced provides its own specific and detailed remedies."

The court asserted that,in contrast to Section 1983, the FCA "is not a purely remedial statute. It provides remedies for different conduct than the conduct covered by the CWA." Furthermore, the FCA provides for different relief (fraud damages and statutory penalties) than the CWA. Thus, Pickens' FCA claims were not preempted by the CWA.

Rule 9(b) Satisfied

In addition, the defendants argued that Pickens failed to plead fraud with particularity as required by F.R.C.P. 9(b). The court disagreed. The defendants cited two paragraphs of the complaint which merely repeated language of the FCA. However, according to the court, the rest of the complaint provided "a description of the parties involved, the exact contract at issue, and the provision of the contract that pertains to the misconduct alleged and the approximate time of the misconduct. All of which provides the Defendants adequate notice of the alleged fraud."

Venue Not Improper

Finally, the defendants argued that venue was improper in the Southern District of Ohio under FCA §3732(a), which states that an FCA action "may be brought in any judicial district in which the defendant, or in the case of multiple defendants,any one of the defendants can be found, resides, transacts business, or in which any act proscribed by section 3729 occurred." In particular, they asserted that they did not transact business in Ohio and that the Gallipolis Lock and Dam is in fact in West Virginia. The district court, however, found that "some" of the alleged FCA violations "occurred in part" within its judicial district. That is, the defendants had a contract with the Army Corps of Engineers based in Cincinnati, and therefore any false certifications and claims for payment under that contract would have occurred in Cincinnati.

Editor's Note: In a factually similar case also pending in the Southern District of Ohio, a magistrate judge's report and recommendation makes findings consistent with the Pickens decision. See U.S. ex rel. Stevens v. McGinnis, Inc. et al., Report and

Recommendation, No. C-1-93-442 (S.D.Ohio Feb. 16, 1996). A discussion of Stevens will appear in the TAF Quarterly Review after the district court judge has ruled upon the magistrate's decision.

§3732(a) Jurisdiction and Venue

U.S. ex rel. Thistlethwaite v. Dowty Woodville Polymer Limited et al., 1996 WL 15695 (S.D.N.Y. Jan. 17, 1996)

A New York district court dismissed an action against three foreign defendants for lack of jurisdiction under FCA §3732(a) because none of the defendants resided, transacted business, could be found, or violated the FCA within the judicial district. According to the court, §3732(a) is not only a venue provision but also a "geographically-limited grant of subject-matter jurisdiction."

In 1994, Jeffrey Thistlethwaite sued Dowty Woodville Polymer Limited and two of its employees for FCA violations in connection with Dowty Woodville's sale of aircraft wing slot seals to the U.S. Air Force. The Government intervened in the action and filed an amended complaint. The defendants moved to dismiss on the grounds that the court lacked subject matter and personal jurisdiction and that the district was an inconvenient forum. All three defendants were residents of England, and none had any significant contacts with the Southern District of New York. There did appear to be significant contacts with California and Oklahoma, however. The relator, also a resident of England, had filed the action in New York for reasons of convenience.

§3732(a) Limits Jurisdiction As Well As Venue

The defendants argued that the court lacked jurisdiction under FCA §3732(a), which states that an FCA action "may be brought in any judicial district in which the defendant, or in the case of multiple defendants, any one of the defendants can be found, resides, transacts business, or in which any act proscribed by section 3729 occurred." Thistlethwaite responded that §3732(a) is merely a limitation on venue and that it is trumped in this case by the Alien Venue Act, 28 U.S.C. 1391(d), which permits an alien to be sued in any district.

Relying on the legislative history of the 1986 amendments to the FCA, the district court found that §3732(a) limits jurisdiction as well as venue, describing the provision as "a geographically-limited grant of subject-matter jurisdiction." Accordingly, the court dismissed the amended complaint, without prejudice, for lack of jurisdiction "[b]ecause no defendant in this case can be found or resides or transacts business or violated the [FCA] in this district."

Knowledge Standard

Izieh Abdelkhalik v. U.S., 1996 WL 41234 (N.D.Ill. Jan. 30, 1996)

A grocery store that had been involved in the exchange of food stamps for cash instead of food violated the False Claims Act according to an Illinois district court. The court ruled on summary judgment that the undisputed facts showed at least sufficient "reckless disregard" by the store to conclude that the store had "knowingly" submitted false claims.

Store Manager Acted with "Reckless Disregard" of the Truth

The store manager testified that he neither was involved in the food stamp trafficking nor knew of employees engaging in such trafficking. However, he also testified that he sometimes left the cash register unlocked and unattended when "friends" or "gangs" were in the store. According to the court, had the manager followed the typical business practice of counting the money in the cash register at the end of the day, he would have been alerted that substantial sums of money were missing on the days that the food stamp violations occurred. This lack of supervision demonstrated at least "reckless disregard" with respect to certifying that the food stamps had been accepted in compliance with all program requirements. As a result, the court found that the store had "knowingly" submitted false claims in violation of the FCA.

$5,000 is Appropriate Civil Penalty for Each False Claim

The Government requested a civil penalty of $7,500 for each violation, arguing that trafficking is the most serious offense under the food stamp regulations. While the court recognized the seriousness of the offense, it found that the Government had failed to indicate any aggravating circumstances that would warrant that elevated amount. Therefore, the court imposed the minimum $5,000 penalty for each of the two food stamp redemption certificates presented to the Government in violation of the FCA.

Self-Critical Analysis Privilege

U.S. ex rel. Falsetti et al. v. Southern Bell Telephone and Telegraph Company, *1996 WL 32767 (N.D.Fla. Jan. 25, 1996)*

The defendant cannot assert a "self-critical analysis" privilege to withhold certain discovery from the plaintiffs because such a privilege does not exist in an FCA *qui tam* action, ruled a Florida district court.

This *qui tam* suit alleged that Southern Bell Telephone and Telegraph Company billed the Government for telephone access lines which it knew were out of service, billed for services not provided, and failed to provide required refunds. The instant ruling followed plaintiffs' motion to compel documents pertaining to an internal investigation conducted by Southern Bell for purposes of a related inquiry by the Florida Public Service Commission. Southern Bell asserted three privileges: attorney-client, attorney work product, and self-critical analysis. The district court rejected the attorney-client and attorney work product privilege claims, citing defendant counsel's earlier promises not to raise such claims.

The court noted that a self-critical analysis privilege, which protects information gathered pursuant to a company's internal investigation, has been recognized by some district courts. While the privilege has not been universally accepted or applied, this particular district court had recently applied a self-critical analysis privilege to a company's retrospective assessment of its compliance with environmental regulations. *See* Reichhold Chemicals, Inc. v. Textron, Inc., 157 F.R.D. 522 (N.D.Fla. 1994). There, the court stated that its power to recognize a new common law privilege should not be exercised expansively, but that a privilege should be recognized when it "promotes sufficiently important interests to outweigh the need for probative evidence." The court noted that in both Reichhold and the case at hand the documents at issue did not contemporaneously record events giving rise to the plaintiffs' allegations. Instead, the documents contained information regarding past events, gathered and analyzed after-the-fact, which arguably the plaintiffs could gather and analyze for themselves.

Nevertheless, stated the court, because the claims in this case arose under the FCA (unlike in Reichhold), it was first necessary to determine whether Congress in enacting the FCA considered the competing interests surrounding a self-critical analysis privilege. Reviewing the 1986 amendments to the Act and their legislative history, the court noted that Congress provided for reduced damages for defendants who conducted internal investigations and voluntarily brought the information to the Government. 31 U.S.C.3729(a). The court found that Congress had already considered the competing interests and provided its own version of a self-critical analysis privilege. Therefore, the court ruled that a self-critical analysis privilege does not exist in an FCA action.

U.S. ex rel. Schumer v. Hughes Aircraft Co. (CD CA No. CV-89-390-MRP)

In February 1996, Hughes Aircraft Co. filed a petition for writ of certiorari with the Supreme Court seeking review of several issues previously decided by the 9th Circuit in favor of relator William Schumer. *See* U.S. ex rel. Schumer v. Hughes Aircraft Co., 63 F.3d 1512 (9th Cir. 1995), 3 TAF QR 4 (Oct. 1995). In its petition, Hughes argues that the Courts of Appeals are divided on whether the 1986 jurisdictional amendments can be retrospectively applied to pre-1986 conduct, whether government disclosures to company employees and the availability of government documents through the Freedom of Information Act (FOIA) constitute public disclosures, and whether injury to the public fisc is an essential element of a cause of action under the FCA. Hughes also challenges the constitutionality of the *qui tam* provisions, which thus far has been upheld by every federal court to have addressed the issue.

U.S. ex rel. LeBlanc v. Raytheon Company, Inc. (D MA No. 88-2363-T)

In February 1996, the Supreme Court denied the petition for certiorari filed by the relator LeBlanc, letting stand a lower court dismissal of his *qui tam* suit on jurisdictional grounds. The suit had alleged that Raytheon made false and fraudulent claims in connection with the Patriot Missile's performance capabilities. The district court ruled that the public disclosure bar precluded the relator's suit from going forward because the relator would not have known about the Patriot's defects "but for" public disclosures in congressional hearings and news articles. That decision was subsequently affirmed by the 1st Circuit, which summarily adopted the district court's opinion. *See* U.S. ex rel. LeBlanc v. Raytheon Company, Inc., 62 F.3d 1411 (1st Cir. 1995), 3 TAF QR 6 (Oct.1995).

SPOTLIGHT

GAO Releases Study of DOD Voluntary Disclosure Program

Qui Tam Actions Shown to Provide Necessary Check on Contractor Voluntary Disclosures

In its recently released study of the Department of Defense's Voluntary Disclosure Program, the General Accounting Office recognized the necessary complementary role of *qui tam* in the Government's anti-fraud enforcement strategy. Responding to an inquiry from Senator Charles Grassley, Chairman of the Senate Judiciary Subcommittee on Administrative Oversight and the Courts,GAO found "little overlap" between *qui tam* actions and DOD voluntary disclosures as only 4 of the 129 voluntary disclosure cases completed since the program began a decade ago involved *qui tam* suits. Still, GAO noted that in one of these cases the Government benefited substantially from the *qui tam* action, which "(1) provided a road map essential to the government's case, (2) identified additional fraudulent activity, and (3) increased the amount of money recovered by the government." The findings in the February 1996 GAO Report undercut contractor efforts to amend the law to immunize companies that "voluntarily disclose" from private lawsuits under the False Claims Act.

GAO's findings support that corporate voluntary disclosures of their own wrongdoing cannot substitute for the information and assistance that *qui tam* relators can provide the Government. As one DOD official pointed out in the Report, voluntary disclosures and *qui tam* actions "complement each other" and *qui tam* suits "act as a 'check and balance' to the [Voluntary Disclosure] program and contractor honesty." (In fact, although not specifically cited by GAO, the largest *qui tam* case to date involved an inadequate voluntary disclosure. According to the lawsuit filed by Douglas Keeth, a former vice president of finance at United Technologies Corporation, UTC misrepresented facts to DOD in disclosing inflated progress payment billings by its Sikorsky Aircraft Division. The company ultimately paid $150 million to the Treasury for its misconduct. *U.S. ex rel. Keeth v. United Technologies Corporation, D CT, No. H-89-323, settlement March 30, 1994.*)

Few Disclosures and Modest Recoveries

DOD's Voluntary Disclosure Program was established in 1986 to encourage contractors to come forward with evidence of their own wrongdoing and, in turn, receive more lenient treatment, including decreased civil, criminal, and administrative liability. Under the criteria for acceptance into the program, the disclosing contractor must (1) not be motivated by imminent detection, (2) be a business entity, (3) take prompt and complete corrective actions, and (4) fully cooperate with the Government in any ensuing investigation or audit.

Despite strong incentives to participate in the program, GAO found that the number of voluntary disclosures has been "relatively small" and the dollar recoveries "modest." Of the more than 32,000 contractors doing business with DOD, the Department reported that, through

September 1994, 138 contractors made 325 voluntary disclosures, with 48 of the top 100 contractors accounting for 222 disclosures. Of the program's 129 closed cases, about 63% had reported recoveries of less than $100,000, with 40% having zero dollar recoveries. Moreover, GAO found that DOD's reported figure of $290 million in program recoveries was overstated because it included $75 million in premature progress payments as well as funds from disclosures made prior to the start of the program.

Limited Contractor Cooperation

The GAO Report identified several shortcomings in the Voluntary Disclosure Program. For example, DOD has accepted some disclosures that DOJ considered to be "triggered by imminent government discovery" and therefore not eligible for admission. And once accepted into the program, some contractors have failed to cooperate. A DOJ official observed that "few companies provide the government all its witness interview memoranda and that fewer still agree to provide the government a 'road map' of the cases ...." Beyond withholding documents,GAO also cited destruction of records as a problem.

Low Priority and Slow to Closure

A variety of practical difficulties have hindered the DOD program according to GAO. Case management has been a "low priority," which together with "less than full contractor cooperation" has slowed completion of the matters. Investigative agencies have not systematically submitted progress reports as required, and necessary meetings are not being held because of limited staffing and other constraints. Moreover, DOD has "not been following up to ensure that the DOD requirements were met and cases were handled expeditiously."

GAO reports that it has taken an average of 2.8 years to close voluntary disclosure cases, with about 25% taking over 4 years. As of September 1994, open cases averaged 3.5 years, with more than 65% of the cases disclosed in fiscal year 1990 still open. Overall, more than half the disclosures made since the program began are reported as open. And the open case load is growing: The number of open cases at the end of fiscal year 1994 was greater than it was at the end of fiscal year 1990 despite a decline in the number of disclosures over the past 4 fiscal years.

Frequent Violations: Mischarging and Product Substitution

According to DOD, the most common types of violations disclosed have been contract mischarging and product substitution, accounting for 57 and 32 closed cases respectively. Other disclosures have involved overpricing of contracts under the Truth in Negotiations Act, false claims or statements, and excessive progress payments.

Copies of the Report, "DOD Procurement, Use and Administration of DOD's Voluntary Disclosure Program" GAO/NSIAD-96-21, can be obtained from GAO by calling (202) 512-6000 or by using fax number (301) 258-4066. On the Internet, the Report may be found at http://www.gao.gov/reports.htm.

INTERVENTIONS AND SUITS FILED/UNSEALED

U.S. ex rel. Dobrowolski v. United Telecontrol Electronics (D NJ No.__)

A *qui tam* suit alleging that United Telecontrol Electronics (UTE) made false claims in connection with the Maverick Missile Launcher has recently been reported. According to the lawsuit, filed in 1989 and subsequently joined by DOJ, UTE falsely represented that components conformed to the applicable specifications, deviated from required quality assurance procedures, and failed to disclose product defects to the Government. The relator, formerly a product assurance supervisor at UTE, was allegedly instructed not to document findings of cracks in lugs and to conduct inspections after hours so federal inspectors would be off site and unaware of any problems. Mr. Dobrowolski was further directed to send the cracked lugs to the machine shop to be secretly "dressed out" by sanding or filing. In connection with its wrongdoing, UTE as well as a vice president, two quality control supervisors, and an engineer have reportedly pleaded guilty to charges of conspiracy to defraud the Government. The company was fined $250,000, has gone into bankruptcy proceedings, and is no longer in operation. Alice W. Ballard of Samuel and Ballard (Philadelphia, PA) is representing the relator.

Petar Lekich v. Fluor Daniel Corp. and Fernald Environmental Restoration Management Corporation (SD OH C-1-95-886)

In October 1995, a §3730(h) retaliation claim was filed alleging that Fluor Daniel Corp. and its subsidiary Fernald Environmental Restoration Management Corporation (FERMCO) retaliated against company employee Petar Lekich for assisting in a *qui tam* case previously brought against them by employee William Watt (SD OH C-1-93-852). The Watt suit, in which DOJ declined to intervene, alleged that the defendants inflated cost estimates and fabricated data in connection with the cleanup of a former uranium processing plant. According to Mr. Lekich's §3730(h) complaint, after he was identified as a confidential source of information to Watt and extensively interviewed by defense counsel in the Watt case, Lekich was removed from his management position and "reassigned" to a clerk/typist job. Mr. Lekich's counsel is William H. Blessing (Cincinnati, OH).

U.S. ex rel. Aranda and DeWitt v. Community Psychiatric Centers of Oklahoma, Inc. (WD OK No. 94-608-A)

In January 1996, DOJ filed an amended complaint in a *qui tam* suit alleging that CPC Southwind Hospital in Oklahoma City, operated by Community Psychiatric Centers of Oklahoma, Inc. (CPCO), fraudulently billed Medicare, Medicaid, and CHAMPUS for psychiatric services that were not provided or were performed by inappropriate personnel. The lawsuit was originally brought by Lisa Aranda and Gayle DeWitt in 1994, and was joined by the Government the following year. Ms. Aranda is a former nurse at CPC Southwind, where two of Dewitt's children have also worked. According to the complaint, CPCO improperly altered medical records to pass state and federal hospital inspections and sometimes billed twice for the same treatment. The suit further alleges that CPCO provided inadequate and unsafe treatment to adolescent patients admitted for sexual problems, resulting in sexual abuse among the patients. The relator is represented by Loren Gibson of McCaffrey & Tawwater (Oklahoma City, OK). Handling the matter for the Government are Assistant U.S. Attorney Robert Bradford and Scott Dahl of the DOJ Civil Division.

U.S. ex rel. Graber v. The City of New York et al. (SD NY 93 Civ. 8984)

The Department of Justice has intervened in a *qui tam* suit alleging that the City of New York, its Child Welfare Administration (CWA), the State of New York, and other city and state departments routinely submitted false claims in order to obtain millions of dollars in funding for certain foster care services that were never provided. The relator, Bracha Graber, has been employed for more than 10 years in several divisions of the City's foster care agencies. According to the lawsuit, by falsely representing they were providing the mandated services and protections, the defendants improperly diverted federal funds furnished to ensure quality foster care. Specifically, the City, with the knowledge of high ranking CWA officials, failed to conduct case reviews every six months as required by federal law. The suit further alleges that CWA employees entered false data into the state computer system to reflect the timely provision of services that were in fact never rendered.

According to the Government, the State of New York obtained over $37 million between 1990 and 1994 in federal incentive funding knowing that it did not meet the requirements for those funds. In particular, the State had not satisfied the requirement that 90 percent of its foster care cases comply with certain mandatory statutory protections for foster children. Carl Loewenson of Morrison & Foerster (New York,NY) is representing the relator. Assistant U.S. Attorneys Glenn C. Colton and Sara L. Shudofsky are handling the case for the Government.

U.S. ex rel. Oberman v. McDonnell Douglas Corporation (CD CA No. CV-91-3139)

In February 1996, DOJ intervened in a *qui tam* suit alleging that McDonnell Douglas Corporation improperly billed the Government for repair costs for defective assembly tools on the C-17 cargo jet. According to the lawsuit, filed in 1991 by former company senior engineer Douglas Oberman, McDonnell Douglas accepted delivery of hundreds of large-scale aircraft tools that had major defects and charged the Government, rather than the subcontractors who built the tools, for the repair costs. McDonnell Douglas further misrepresented the severity of the problems to the Air Force. The equipment at issue is used to hold and align sections of the plane as it is being built. The relator is represented by Phillip Benson (Newport Beach, CA) and Donald Warren of Monaghan & Warren (San Diego, CA).

U.S. ex rel. Aflatooni v. Kitsap Physician Services et al. (WD WA No.__)

In March 1996, a *qui tam* suit was unsealed alleging that Kitsap Physician Services (KPS), Northwest Diagnostic Imaging, Inc., Pathology Associates of Kitsap County, and several individuals colluded to receive illegal reimbursements from Medicare. The action was filed in January by a longtime member of KPS, Dr. Alfred Aflatooni. KPS is a physician-owned insurer that until about four years ago was also a Medicare subcontractor of Washington Physician Services. According to the lawsuit, claimed procedures were rendered by a select group of physicians who were shareholders or partners of the companies providing the services. The excessive claims allegedly were made possible by tampering with the standard allowable maximum charges programmed into the computers that calculate reimbursement. In addition to kickbacks, the complaint cites billing for services never provided, upcoding, improper cost reportings, and grant or program fraud. DOJ has declined to intervene in the action. Larry G. Johnson (Seattle, WA) is the relator's counsel.

Settlements

Pneumo Abex Corporation

In January 1996, DOJ announced that Pneumo Abex Corporation agreed to pay the Government $12.5 million to settle allegations of labor mischarging in connection with the supply of hydraulic valves. According to DOJ, the Abex Aerospace Division improperly charged cost overruns on fixed price contracts as "general and administrative" expenses. The settlement resolves allegations under the False Claims Act and related contract disputes. The improper accounting practices were identified by the Defense Contract Audit Agency and investigated by the Naval Criminal Investigative Service, the Air Force Office of Special Investigations, and the Army Criminal Investigations Division. Los Angeles Assistant U.S. Attorney Consuelo Woodhead handled the matter for the Government.

U.S. ex rel. Relator v. Healthwest Regional Medical Center et al. (WD WA No. __)

In February 1996, DOJ announced that Sutter Memorial Hospital of Sacramento, California agreed to pay the Government $1.265 million to settle allegations of improper billing for cardiac device implant procedures that it had been advised were not covered by Medicare. Pursuant to the settlement, Sutter will be dismissed from a pending *qui tam* lawsuit against over 130 hospitals for Medicare misbilling. According to DOJ, between 1986 and 1994 participating Medicare hospitals were advised that the federal program would not reimburse for procedures involving "investigational devices," that is, devices that had not received final approval for marketing from the Food and Drug Administration. The hospitals were notified, both in correspondence and written manuals specifying coverage, that the implant procedures were not considered "reasonable and necessary" and therefore were not covered. In addition to its settlement payment, Sutter agreed to implement internal remedial measures to ensure future compliance, including establishing a confidential disclosure program for improper billings and conducting a training session for employees. The relator was represented by Phillip Benson (Newport Beach, CA) and Donald Warren of Monaghan & Warren (San Diego, CA).

U.S. ex rel. Wood v. KCI Holdings Inc. (D DC No. __)

In February 1996, DOJ announced that KCI Holdings Inc. agreed to pay the Government $305,000 to settle a *qui tam* suit alleging that the Maryland consulting company overcharged four federal agencies for computer services used in designing and drafting plans for construction projects. According to the lawsuit, brought in 1994 by former company employee William Wood, KCI and its affiliates and joint ventures overbilled on contracts with the Departments of Defense, Transportation, and Agriculture, the General Services Administration, and on federally funded state contracts. The projects involved highway construction, office building renovation, and transportation operations in Washington, D.C., Maryland, Virginia, Pennsylvania, and Delaware. The relator's share was 15 percent or $45,750.

Corning Clinical Laboratories, Inc.

In February 1996, Corning Clinical Laboratories, Inc., formerly known as Bioran Medical Laboratories, agreed to pay the Government $6.675 million to settle False Claims Act allegations involving fraudulent reimbursement of laboratory tests by Medicare and other government programs. The agreement resolves claims that Bioran manipulated doctors into receiving medically unnecessary tests for serum irons whenever doctors ordered certain basic blood series performed on automated equipment. In the past, Bioran had included a serum iron as one of the tests performed on the "SMAC" machine and billed to Medicare as part of a series. But starting in 1989, whenever a doctor ordered a SMAC series, Bioran billed separately for the iron test even though the test continued to be performed on the SMAC machine. Bioran did not notify doctors of the billing change, and the number of serum iron tests it billed to Medicare annually increased from a few hundred in 1988 to over 100,000 in 1991. As a result of

Bioran's practices, losses were also incurred by CHAMPUS, the Railroad Retirement Board, the Office of Personnel Management, and state Medicaid programs. Representing the Government were Massachusetts Assistant U.S. Attorney Susan Winkler and Laurence Freedman of the DOJ Civil Division.

Philips Electronics North America Corporation

In February 1996, DOJ announced that Philips Electronics North America Corporation agreed to pay the Government $65.3 million to settle allegations that Philips sold improperly tested capacitors and resistors for a number of military and aerospace programs. According to DOJ, the settlement is one of the largest ever involving allegations that a defense contractor sold electronic components to the Government that failed to meet military specifications. The agreement covers capacitors sold from 1983 through 1992 by Philips' Jupiter, Florida operation and resistors sold by Philips' Mineral Wells, Texas facility during the same period. The settlement resolves the company's potential liability under the False Claims Act and Lanham Act. (Many of the resistors and capacitors sold by Philips bore the "JAN" certification mark as an indication they were made and tested in accordance with military specifications.) Thelma Colbert, an Assistant U.S. Attorney in Fort Worth, represented the Government.

DOJ stated that the Government was unaware of any field systems failures attributed to Philips' components. However, the company admitted that "in a significant number of instances" its Florida facility falsified test reports for capacitors and did not report test failures. The company also acknowledged that certain assembly and testing processes that were required to be performed in its Florida facility actually were performed in a Dominican Republic factory. Philips further admitted that its Texas facility falsified test results for resistors and did not disclose test failures. In a related matter last June, Philips pleaded guilty to 18 criminal counts and paid the Government $9 million in criminal fines, which were not included in the civil settlement.

Philips' sale of nonconforming capacitors was the subject of a 1992 report that the company submitted to DOD under the Department's Voluntary Disclosure Program. In connection with that disclosure, Philips has paid the Government $9.6 million,and will receive a credit for that amount under the False Claims Act agreement.

U.S. ex rel. Hughes v. Deloitte & Touche, LLP et al. (WD WA No. C95-594WD)

In March 1996, Deloitte & Touche, LLP agreed to pay the Government $396,000 to settle a *qui tam* suit brought by David Hughes in 1995. According to the lawsuit, the accounting firm submitted false claims in connection with consulting contracts with the Bonneville Power Administration and the Department of Justice. Specifically, Deloitte's invoices contained charges for hours and per diem expenses that were not compensable or reimbursable. The relator is a former employee of Deloitte. The relator's share was $68,500. Steve Berman and Jeffrey Sprung of Hagens & Berman (Seattle, WA) represented Mr. Hughes. Assistant U.S. Attorney Harold Malkin handled the case for the Government.

Circa Pharmaceuticals Inc.

In March 1996, DOJ announced that Circa Pharmaceuticals Inc., formerly known as Bolar Pharmaceuticals Inc., agreed to pay the Government $2.7 million to settle allegations that it sold untested generic drugs to Medicare, Medicaid, and the Department of Veterans Affairs. According to DOJ, Bolar substituted the brand name drug for the generic version when comparing the effectiveness of the drugs and then submitted the results to FDA to receive approval for the generic version. Bolar also kept a second set of records, known as "coversheets," to show FDA inspectors that the drugs were manufactured according to FDA's formula when in fact they were not.

In 1991, Bolar pleaded guilty to 21 generic drug manufacturing violations,paid $10 million in fines, and agreed to withdraw from the market virtually all of its generic drugs. In addition, several Bolar employees, including its president, have pleaded guilty to various criminal charges relating to the company's generic drug programs.

TAF on the *MOVE*

On May 1 (or shortly thereafter),
TAF will be moving to a new location,
a short walk from our current site south
of Dupont Circle.
TAF's new address will be:
1220 19th Street, NW, Suite 501
Washington, DC 20036.
Our phone and fax numbers will
not change.

TAF NEWS

Advisory Committee Sought

- TAF would like to form an advisory committee made up of *qui tam* attorneys and others to help plan regional seminars and/or a national conference. If you have an interest in joining this committee,please e-mail (ams@taf.org) or fax (202-296-4838) Associate Director Alan Shusterman.

Library Resources

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

Qui Tam Attorney Network

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

Quarterly Review Submissions

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

TAF On The Move

- In early May, TAF will be moving to a new location, a short walk from our current site south of Dupont Circle. TAF's new address will be: 1220 19th Street,NW, Suite 501, Washington, DC 20036. Our phone and fax numbers will not change.

Previous Publications Available

- Back issues of the *Quarterly Review*, including the "1995 Year In Review," are still available at no cost. Requests can be made by phone, fax, or mail.

Internet Site Expands

- TAF's Internet presence, designed to educate the public and legal community about the False Claims Act and *qui tam*, now features issues of the *Quarterly Review* as well as information on TAF's *Qui Tam* Attorney Network and Library Resources. The Internet presence, which includes an on-line version of the Act, will be updated regularly to highlight available resources and new developments in the field. TAF's site is located at http://www.taf.org/ or via e-mail at taf-info@taf.org.

Acknowledgments

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