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AN ANALYSIS OF THE WEB OF CIVIL AND CRIMINAL LIABILITY FOR DEFECTIVE PRICING OF GOVERNMENT CONTRACTS

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In the past year, the federal government has intensified its campaign to curb waste, fraud, and abuse in government contracting, especially in government defense contracting. Consider the following developments:

1. In the 1983 Defense Authorization Act, Congress mandated the creation of a new Inspector General (IG) post for the Department of Defense. Section 1117(b) of the Act empowers the IG to act as principal adviser to the Secretary of Defense on matters relating to the prevention and detection of fraud and abuse. This same section grants the IG the power to initiate, conduct, and supervise audits and investigations as the IG deems appropriate.

2. The Department of Justice, in conjunction with the Department of Defense, has established an investigative Procurement Fraud Unit to probe and prosecute fraud in the purchase of military equipment. The Unit is composed of attorneys from the Criminal and Civil Divisions of the Department of Justice, attorneys from the Defense Department, the

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3. Joseph H. Sherick has been chosen to fill the new Defense Department IG post. One of Sherick's first acts in his new position was to reform the Defense Department's waste and fraud "hotline." Gordon, The Pentagon Fraud and Waste Hotline Is Producing Results—Sometimes, 15 NAT. J. 1058 (1983).
United States Attorney's office in the Eastern District of Virginia, and investigators from both the Defense and Justice Departments. The Procurement Fraud Unit was designed to provide leadership and coordination with the audit and investigative resources already in place at the Department of Defense. Moreover, the Unit was created to provide a consistent pattern in federal prosecution of procurement fraud cases.

3. Senator Roth introduced a bill entitled the Program Fraud Civil Penalties Act of 1983 that would allow the Department of Defense, as well as other federal agencies, administratively to impose civil penalties against contractors who defraud the federal government. The bill would allow agencies to assess civil penalties for fraud without relying on the Justice Department. Under the bill, anyone who knowingly makes a false statement or claim to the government would face a civil penalty of $10,000 for each false claim, plus double the amount of money paid or value of property or services delivered as a result of the false statement or claim. Alternatively, agencies could recover double the amount of damages incurred, including the costs of investigating the claim, and consequential damages. The bill does, however, limit administrative fraud proceedings to claims not exceeding $100,000. Senator Roth and other supporters of the bill believe that the bill will be effective in combating smaller fraud cases that the Justice Department does not prosecute due to a lack of resources.

4. The government has reacted aggressively to the "horror stories" of the purchase by the military services of spare parts at grossly inflated prices. The issue of excessive pricing for spare parts was raised when a draft report from the Defense Department's Inspector General was made

5. R. Olsen, Deputy Assistant Attorney General, Criminal Division, Department of Justice, Remarks Before ABA, FBA, and D.C. Bar Ass'n (Feb. 10, 1983). The Procurement Fraud Unit is headed by Richard Sauber, an attorney from the Fraud section of the Criminal Division, and is located in Alexandria, Virginia. In his address, Olsen noted that the unit's geographical proximity to the Department of Defense will permit greater coordination of investigative manpower.

6. D. Jensen, Assistant Attorney General, Criminal Division, Department of Justice, Remarks Before ABA-Public Contract Law section (Feb. 4, 1983).

7. Id.


9. Id. § 802.

10. See supra note 8.

11. Id. § 806.

12. See supra note 8.

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public by the Project on Military Procurement, a nonprofit organization that gathers information on the cost of weapons. The report, which focuses on the review of the procurement of engine spare parts, reveals that Navy and Air Force contracting officers were not buying engine spare parts in a cost-effective manner because procedures designed to assure that the government pay fair and reasonable prices were not being implemented. These revelations of gross overpricing have been a source of embarrassment to government officials, and public and congressional outcry prompted Defense officials to institute new measures to combat waste and fraud in government contracting. For example, Defense Secretary Caspar W. Weinberger, in a memorandum to Defense officials, announced a ten-point strategy to eliminate excessive pricing in government contracts in the future. The plan relies on a two-pronged approach: internal Department of Defense efforts and dealings with government contractors. The first prong calls for increased competitive bidding and stern disciplinary action against Defense employees who are negligent in implementing Defense procedures. The second prong calls for, in part, the Defense Department to exercise legal rights and seek refunds from contractors guilty of excess pricing.

The foregoing examples clearly demonstrate the federal government’s commitment to eliminating waste, fraud, and abuse in government contracting. At the same time, these recent developments indicate that the government contractor occupies an extremely vulnerable position in the procurement process. A contractor that fails to deal with the government honestly may become entangled in a web of civil and criminal liability. It is the government contractor’s vulnerability that is the focus of this article.

More specifically, this article explores in detail the potential civil and criminal liability that may result when the government contractor certifies that cost or pricing data submitted in price negotiations with the government are accurate, complete, and current but later are discovered to be

15. Id. The report revealed that prices for the engine spares had escalated rapidly and were well in excess of inflation-related increases (some as much as 500%).
defective (i.e., inaccurate, incomplete, noncurrent). In particular, we focus on the government contractor's potential liability under the Truth in Negotiations Act, as well as under what is commonly referred to as the False Claims Act. At the same time, we explore the interrelationship between the Truth in Negotiations Act and the False Claims Act.

We have chosen defective pricing to illustrate the government contractor's vulnerability in the procurement process for three reasons. First, as the Department of Defense's response to overpricing of spare parts indicates, the government is intent on vigilantly monitoring the pricing of government procurements. Second, the pricing of government contracts is a complex, time-consuming process that involves gathering and processing information from many different departments within the contractor's organization. Given the financial and technical complexities involved, the potential for defective pricing is always present. Third, government contractors have failed to appreciate the seriousness and the full consequences of defective pricing. While many contractors are aware of their liability under the Truth in Negotiations Act, few contractors realize that defective pricing may lead to potential liability under the False Claims Act as well.

Thus, to aid in our analysis, we have divided our discussion into three

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18. In addition to the government contractor's obligation to certify the cost or pricing data, the government contractor throughout the contracting process is required to make numerous certifications as to compliance with various laws and regulations. For example, as part of the government contractor's proposal submission, the contractor may be required to certify that: (1) it has not paid or agreed to pay any company, other than a bona fide employee working solely for the offeror, a contingent fee upon the award of the contract; (2) it does not maintain segregated facilities; and/or (3) it does not utilize any facilities in the performance of the proposed contract that have been listed on the Environmental Protection Agency's list of violating facilities. See Armed Service Procurement Regulation F-100.33, Standard Form 33: Solicitation, Offer, and Award (1979, 1980, 1981); Armed Service Procurement Regulation F-100-33, Standard Form 33 (Exception): Solicitation, Offer, and Award (1979, 1981). Failure to make an accurate certification may expose the contractor to civil and criminal liability as well as lead to the contractor's debarment or suspension.


21. While we limit our analysis to these statutes, the government contractor's potential liability does not stop here. For example, to the extent that two or more persons conspire to submit false statements or claims, the contractor may be prosecuted under the Federal Conspiracy Statute, 18 U.S.C. § 371 (1982). Moreover, if the contractor used the mail or wires to defraud or obtain money or property from the government, the contractor may be prosecuted under the Mail Fraud Statute, 18 U.S.C. § 1341 (1982), and the Wire Fraud Statute, 18 U.S.C. § 1343 (1982). If the contractor has engaged in two acts of mail or wire fraud over the last ten years, it may be prosecuted under the Racketeer Influenced and Corrupt Organizations Act, 18 U.S.C. § 1961 (1982).
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parts. Part I sets forth the elements that constitute a prima facie violation of the Truth in Negotiations Act. Part II discusses the elements that constitute a prima facie violation of the False Claims Act. Part III then analyzes, in the context of a hypothetical example, the contractor’s liability for defective pricing under the Truth in Negotiations Act and the False Claims Act, and the interrelationship between these two Acts.

I. THE GOVERNMENT CONTRACTOR’S LIABILITY FOR DEFECTIVE PRICING UNDER THE TRUTH IN NEGOTIATIONS ACT

A. The Operation Of The Truth In Negotiations Act

The Truth in Negotiations Act requires a government contractor to submit cost or pricing data in negotiating procurements and to certify that such data are accurate, complete and current as of the date that the agreement is reached on the price. The Act applies to negotiated Defense Department and National Aeronautics and Space Administration (NASA) prime or subcontracts and modifications to those contracts in excess of $500,000. The Act exempts from its coverage negotiated contracts where the price is based on adequate price competition or established catalog or market prices of commercial items sold in substantial quantities to the general public.

The legislative intent of the Truth in Negotiations Act was to eliminate overpricing in the negotiation of noncompetitive defense contracts. Congress believed that overpricing resulted from the failure of contractors to disclose, during the pricing of defense contracts, complete, current, and accurate cost and pricing data:

In determining the price under many types of negotiated contracts the Government must rely, at least in part, on cost and


24. Although the Truth in Negotiations Act does not govern contracts with civilian agencies, these agencies have nonetheless adopted the Act’s procedures as reflected in Federal Procurement Regulations (FPR) § 3-807.3 to 3-807.5. Effective April 1, 1984, the Federal Acquisition Regulations (FAR) will become the primary regulations for federal procurement, replacing the Defense Acquisition Regulations, Federal Procurement Regulations and NASA Procurement Regulations. The objective of FAR is both to simplify and to unify the three sets of federal procurement regulations that currently govern defense, civilian and NASA procurements. The FAR provisions governing cost or pricing data are set forth in 48 Fed. Reg. 42,186-219 (1983) (to be codified at 48 C.F.R. § 1).
pricing data submitted by the contractor or his subcontractor. In recent years the General Accounting Office submitted several reports to the Congress on cases in which contractors received unwarranted profits because the data used in establishing target costs or prices were inaccurate, incomplete, or out of date. Although many of these reports were on incentive contracts, the objective of avoiding enhanced profits through failure to inform the contracting agency of the most current, accurate, and complete cost data is equally desirable in other types of negotiated contracts.25

To prevent overpricing, the Truth in Negotiations Act and its provisions, as set forth in the Defense Acquisition Regulations (DAR), require that a government contractor submit cost or pricing data with its proposal in a negotiated procurement exceeding $500,000.26 The contractor must submit data on DD Form 63327 and certify that the submitted cost or pricing data is “accurate, complete and current” as of the date the agreement is reached on price.28 The submission of inaccurate, incomplete, or noncurrent data will result in a defective pricing action whereby the government is entitled to a reduction in the contract price equal to the amount that the contract has been overpriced.29

To understand the government contractor’s obligation under the Act, it is necessary to identify the cost or pricing data that the government requires the contractor to submit. Cost or pricing data is defined as all “facts” existing up to the time of agreement on price that prudent buyers and sellers would reasonably expect to have a significant effect on price negotiations.30 Cost or pricing data embraces more than historical accounting data and must be the kind of factual data that is capable of being verified. Such data includes: (a) historical accounting data, (b) vendor

26. 32 C.F.R. § 1-3-807.3(2) (1983).
27. Id. Under this section the contractor is required to submit data on forms pursuant to § 1-16-806, or to specifically identify such data in writing if actual submission is not possible.
28. Id. 32 C.F.R. § 1-3-807.4 sets forth the certificate the contractor must execute when price negotiations are concluded and the contract price is agreed to.
29. 32 C.F.R. § 1-3-807.5(a) (1983) provides in pertinent part:
If... certified cost or pricing data is subsequently found to have been inaccurate, incomplete or noncurrent as of the effective date of the certificate, the Government is entitled to an adjustment of the negotiated price, including profit or fee, to exclude any significant sum by which the price was increased because of the defective data.

For a more detailed discussion of the government’s recovery in a case of defective pricing, see infra notes 53-59 and accompanying text.
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quotations, (c) nonrecurring costs, (d) changes in production methods, (e) changes in production or procurement volume, (f) data in support of projections, (g) unit cost trends, (h) make or buy decisions, and (i) significant management decisions. The Armed Services Board of Contract Appeals (ASBCA) has followed the DAR’s definition of the terms “cost or pricing data.” For example, in Aerojet General Corporation,\footnote{31} a contractor had prepared engineering studies and cost analyses tending to show that a subcontractor’s quotation was unreasonably high. The contractor was actually using these analyses in simultaneous negotiations with the subcontractor, but failed to submit them to the government negotiators. The ASBCA held that the analyses constituted cost or pricing data that should have been disclosed because they were the “type of facts which prudent buyers and sellers would reasonably expect to have a significant effect on the price negotiations and are data which could reasonably be expected to contribute to the sound estimates of future costs as well as to the validity of costs already incurred.”\footnote{32}

In defining cost or pricing data, the DAR draws a clear distinction between “judgments” of estimated future costs and “data” upon which such judgments are based. The judgments alone are not capable of being verified and are not cost or pricing data. The data on which the judgments are based, however, are verifiable and do constitute cost or pricing data.\footnote{33} The ASBCA also recognized the DAR’s distinction between “judgment” and “data.” For example, in E-Systems, Inc.,\footnote{34} appellant furnished a proposal for the manufacture of electronics modification kits to the Air Force. As part of the data included in the proposal, appellant listed a manufacturing overhead rate of 125% and information on past experienced overhead. The Defense Contracting Auditing Agency (DCAA) recommended acceptance. Negotiations were concluded on February 16, 1968, and appellant executed its certificate of cost and pricing data as of that date. A contract was awarded in the amount of $6,394,360 for 164 units.

Two and one-half years later, DCAA conducted a routine defective pricing audit and discovered that appellant had prepared a “profit plan” that had never been furnished to the government. The plan included information on projected sales, and indicated a projected overhead rate for manufacturing of 91.8%, substantially lower than the 125% rate previously

\footnote{31. ASBCA No. 12,264, 69-1 B.C.A. (CCH) ¶ 7664 (1969), modified, 70-1 B.C.A. (CCH) ¶ 8140 (1970).}
\footnote{32. Id. ¶ 7664, at 35,584.}
\footnote{33. 32 C.F.R. § 1-3-807.3(h)(1) (1983).}
\footnote{34. ASBCA No. 17,557, 74-2 B.C.A. (CCH) ¶ 10,782, reconsid. denied, 74-2 B.C.A. (CCH) ¶ 10,943 (1974).}
furnished. DCAA concluded that if this data had been available, the contract price would have been $761,284 lower. The appellant disagreed, and an appeal followed.

At the hearing, the evidence showed that the "profit plan" was a projection used for a variety of purposes, including motivation of sales and management personnel. In effect, the plan was a set of "targets" rather than a report of firm contract activity or actual backlog. Based on these findings, the ASBCA first found that the basic underlying data upon which the appellant's profit plan was based were known by government auditors and negotiators. The ASBCA then found that the profit plan included inaccuracies because it was not prepared in accordance with the appellant's normal accounting methods and was prepared primarily for training purposes. As such, the ASBCA concluded that the plan did not have to be disclosed. It also noted that even if the profit plan had been cost or pricing data, the government's defective pricing claim would be denied because the government had failed to establish that the failure to disclose the plan resulted in a higher contract price.

Moreover, the contractor's obligation to submit cost or pricing data is subject to a standard of reasonableness. The contractor's obligation extends only to data "reasonably available" at the time of the agreement on price. Data relating to any significant item is considered to be available if it is known anywhere in the contractor's organization. Contractors have successfully invoked the DAR's "reasonably available" criterion in defending against government claims of defective pricing. Thus, for example, in *LTV Electrosystems, Inc.*, the government asserted a defective pricing claim against the contractor because the latter had failed to update a bill of materials. The ASBCA rejected the claim, reasoning that although the contractor had more current data in its organization, this was a rush procurement, and the contractor simply did not have the time or staff to update the bill of materials. In this situation, the ASBCA held, the data were not "reasonably available."

35. *Id.* ¶ 10,782, at 51,263.
36. *Id.*
37. 32 C.F.R. § 1-3-807.3(h)(2) (1983).
38. See 32 C.F.R. § 1-3-807.5(a)(1) (1983) which discusses in greater detail when cost or pricing data may be said to be reasonably available to the contractor.
40. In American Bosch Arma Corp., ASBCA No. 10,305, 65-2 B.C.A. (CCH) ¶ 5280 (1965), the Board also recognized that some data, although existing in the contractor's organization prior to certification, may not be "reasonably available" if it cannot be processed in time.
Finally, assuming data are "reasonably available," the contractor does not fulfill its obligations to submit cost or pricing data by merely making available to the government the company's books and records without specific identification of the cost or pricing data. The DAR makes clear that the contractor must actually submit cost or pricing data on DD Form 633, or in the attachments thereto, as part of the formal proposal submission. A contractor, however, may identify specific data in his proposal where they are too voluminous to be attached physically.

B. The Prima Facie Case

As the discussion below indicates, to make out a prima facie case of defective pricing, the following elements must be established: (1) the existence of an executed "Certificate of Cost or Pricing Data" in the government's possession; (2) the government's reliance on the noncurrent, inaccurate, or incomplete data in its negotiations with the contractor; and (3) the government's reliance on the noncurrent, inaccurate, or incomplete data caused an increase in the contract price.

To establish a violation of the Truth in Negotiations Act, the government must first show that the contractor executed a "Certificate of Cost or Pricing Data." This certificate is the contractor's statement that the cost or pricing data submitted is accurate, complete, and current as of the date the agreement is reached on price. Without this certificate, a contractor cannot be held liable for failing to disclose cost or pricing data in his possession. Thus, in Libby Welding Co., Inc., the contract contained the required clause permitting a reduction in price in the event of defective pricing. However, the contractor was not asked to and did not provide a "Certificate of Current Cost or Pricing Data" for a contract modification in excess of $100,000. The government later asserted a defective pricing claim, but the ASBCA held that the claim was precluded by the absence of a certificate. The Board noted that the price reduction clause was tied directly to the certificate. In its absence, a contractor is not liable under the price reduction clause of the contract.

To prevail in a defective pricing action under the Truth in Negotiations Act, the government must also show that it relied on the defective cost or

41. 32 C.F.R. § 1-3-807.3(h)(2) (1983).
42. Id. § 1-16-806 (1983).
43. See 32 C.F.R. § 1-3-807.3(h)(2) (1983).
44. Libby Welding Co., ASBCA No. 15,084, 73-1 B.C.A. (CCH) ¶ 9859 (1972).
45. Id.
The applicable regulation, DAR section 3-807.10(a)(2), establishes a rebuttable presumption that the government relied on the defective data. This section provides that:

In the absence of evidence to the contrary, the natural and probable consequence of defective data is an increase in the contract price in the amount of the defect plus related burden and profit or fee; therefore, unless there is a clear indication that the defective data were not used, or were not relied upon, the contract price should be reduced in that amount. In establishing that the defective data caused an increase in the contract price, the contracting officer is not expected to reconstruct the negotiation by speculating as to what would have been the mental attitudes of the negotiating parties if the correct data had been submitted at the time of agreement on price.48

DAR section 3-807.10(a)(2) has been interpreted as shifting the burden of going forward with the evidence to the contractor.49 The contractor, however, may shift the burden back to the government by introducing evidence of nonreliance. Once the contractor does this, the government then has the ultimate burden of proving that it relied on the defective data.50

Finally, the government must show that the submission of defective cost or pricing data resulted in a higher contract price to the government. DAR section 3-807.10(a)(2), set forth in the preceding paragraph, presumes that the "natural and probable" consequence of defective data is an increase in contract price. Because this regulation provides a rebuttable presumption, it shifts the burden of going forward with evidence to the contractor. Once the contractor introduces his evidence, the government then has the burden of proving that defective data actually increased the contract price. This was made clear in Lear Siegler, Inc.51 There, the contractor purported to base his proposal on historical average labor hours. The government, however, claimed that data for the most recent six months had not been disclosed and, if disclosed, would have shown reduced labor costs. The ASBCA rejected the government's claim because the government did not show that the failure to disclose this data in question caused an increase in the contract price:

48. 32 C.F.R. § 1-3-807.10(a)(2) (1980).
49. Id.
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Accordingly, even were we to conclude that the government made a prima facie showing of the nondisclosure of significant cost data and we presumed, therefore, that there was a price overstatement, we would conclude that appellant rebutted that showing, at least by making the extent of that overstatement so speculative that not even a 'jury verdict' would be appropriate. The government has not shown that the failure to disclose current cost data caused an overstated price in any reasonably ascertainable amount.\(^{52}\)

C. The Government's Recovery in a Case of Defective Pricing

In the case of defective pricing under the Truth in Negotiations Act, the government is entitled to a price reduction equal to the amount of the contractor's cost overstatement plus the appropriate burden, profit, or fee.\(^{53}\) The rule is clearly illustrated in *Sylvania Electric Products, Inc.*\(^{54}\) In that case, the ASBCA found that the contractor failed to disclose certain low quotations for six items of electronic equipment before executing a Certificate of Cost and Pricing Data. To arrive at the price reduction, the ASBCA reduced the price of six items of equipment by an amount equal to the difference between the contractor's proposal price and the low quotation and then added the appropriate overhead and profit. The cost overstatements for all six items of equipment totalled $202,808 and, with the negotiated 6% for overhead and 11.6% for profit, the total price reduction equalled $239,913.75.

The natural and probable consequence of defective data is to increase the contract price in the amount of the cost overstatement plus related overhead, profit, or fee. Nevertheless, the contractor may overcome this presumption by demonstrating that, even if it had disclosed the correct data, the parties would not have negotiated a price that would have reflected the total amount of the overstatement. The contractor meets its burden of going forward with evidence by reconstructing the course of its previous price negotiations with the government.

Thus, in *Bell & Howell Co.*\(^{55}\) the government negotiated a contract with

\(^{52}\) *Id.* at 64,070 (emphasis added); *but see* Universal Restoration, Inc., ASBCA No. 22833, 83-1 B.C.A. (CCH) ¶ 16,265 (1983), where the ASBCA reversing its earlier decision implied that the presumption of 32 C.F.R. § 1-3-807.10(a)(2) (that defective data increased the contract price) will only be overcome if the contractor can produce evidence clearly indicating that the government was aware of defective data but elected to ignore it and award a price higher than the data indicated.

\(^{53}\) 32 C.F.R. § 1-3-807.10(a)(2) (1983).


\(^{55}\) ASBCA No. 11,999, 68-1 B.C.A. (CCH) ¶ 6993 (1968).
the contractor for M65 fuzes. The ASBCA found that during negotiations the contractor failed to disclose several low quotations from various suppliers. This failure to disclose resulted in an overstatement of $389,281 or $0.76 per fuze. The ASBCA refused to grant the government a price reduction for the full amount of $389,281 because it was not convinced that disclosure of the low quotations would have enabled the government to negotiate a further price reduction of $0.76 per fuze. The contractor established that its management would not have agreed to a significantly lower figure. The final price was lower than the contractor's negotiation team was authorized to go and the price had to be cleared with top management. Furthermore, the ASBCA found that the contractor would have exposed itself to considerable risk if it had based the firm price on the low quotations. The vendors recently were not producing the parts and were offering prices substantially lower than those at which the parts had previously been procured. Accordingly, the ASBCA held that the effect of failing to disclose the low quotations was a $233,569 increase in the ultimate price paid by the government.56

The contractor may further reduce its liability for defective pricing by offsetting understatements of cost against overstatements of liability. In other words, it can reduce its liability by the amount that other defective data decreased the contract price.57 Set-offs are permitted only up to the amount of the government's claim in a single pricing action.58 Moreover, the set-offs need not be part of the same cost category that forms the basis for the government's price reduction.59

56. To the same effect, see McDonnel-Douglas Corp., ASBCA No. 12,786, 69-2 B.C.A. (CCH) ¶ 7897 (1969) (contractor is not liable for overstated costs reflected in its proposal that have been eliminated through negotiation of the contract price); but see American Bosch Arma Corp., ASBCA No. 10,305, 65-2 B.C.A. (CCH) ¶ 5280 (1965), corrected decision, 66-2 B.C.A. (CCH) ¶ 5747 (1966), vacated, 67-2 B.C.A. (CCH) ¶ 6564 (1967) (contract reduced by the amount of overstatement where contractor fails to produce specific evidence showing that parties would nonetheless have negotiated a contract price reflecting the overstatement).


II. THE FALSE CLAIMS ACT PROHIBITS THE INTENTIONAL SUBMISSION OF FALSE, FICTITIOUS, OR FRAUDULENT STATEMENTS OR CLAIMS TO THE GOVERNMENT

The original False Claims Act was passed in 1863 as a result of investigations of the fraudulent use of government funds during the Civil War.60 The debates at that time suggest that the Act was intended to reach all types of fraud, without qualification, that might result in financial loss to the government.61 The original Act provided both civil and criminal sanctions in combating the fraudulent activities of those who deal with government agencies. The civil provisions of the original Act recently have been recodified in 31 U.S.C.A. § 3729.62 The House Report makes clear that the recodification made no substantive change in the Act and that its sole purpose was to substitute simple language for awkward and obsolete terms.63

It is important to recognize that the civil and criminal sanctions of the False Claims Act extend to the corporate entity as well as to corporate employees.64 Corporate liability is determined by focusing on the activities of corporate employees. Corporate liability will be imposed if the corporation's employees, while engaged in the unlawful conduct, were acting within the scope of their authority and for the purpose of benefiting the corporation.65

A. The Civil False Claims Statute Imposes Civil Liability for the Knowing Submission of a False Claim to a Government Agency

1. The Prima Facie Case

The Civil False Claims Statute (31 U.S.C.A. § 3729) imposes civil liability on any person not in the United States military or naval forces presenting a false, fictitious, or fraudulent claim to the government.66

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61. See CONG. GLOBE, 37th Cong., 2d Sess. 952-58 (1862).
64. See, e.g., United States v. Hangar One, Inc., 563 F.2d 1155 (5th Cir. 1977); United States v. Lange, 528 F.2d 1280 (5th Cir. 1976); United States v. Empire Packing Co., 174 F.2d 16 (7th Cir.), cert. denied, 337 U.S. 959 (1949).
66. The discussion that follows is based on judicial precedent interpreting provisions of the original act, which were previously codified at 31 U.S.C. § 231 (1976). Inasmuch as the
A person not a member of an armed force of the United States is liable to the United States Government for a civil penalty of $2,000, an amount equal to 2 times the amount of damages the Government sustains because of the act of that person, and the costs of the civil action, if the person—

1. knowingly presents, or causes to be presented to an office or employee of the Government or a member of an armed force a false or fraudulent claim for payment or approval . . . . 67

Thus, as the discussion below indicates, to establish a prima facie violation of section 3729, the government must prove by clear, explicit, and unequivocal evidence68 that: (1) there was a presentation of a claim to a government agency; (2) the claim was false; and (3) the party submitted the claim either knowing it to be false or with the intent to defraud. Significantly, because the courts have construed section 3729 to permit recovery of the $2,000 forfeiture without proving actual damages,69 a violation of section 3729 often occurs upon the mere submission of a false claim. Therefore, the government's reliance on the claim is not essential.

For purposes of determining liability under section 3729, it is essential that a “claim” was made or presented to a government agency or department. In United States v. Neifert-White Co.,70 the Supreme Court refused to accept a rigid and restrictive reading of the term “claim.” In that case, the Commodity Credit Corporation (CCC) was authorized to make loans to grain growers to finance the construction or purchase of storage facilities. The loans were not to exceed 80% of the purchase price of the storage bins. The CCC required grain growers to support loan applications with invoices showing the price of the bin. The defendant, a dealer in storage bins, prepared invoices for growers in which the purchase price was deliberately overstated. The invoices were then submitted to the CCC along with the loan application. Based on this evidence, the government brought suit contending that false claims were made in violation of section 231. The defendant argued that an application for a CCC loan, as distinguished from a claim for payment of an obligation owed by the government, is not a “claim” within the meaning of the statute. The Court rejected the de-

68. United States v. Mead, 426 F.2d 118, 123 (9th Cir. 1970).
70. 390 U.S. 228 (1968).
fendant's assertion and held that a "claim" encompassed all attempts to cause the government to pay out sums of money:

Analogous reasoning leads us to hold today that the False Claims Act should not be given the narrow reading that [defendant] urges. This remedial statute reaches beyond "claims" which might be legally enforced, to all fraudulent attempts to cause the Government to pay out sums of money. We believe the term "claim," as used in the statute, is broad enough to reach the conduct alleged by the Government in its complaint. 71

Judicial opinion conflicts as to the type of "intent" required to constitute a violation of section 3729. Some courts have held that in order to be liable under section 3729 for the submission of a false claim, a specific intent to defraud the government must be found. 72 Other courts, however, have held that a specific intent to defraud need not be proven and that the knowing submission of a false claim is sufficient to sustain liability. 73 Confusion surrounds the application of these two standards. For example, some courts, while appearing to endorse strongly one of the two standards, have referred to both standards as if they were one. 74

In United States v. Mead, 75 the United States Court of Appeals for the Ninth Circuit held that an intent to defraud must be found to sustain liability under the statute. 76 In Mead, the government brought suit against the defendant, a contractor-farmer, to recover alleged overpayments made to the defendant under the Agriculture Conservation Program. Under this program, the government reimbursed participating farmers for a percentage of the construction cost of conservation ditches. Payments were to be made directly to the contractor who performed the work. To obtain payment, the contractor was required to submit invoices and execute forms indicating the cost of the construction of the ditches. The defendant, an inexperienced businessman, construed the program's relatively new regulations and forms as permitting him to submit to the government claims

71. Id. at 233 (emphasis added).
74. See United States v. Mead, 426 F.2d at 123; Fleming v. United States, 336 F.2d at 479.
75. Mead, 426 F.2d at 118.
76. Id. at 122.
for payment which represented the market value of the work. Thus, when the defendant submitted his claims to the government for payment with invoices attached showing prices higher than the cash price actually charged to the farmer, the government brought suit. The defendant contended that the invoices were not false, and, even if they were, the government had not shown an intent to defraud.

The Ninth Circuit rejected the government's contention that the statute was violated. The court noted that while the invoices were false, the government failed to prove an intent to defraud.\footnote{77} The court stated that the Civil False Claims Statute was not intended to catch the hapless and inexperienced. Moreover, it noted that while only two of the six types of conduct proscribed by the statute explicitly required an intent to defraud, there was no reason to assume that Congress eliminated this intent requirement for the other types of conduct proscribed by the statute.\footnote{78}

Contrary to \textit{Mead}, the United States Court of Appeals for the Tenth Circuit held, in \textit{Fleming v. United States},\footnote{79} that a specific intent to defraud need not be proven and that the knowing submission of a false claim is sufficient to sustain liability under the Civil False Claims Statute.\footnote{80} In \textit{Fleming}, the defendant was a certified grain dealer under the Emergency Feed Program. Under this program, farmers made application for emergency feed to their county committee. If a farmer was determined to be eligible for assistance, the county issued a purchase order for a specified amount of grain, which the farmer then transferred to a certified dealer as payment for the grain. The dealer in turn presented the purchase order to the county in exchange for a Dealers Certificate at a face value equal to the value of the purchase order. Before the dealer presented a purchase order to the county, he was required to certify that he had sold and actually delivered to the farmer the specified surplus grain.

The evidence in \textit{Fleming} revealed that the defendant received Dealer Certificates and later negotiated them without ever having delivered grain to farmers. The defendant's sole defense to the government's suit was that

\footnote{77} Id. at 124. The court used the terms "intent to deceive" and "intent to defraud" interchangeably. However, as will be discussed in the fraud and false statements analysis of 18 U.S.C. § 1001, courts that have construed this statute have distinguished between an "intent to deceive" and an "intent to defraud." See \textit{infra} notes 130-33 and accompanying text.

\footnote{78} \textit{Mead}, 426 F.2d at 122-24. The two types of conduct the court referred to are: (1) conspiring to \textit{defraud} the United States by obtaining the payment of a false or fraudulent claim; and (2) delivering with \textit{intent to defraud} a receipt for property without a full knowledge of the truth of the facts stated therein. This conduct is now set forth in 31 U.S.C.A. § 3729(3) and (4) respectively. 426 F.2d at 123.

\footnote{79} 336 F.2d at 475.

\footnote{80} \textit{Id.}
the government had failed to prove that the defendant had intentionally defrauded the United States.\textsuperscript{81} The Tenth Circuit rejected the defendant's contention. The court held that because the statute states the terms "false, fictitious, or fraudulent" in the disjunctive, in order to prove a violation of the statute the government need only establish that a party knowingly submitted a "false" claim.\textsuperscript{82}

2. Government Recovery Under the Civil False Claims Statute

Under section 3729, the government may recover (1) double its actual damages, (2) a $2,000 forfeiture for each false claim, and (3) costs of the suit.\textsuperscript{83} The Supreme Court has held that damages under section 3729 are intended to "afford the Government complete indemnity for the injuries done it."\textsuperscript{84} The Court has ruled that "the chief purpose of the statutes here was to provide for restitution to the government of money taken from it by fraud, and that the device of double damages plus a specific sum was chosen to make sure that the government would be made completely whole."\textsuperscript{85}

The basic rule of law for computing damages under section 3729 is the difference between the amount the government actually paid in reliance on the false claims and the amount it would have paid had the contractor been truthful.\textsuperscript{86} Under section 3729, the government has the burden to prove what it would have paid absent the fraud.\textsuperscript{87} Unlike the Truth in Negotiations Act,\textsuperscript{88} where the regulations create a rebuttable presumption that the government is entitled to a price reduction equal to the amount of the cost overstatement plus appropriate overhead and profit, no such presumption aids the government in meeting its burden of proof under section 3729. Moreover, the government may not use speculation or guesswork to establish the amount of damages. It must prove its losses with sufficient specificity to allow a reasonable estimate of the damages. The govern-

\textsuperscript{81.} Id. at 478.
\textsuperscript{82.} Id. at 480. When 31 U.S.C. § 231 was recodified in 31 U.S.C.A. § 3729 the term "fictitious" was eliminated. The statute now addresses "false" or "fraudulent" claims. 31 U.S.C.A. § 3729 (1982).
\textsuperscript{88.} See supra note 23 and accompanying text.
ment's failure to meet its burden of proof under section 3729 may relieve the contractor from paying anything more than nominal damages, and may even relieve it from paying any damages at all. The government fulfills its burden of proof only if it shows that the claimed damages are, in the language of the statute, "because of" the doing of the fraudulent act. It must establish a direct causal connection between its losses and the defendant's fraudulent conduct. Consequential damages are not recoverable under the statute because they are not directly caused by the submission of false claims.

In cases involving misrepresentation of cost estimates, damages are based upon the amount that the contractor actually overcharged the government as a result of the misrepresentation. In these cases, as in cases under the Truth in Negotiations Act, amounts eliminated in price negotiations are deducted from the total amount of the overstatement. For example, in United States v. Foster Wheeler Corp., the contractor entered into a contract with the Navy to sell replacement boilers and related spare parts for Navy vessels. In preparing its price proposal, the contractor estimated its costs to be $1,242,380. If the contractor had added its usual mark-up of 25.32%, its proposal price would have been $1,556,919. However, the contractor instead used a mark-up of 40%, which resulted in a proposal price of $1,739,336. To conceal this unusually high mark-up, the contractor included a 25.32% mark-up in its cost and price analysis on the government DD Form 633, and increased its estimate costs to $1,427,042 by inflating various items. In short, the contractor predetermined a price that would assure it a very high profit and then created false cost figures to substantiate that price.

In Foster Wheeler, the court calculated the government's damages by first applying the disclosed 25.32% mark-up to the contractor's true cost estimate of $1,242,380. It then subtracted that amount ($1,556,919) from the amount actually proposed ($1,739,376). It further reduced the remainder ($182,417) by amounts eliminated during price negotiations and found

89. See United States v. Collyer Insulated Wire Co., 94 F. Supp. 493 (D. R.I. 1950) (court assessed double nominal damages plus allowed the government to recover the $2,000 forfeiture on each of the 105 false claims the contractor submitted); see also Little v. United States, 152 F. Supp. 84 (Ct. Cl. 1957).
93. The rule is the same for misrepresentation of actual costs. See Ueber, 299 F.2d at 310.
that the government had been overcharged by $132,209. The court awarded the government twice the $132,209 overcharge actually sustained as a result of the fraud.95

In addition to damages, section 3729 entitles the government to a $2,000 forfeiture for each false claim submitted. Since these damages are primarily punitive in nature, liability is enforced whether or not the contractor is liable for actual damages. Thus, in United States v. American Precision Products Corp.,96 the contractor submitted six invoices containing false statements. The government paid only four of the six. The court, however, held the contractor liable for $2,000 on each of the six invoices because "forfeitures go regardless of damages."97

In determining the number of forfeitures the government may recover, the Supreme Court has stated that the "number of imposable forfeitures has generally been set at the number of individual false payment demands that the contractor has made upon the government."98 In Brown v. United States,99 the court assessed a $2,000 penalty for each of the fourteen purchase orders submitted for payment under the contractor's various bid rigging schemes.100 The government, however, cannot recover more than one forfeiture for a single false claim no matter how many times the claim is submitted.101

The United States Supreme Court has held that a contractor can only be assessed forfeitures for those false payment demands over which it had knowledge and control.102 In Bornstein, a subcontractor, "United," contracted to supply electron tubes to a prime contractor, "Model," under Model's contract with the government. United knowingly sent three separately invoiced shipments of defective tubes. Model, unaware of the de-

95. Id. at 973; see also United States v. Sych, 257 F.2d 475 (3d Cir. 1958).
97. Id. at 827-28; see also United States v. Ridglea State Bank, 357 F.2d 495 (5th Cir. 1966); Toepkeleman v. United States, 265 F.2d 697 (4th Cir.), cert. denied sub nom. Cato Bros., Inc. v. United States, 359 U.S. 989 (1959) (proof of actual damages is not a prerequisite to the recovery of forfeitures because the investigation necessary to detect a false claim costs the government money even if no money is paid on the claim).
98. Bornstein, 423 U.S. at 309 n.4; see also, Fleming, 336 F.2d at 480.
99. 524 F.2d 693 (Cl. Ct. 1975).
100. Id. at 705-06.
101. Acme Process Equip. Co. v. United States, 347 F.2d 509, rev'd on other grounds, 385 U.S. 138 (1965), reh'g denied. 385 U.S. 1032 (1967). The court in Acme noted that where a contractor submits one false claim that is denied by the government and thereafter resubmits the same claim, the government is only entitled to one $2,000 forfeiture. The court noted that such a situation is different from one where a contractor submits to the government numerous vouchers each containing a separate and distinct false claim. In this situation, the government is entitled to multiple forfeitures. 347 F.2d at 527.
fects, incorporated the tubes into the radio kits and shipped them to the government. Model sent thirty-five invoices to the government, requesting payment for the defective tubes. The United States District Court for the District of New Jersey held that there had been thirty-five forfeitures. According to the court, United's fraudulent acts "caused Model to submit thirty-five false claims, each of which constituted a separate violation justifying a separate forfeiture."  

The United States Court of Appeals for the Third Circuit reversed and held that there was only one forfeiture. The court focused upon United's conduct rather than upon "the fortuity of the number of invoices submitted by the main contractor." There was a single forfeiture because United's fraud affected the performance of a single purchase order from Model to United. The United States Supreme Court reversed the Third Circuit's decision and held that there were three forfeitures. The Court found that United's acts had nothing to do with the fact that Model submitted thirty-five false claims. The number of false claims submitted by Model was completely fortuitous as far as United was concerned. United could not be held liable for thirty-five forfeitures when the number of false claims was beyond United's knowledge and control.

The Court clearly distinguished the acts committed by Model from those committed by United. It emphasized that the False Claims Act "penalizes a person for his own acts, not for the acts of someone else." Thus, the proper test for determining the number of forfeitures focuses on an evaluation of the conduct of the person liable for the statutory forfeitures. In reversing the Third Circuit's decision, the Court also ruled that the number of forfeitures under the Act is not measured by the number of contracts involved in a case. It stated that the language of the statute focuses on false claims, not on contracts. To focus on the number of contracts would result only in a single forfeiture in most cases, which would be contrary to the language and purpose of the Act.

The United States Court of Appeals for the Ninth Circuit recently applied the "knowledge and control" test in United States v. Ehrlich. In that case, the defendant general contractor for a low-income housing pro-

105. 423 U.S. at 313. The court held that there were three forfeitures because United sent three separately invoiced shipments to model.
106. 423 U.S. at 312.
107. Id.
108. Id. at 313.
109. Id. at 311.
ject entered into an agreement with the Department of Housing and Urban Development (HUD) under which HUD insured the mortgage for the project and subsidized a portion of the interest payments. HUD paid the interest subsidies directly to the mortgagee, who submitted monthly vouchers to HUD. The agreement provided that the contractor would estimate costs at the beginning of the project. At the end, if the actual costs were less than estimated, the contractor was required to repay a portion of the principal to the mortgagee. One year after the contractor entered the agreement, it prepared and submitted (1) a Mortgagor’s Certificate of Actual Cost, and (2) a Contractor’s Certificate of Actual Cost. Both certificates overstated actual construction costs to relieve the contractor from repaying a portion of the principal.

The *Ehrlich* court held that the mortgagee’s monthly vouchers were false claims under the Act. The concept of a claim includes a demand for money. The court ruled that due to Ehrlich’s false certifications, the interest subsidies demanded and paid each month were falsely inflated individual claims. Accordingly, the contractor was liable for seventy-six forfeitures on the basis of seventy-six monthly vouchers. The court rejected the contractor’s argument that he should be liable for only one forfeiture because he did only one act—that of inflating the actual construction costs—that caused false claims to be filed. The court applied the *Bornstein* ruling and held that the number of forfeitures equals the number of false claims that the contractor knowingly causes to be filed. In this case, the contractor knew that a false claim would be filed each month and did nothing to prevent the filing of additional false claims. It was the contractor’s knowledge and control of the situation that rendered him liable for seventy-six forfeitures.

B. The Criminal False Claims Statute Imposes Criminal Liability for the Knowing Submission of a False Claim to a Government Agency—The Prima Facie Case

The Criminal False Claims Statute (18 U.S.C. § 287), imposes criminal liability on any person who presents a false, fictitious, or fraudulent claim to the government:

> Whoever makes or presents to any person or officer in the civil, military, or naval service of the United States, or to any department or agency thereof, any claim upon or against the United States, or any department or agency thereof, knowing such claim

111. *Id.* at 637.
to be false, fictitious, or fraudulent, shall be fined not more than
$10,000 or imprisoned not more than five years, or both.

Thus, to establish a prima facie violation of section 287, the government
must prove beyond a reasonable doubt that: (1) there was the presentation
of a claim to a government agency; (2) the claim was false; and (3) the
party submitted the claim knowing it to be false, and with "criminal in-
tent," i.e., with consciousness that he was doing something wrong or that
he acted with a specific intent to commit an act that violated the law.

In the prosecution of a criminal false claim, the first issue is whether a
"claim" was made to a government agency. It appears that the broad defi-
nition of claim as set forth in Neifert-White,112 will apply to section 287
suits as well,113 inasmuch as 18 U.S.C. § 287 and 31 U.S.C. § 3729 are
part of the same statutory scheme, under the False Claims Act. Thus, any
fraudulent attempt to cause the government to part with its money will
constitute a claim.

The intent element of section 287 is satisfied if the government can
prove beyond a reasonable doubt that the defendant acted (1) with knowl-
dge that a claim was false or fictitious or fraudulent, and (2) with con-
sciousness that he was doing something that was either morally wrong or
had violated the law. In United States v. Maher,"114 the defendant was
charged with submitting false vouchers to a government agency. The de-
fendant's corporation had entered into various contracts with the Depart-
ment of the Army. The corporation's monthly billings to the Army were
based upon time sheets filled out and signed by the corporation's employ-
ees working on the Army contracts. The defendant had instructed the cor-
poration's bookkeeper to inflate the billings to the Army by increasing the
hours reflected on the employees' time sheets. The defendant contended
that he lacked any intent to defraud the government, and therefore, could
not be prosecuted under section 287.

The court disagreed with the defendant's interpretation of the intent ele-
ment of section 287 and held that section 287 does not require the govern-
ment to show an intent to defraud. Section 287 only requires that the
defendant submit a claim knowing it to be false and with consciousness
that he was doing something wrong or that he acted with a specific intent
to do something the law forbids. The court cited three reasons in support
of its conclusion that section 287 does not require an intent to defraud:

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112. 390 U.S. 228; see supra notes 70-71 and accompanying text.
113. See United States v. Winchester, 407 F. Supp. 261, 272 (D. Del. 1975) (cases con-
struing the civil branch of the False Claims Act are relevant to the interpretation of the
criminal branches of the Act).
First, we do not find that the statute specifies an intent to defraud as an element to be proved under § 287. The language of the statute states the terms, 'false, fictitious or fraudulent,' in the disjunctive, and we interpret this to mean that three kinds of claims may be submitted in violation of § 287 and not merely claims which are fraudulent . . . .

Second, in applying general principles of criminal law, the trial court added the element of "willfulness" or criminal intent to the requirements of the government's case, and we think correctly refused to define criminal intent under § 287 solely in terms of purpose or motive. Criminal intent may be proved either by a showing that the defendant acted for a specific purpose to violate the law or that he acted with an awareness that what he was doing was morally wrong, whether or not he had actual knowledge that he was doing something that the law forbids . . . .

Third, we think that § 287 does not require proof of a specific intent to defraud, as defendant defines that term, because the purpose of § 287 will not be furthered by limiting criminal prosecutions to instances where the defendant is motivated solely by an intent to cheat the government or to gain an unjust benefit . . . .

C. The Criminal False Statements Statute Imposes Criminal Liability for the Knowing and Willful Submission of a Material False Statement To a Government Agency—The Prima Facie Case

The Criminal False Statements Statute (18 U.S.C. § 1001) punishes false, material statements made knowingly and willfully concerning a matter within the jurisdiction of any department or agency of the United States:

Whoever, in any matter within the jurisdiction of any department or agency of the United States knowingly and willfully falsifies, conceals or covers up by any trick, scheme, or device a material fact, or makes any false, fictitious or fraudulent statements or representations, or makes or uses any false writing or document knowing the same to contain any false, fictitious or fraudulent statement or entry, shall be fined not more than $10,000 or imprisoned not more than five years, or both.116

115. Id. at 847-48 (emphasis added); United States v. Milton, 602 F.2d 231 (9th Cir. 1979).
116. There are two parts to § 1001. The first clause imposes liability for the knowing falsification, concealment or covering up by trick, scheme, or device of a material fact. We limit our analysis to the second, more commonly applied "false statement" clause, although
Thus, the courts have recognized that the five elements necessary to sustain a conviction under section 1001 are: (1) the submission of a statement; (2) the statement was submitted with the intention that it bear a relation to some matter within the jurisdiction of a department of the United States; (3) the statement was material; (4) the statement was false; and (5) the party submitted the statement knowing it to be false.

To sustain a conviction under section 1001, there first must be a "statement." It would appear that any writing can constitute a "statement." For example, the government successfully prosecuted an individual under section 1001 who had submitted false time sheets to a United States marshal.\(^{117}\) A contractor's submission of a false statement of costs to a government agency also satisfied the "statement" requirement of section 1001.\(^{118}\) Moreover, the term "statement" also has been construed to include statements not made in writing.\(^{119}\)

To sustain a conviction under section 1001, it must be established that a statement relating to some matter within the jurisdiction of a department or agency of the United States was made. Significantly, it is not necessary that the defendant actually present the false statement to the department or agency. This point is well illustrated in *Ebeling v. United States*.\(^{120}\) Appellant Emerling, a prime contractor, entered into a contract with the Army for the production of mortar conversion kits. The contract contained a statutorily required price redetermination clause, which mandated that the contractor file a statement of costs. In an attempt to hide his profits and, thus, avoid the effect of the price redetermination clause, Emerling entered into a subcontract with appellant Ebeling. Under this subcontract, Ebeling sent phony invoices to Emerling for work never performed. Emerling purported to pay these invoices and noted these payments in his statement of costs submitted to the Army. In their defense, appellants contended that because they had not actually presented the false invoices to the Army, they had not submitted a false statement that could be regarded as relating to a matter within the jurisdiction of a department or agency of the United States. The court rejected this argument, holding that Emerling's inflated statement of costs reflected the false invoices and thus,

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as will become apparent in Part II, arguably either clause could apply to a case of defective pricing. *See infra* notes 148-49 and accompanying text.

117. United States v. Godwin, 566 F.2d 975 (5th Cir. 1978).
120. 248 F.2d at 429.
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affected the Army's monitoring of contract costs, a matter clearly within its jurisdiction.

As part of the government's case in a section 1001 prosecution, it must prove that a "material" false statement was submitted to a government agency. While the requirement of "materiality" explicitly applies only to the "trick, scheme, or device" clause of section 1001, courts have inferred a judge-made limitation of "materiality" on the "false statement" clause of section 1001 as well. The purpose of the "materiality" requirement is to exclude trivial falsehoods from the purview of the statute. Thus, the courts have adopted a test to determine whether a statement is "material." The test is whether the statement "has a natural tendency for influence, or was capable of influencing the decision of the tribunal in making a determination required to be made." Application of this test was neatly demonstrated in United States v. Lichenstein, where, the defendants were convicted of falsely designating as "vessel supplies" 1,150 cases of bonded scotch whiskey on a United States Customs form. They challenged on appeal the trial court's finding that their falsification was a material false statement under section 1001. In denning the appeal, the United States Court of Appeals for the Fifth Circuit found that the effect of the defendants' falsification precluded the Customs Bureau from furnishing to the Bureau of Census information needed to compile import-export statistics: "Pervasive falsifications of this nature obviously would totally pervert these statistics and undermine the efforts of the Customs and Census officials assigned to collect the data."

Significantly, the "materiality" requirement of section 1001 can be satisfied even if the false statement did not cause the government any pecuniary loss. Moreover, the "materiality" requirement is satisfied even if the government fails to establish that it relied on the false statement. In United

125. 610 F.2d 1272 (5th Cir.), cert. denied, 447 U.S. 907 (1980).
126. Id. at 1279; see Baker, 626 F.2d at 515.
States v. Coastal Contracting and Engineering Co., a contractor knowingly submitted fictitious statements in connection with a change order proposal. These statements were not relied upon by the government negotiator because he thought the prices were entirely out of line. Nevertheless, the court found that the contractor had violated section 1001.

Finally, intent under section 1001 is shown if the submission of the false statement was done knowingly, willfully, and with the intent to deceive. Intent to defraud is not a prerequisite to liability under section 1001. The distinction between “intent to deceive” and “intent to defraud” was addressed in United States v. Godwin. In Godwin, the defendant was convicted by the trial court of submitting false time sheets to a United States Marshal. On appeal, the defendant claimed that he lacked intent to defraud the government. In denying the appeal, the court found that since section 1001 was designed to protect the government against those who would cheat or mislead it, proof of an intent to deceive was sufficient to sustain a conviction under this section. The court distinguished “intent to deceive” from “intent to defraud” as follows:

Intent to deceive and intent to defraud are not synonymous. Deceive is to cause to believe the false[hood] or to mislead. Defraud is to deprive of some right, interest or property by deceit. Since the purpose of 18 U.S.C. § 1001 is to protect the government against those who would cheat or mislead it in the administration of its programs, a charge that includes specific intent to deceive along with the other elements mentioned above comports with 18 U.S.C. § 1001.

Having set forth the prima facie case for the previously discussed statutes, we are now in a position to discuss their applicability to a defective pricing action. The discussion in Part II indicates, however, that while the statutes are similar in a number of respects, they do contain some significant differences. These similarities and differences will become more apparent as we apply these statutes to our hypothetical problem set forth in Part III of this article.

129. Id. at 479-80; see also Blake v. United States, 323 F.2d 245, 247 (8th Cir. 1963).
130. Lichenstein, 610 F.2d at 1276.
131. Godwin, 566 F.2d at 975.
132. Id.
III. Application of Analysis to Hypothetical Problem

In this section we explore in the context of a hypothetical example the government contractor's liability for defective pricing under the Truth in Negotiations Act and the False Claims Act. At the same time we explore the interrelationship between the two Acts. A graphic illustration of the relationship between the two Acts may be found in Appendix A.

A. Hypothetical

Smith Corporation was awarded a defense contract by the Air Force for the replacement of 500 Warhawk computer terminals. The contract called for delivery of fifty terminals a week, the first delivery due six months after contract award and the remaining deliveries due every two weeks thereafter. Once the terminals were installed, Smith was to provide consulting and programming services for a period of three months. The contract was a negotiated defense contract in excess of $500,000 and was subject to the requirements of the Truth in Negotiations Act.

As part of Smith's pricing proposal for the supply of the 500 Warhawk computer terminals, Smith submitted its cost figures, which consisted of estimated labor hours, material costs, and vendor quotations on DD Form 633. With respect to the consulting services, the government negotiators informed Smith that the price for these services would be based on the education and experience of its employees. The greater the education and experience the more Smith could charge. As part of Smith's pricing proposal for these services, Smith submitted on DD Form 633 resumes reflecting the education and experience of its employees. Smith and the government negotiators reached agreement on price; Smith then executed a cost or pricing certificate certifying the accuracy, completeness, and currency of its cost or pricing data as of the date the agreement was reached.

Smith delivered according to schedule the 500 computer terminals. Each delivery, ten in all, was accompanied by DD Form 250 invoicing the government at prices based on previously submitted cost or pricing data. Smith also successfully completed its consulting and programming services and submitted one invoice to the government for its services. Six months

134. In United States v. Foster Wheeler Corp., 447 F.2d 100 (2d Cir. 1971), the contractor argued that the Truth in Negotiations Act withdraws defective pricing from the False Claims Act because under the rules of statutory construction, the general statute, the False Claims Act, must yield to the specific, the Truth in Negotiations Act. The court disagreed with the contractor and held that the Truth in Negotiations Act does not supersede the False Claims Act. It emphasized that "there is no inconsistency between an act which deals with fraud and one which deals with data which are inaccurate, incomplete or noncurrent." Id. at 101. Thus, the same defective pricing actions may constitute a violation of both Acts.
after Smith provided its consulting and programming services, the DCAA conducted a routine defective pricing audit. The audit revealed that Smith realized on its Air Force contract a profit of 30% on cost as compared to an estimated profit shown on its DD Form 633 of 10% on cost. The auditors discovered that Smith Corporation had inflated its vendor quotations by 10% before submitting those quotations to the government. It was also discovered that Smith had failed to disclose labor hour data on components which were similar to, but not identical with, major components of the Warhawk and that the estimated labor hours contained on its DD Form 633 and supporting schedules for the Warhawk were some 15% higher than the labor hours for the comparable components. The audit further revealed that Smith overstated its price for consulting services by embellishing the resumes of its employees. The investigation concluded that, as a result of Smith Corporation's activities, the federal government was overcharged $200,000.

B. Analysis of Hypothetical

As the discussion below indicates, the same acts that constitute a violation of the Truth in Negotiations Act may also establish liability under the False Claims Act. However, our analysis further reveals that a contractor's defective pricing actions may violate the Truth in Negotiations Act without violating the False Claims Act and vice versa.

The facts of our hypothetical case reveal that Smith Corporation manipulated and withheld cost or pricing data from the government, the effect of which was to enable Smith to realize a significant profit on its Air Force contract. These facts appear to make out a prima facie case of defective pricing under the Truth in Negotiations Act.

First, in connection with the negotiation of its non-exempt government contract, Smith Corporation executed a Certificate of Cost or Pricing Data when it reached agreement on price with the government. Thus, unlike Libby Welding Co.,¹³⁵ we are not faced with a situation where the government is precluded from asserting a defective claim because of the absence of a certificate.

Second, the labor hour data on components which were similar to, but not identical with, major components of the Warhawk was clearly cost or pricing data as defined by DAR § 3-807.1(a)(l) and accordingly should have been presented to the government during price negotiations. This cost data consisted of facts "which prudent buyers and sellers would rea-

reasonably expect to have a significant effect on price negotiations.”¹³⁶ Moreover, as a result of Smith Corporation’s (1) inflation of Vendor quotations, (2) failure to submit labor hour data on comparable components, and (3) submission of embellished resumes, the information submitted on DD Form 633 was inaccurate and thus did not satisfy the requirement under the Truth in Negotiations Act that cost or pricing data be accurate, complete, and current. In short, Smith Corporation’s cost or pricing data was defective.

Third, in price negotiations, the government relied on Smith’s defective data. Fourth, the government’s reliance on Smith Corporation’s defective data, resulted in the government paying higher prices for the computer terminals and the consulting services.

Turning to the question of damages under the Truth in Negotiations Act, the government is entitled to a price reduction equal to $200,000, the amount of Smith Corporation’s cost overstatement plus the appropriate overhead and profit. To the extent that Smith Corporation can show that (1) even if it had disclosed correct data, the parties would not have negotiated a price reduced by the total amount of the overstatement,¹³⁷ or (2) that it understated certain of its contractual costs, the government’s recovery will be reduced accordingly.¹³⁸

The same hypothetical facts also appear to establish a violation of the False Claims Act. In this regard, each of the three relevant statutes discussed in Part II of this paper is considered separately.

1. **The Civil False Claims Statute**

Smith Corporation’s submission of defective cost or pricing data on DD Form 633, its subsequent certification of that data as accurate, complete, and current, and its subsequent invoices to the government on DD Form 250, are all acts that establish a prima facie violation of The Civil False Claims Statute (31 U.S.C.A. § 3729).

First, all three acts fall within the definition of “claims” under section 3729, as they were “attempts [by Smith] to cause the Government to pay out sums of money.”¹³⁹

Second, Smith Corporation’s claims were all false; the DD Form 633 was false because it contained inaccurate cost or pricing data. The data reflected inflated cost figures and embellished resumes. The Certificate of

¹³⁷. See supra note 34 and accompanying text.
¹³⁸. Id.
Cost or Pricing Data was false because it certified that the data were accurate when they were not. The DD Form 250's were false because they contained prices based on the inaccurate data.

Third, Smith acted with the apparent requisite intent, whether intent is defined as the "knowing submission" of false claims or a submission with "intent to defraud." Our hypothetical facts suggest that Smith knowingly and intentionally manipulated cost or pricing data in order to negotiate a higher price with the government for the 500 Warhawk computer terminals and the consulting and programming services.

As a result of Smith Corporation's actions, the government may recover (1) double its actual damages, (2) a $2,000 forfeiture for each false claim, and (3) its costs of suit. Like the computation of damages under the Truth in Negotiations Act, actual damages under section 3729 are computed by determining the amount of the cost overstatement due to the false data, subtracting amounts eliminated during negotiations, and then adding appropriate burden and profit. Thus, assuming that Smith's cost overstatement was not eliminated in any amount during price negotiations, it appears that Smith would be liable for at least $400,000 in actual damages.

With respect to Smith Corporation's liability for forfeitures, the number of imposable forfeitures is generally set at the number of individual false payment demands over which the contractor had knowledge and control. Moreover, the government cannot recover more than one forfeiture for the very same false claim. Thus, the application of these rules to our hypothetical case requires an assessment of eleven forfeitures or $22,000 on the basis of the eleven DD Form 250's Smith Corporation used in invoicing the government. Note that while Smith's other acts—the submission of DD Form 633 and the execution of a Certificate of Cost or Pricing Data—also constitute false claims, Smith should not be assessed additional forfeitures because the government then would be collecting twice on the very same false claims.

2. The Criminal False Claims Statute

Our hypothetical facts also establish a prima facie violation of the Crim-
Defective Pricing of Government Contracts

Defective False Claims Statute (18 U.S.C. § 287). First, the submission of defective cost or pricing data on DD Form 633, the subsequent certification, and the subsequent invoices to the government on DD Form 250's certifying prices based on that data are all claims within the definition of Neffert-White.146 Second, for the reasons already set forth in our discussion of section 3729 liability, the DD Form 633's, the Certificate, and the DD Form 250's were all false. Third, the intent element of section 287 appears to be satisfied. Smith's inflated cost figures and embellished resumes of its employees suggest that Smith acted with knowledge that a claim was false and with consciousness that it was doing something that violated the law.147

3. The Criminal False Statements Statute

Our hypothetical facts also appear to make out a prima facie violation of the Criminal False Statements Statute (18 U.S.C. § 1001).

First, the DD Form 633's, the Certificate, and the DD Form 250's are all "statements" under section 1001, inasmuch as each document is a written representation to the government of Smith Corporation's cost or pricing data, the accuracy of that data or the prices ultimately based on that data. Second, these statements relate to matters within the jurisdiction of a government agency as all were made to the Air Force as part of that agency's procedure for the pricing and payment of government contracts. Third, for the reasons noted above, all the statements were false.

Fourth, these statements were "material" within the meaning of section 1001. The submission of defective cost or pricing data and its subsequent certification resulted in a higher contract price. Clearly, an unjustifiable contract price, obtained in violation of the Truth in Negotiations Act, would be material in the sense that such a price works to impair the functioning and efficiency of the Air Force's procurement branch whose mission is to negotiate the best price for the government.148 Even if Smith's false statements did not cause an increase in the contract price, they arguably would be material because they had the capability of impairing the functioning of the Air Force's procurement branch.149 Moreover, Smith's invoices to the government on the DD Form 250's were material in that they sought payment of sums that Smith Corporation had no right to collect.

146. 390 U.S. at 233. See supra notes 70-71 and accompanying text.
147. Maher, 582 F.2d at 847. See supra notes 114-15 and accompanying text.
148. United States v. Lichenstein, 610 F.2d at 1278. See supra notes 125-26 and accompanying text.
149. Lichenstein, 610 F.2d at 1278.
Fifth, the intent element of section 1001 appears to be satisfied. Once again, the inflated cost figures and the embellished resumes suggest that Smith Corporation made the false statements knowingly, willfully, and with the intent to deceive the government during price negotiations.\textsuperscript{150}

Thus, in our hypothetical example the same acts that constitute defective pricing under the Truth in Negotiations Act also establish liability under the False Claims Act. However, not all violations of the Truth in Negotiations Act necessarily constitute violations of the False Claims Act. It is possible, therefore, that the government may successfully prosecute a government contractor for defective pricing under the False Claims Act but be unsuccessful in prosecuting the contractor for the same acts under the Truth in Negotiations Act. These points can be neatly demonstrated by modifying our hypothetical example.

For example, suppose that the government’s price negotiation memoranda reveal that the negotiators never relied on Smith’s inflated cost figures or embellished resumes. Rather, the memoranda establish that prior to Smith’s proposal submission, Air Force negotiators had arrived at a contract price range by surveying what other Department of Defense (DOD) agencies were paying for similar computer terminals and consulting and programming services. The memoranda further reveal that because the low end of the contract price range was higher than Smith’s proposal submission even with the inflated cost figures and embellished resumes, the Air Force negotiators “jumped” at Smith’s proposal price without actually relying on the information contained in the proposal. Under these circumstances the government’s defective pricing action under the Truth in Negotiations Act would be defeated because the government would be unable to prove that it relied upon Smith’s defective cost or pricing data in negotiating the contract price and that such reliance resulted in a higher contract price.

Contrary to the result under the Truth in Negotiations Act, the government’s failure to prove reliance, and that the defective data resulted in a higher contract price, would not defeat its action under the False Claims Act. Under section 1001, the government need not prove that it detrimentally relied on a false statement. It must prove that Smith submitted a material false statement. As discussed earlier, materiality is defined in terms of whether the statement had the capability of influencing or impairing the functioning of a government agency. The statement, therefore, need not cause the government pecuniary loss.\textsuperscript{151} Thus, in our modified

\textsuperscript{150} Id. at 1276.
\textsuperscript{151} Id. at 1278.
hypothetical example, the requirement of materiality would be deemed satisfied because Smith's mere submission of defective data, regardless of whether that data was relied on or its economic effect, was capable of influencing or impairing the functioning of the Air Force's procurement branch.

The result would probably be the same under the Criminal False Claims Statute (18 U.S.C. § 287). Unlike the Criminal False Statements Statute (18 U.S.C. § 1001), the Criminal False Claims Statute (18 U.S.C. § 287) does not explicitly state that materiality is an essential element of the offense. Therefore, courts are divided on the question of whether materiality is an element of a section 287 suit. The courts that have held that materiality is an element of section 287, while not specifically addressing the issue, would probably adopt the section 1001 definition of materiality and conclude that materiality is satisfied regardless of whether the government relied to its detriment on the false claim. Those courts that have held that materiality is not an element of a section 287 offense probably would focus on the submission of a false claim. The question of detrimental reliance would be irrelevant. Thus, Smith probably would be liable under section 287 whether or not the government established detrimental reliance.

In section 3729 suits, courts have permitted recovery of the statutory forfeiture ($2,000) without requiring that actual damages be proven. Thus, the government need not show detrimental reliance in order to assess forfeitures under section 3729.

Now, let us modify the intent element of our hypothetical example. Suppose, for example, that Smith Corporation failed to disclose certain vendor quotations because it believed that such quotations were inaccurate and unreasonably low, and thus, unreliable for purposes of pricing. Moreover, suppose that Smith inadvertently made an error while transposing figures from its work sheets to its pricing proposal, resulting in an increase in the contract price.

Under these circumstances, Smith Corporation would still be held liable under the Truth in Negotiations Act for any overstatement in contract price caused by the submission of defective cost or pricing data. The fact that Smith had honorable intentions and did not intentionally withhold cost or pricing data from the government is irrelevant. The Truth in Negotiations Act and the implementing regulations address the question of defects in the data and not individual or corporate intent in determining

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152. See supra note 94 and accompanying text.
153. See supra note 69 and accompanying text.
liability. Any culpability or lack of it on the part of Smith Corporation does not affect its obligation to refund the money.

Smith Corporation, however, could probably escape liability under the False Claims Act. Before liability under the False Claims Act could be found, the government would have to prove that Smith Corporation presented a false claim or statement with the requisite intent. Specifically, in order to prevail under section 3729, the government would have to establish that Smith Corporation presented a false claim either with the intent to defraud or knowing that such a claim was false. Under section 287, the government would have to establish that Smith Corporation knowingly submitted a false claim with the consciousness that it was doing something that was morally wrong or that violated the law. Under section 1001, the government would have to establish that a false statement was submitted knowingly, willfully, and with the intent to deceive. The fact that Smith Corporation believed the data to be inaccurate and unreliable and that Smith inadvertently submitted defective data would negate the proposition that it had the intent to violate the False Claims Act. Absent such intent, there can be no violation of the False Claims Act.

In summary, the same acts that constitute liability under the Truth in Negotiations Act may also establish liability under the False Claims Act. Our analysis also reveals that a party may escape liability under the Truth in Negotiations Act, but be found liable under the criminal and civil provisions of the False Claims Act. Thus, if the federal government does not rely on defective cost or pricing data, or if there is no price increase as a result of the submission of defective cost or pricing data, the government is not entitled to a price reduction under the Truth in Negotiations Act. Nevertheless, neither reliance nor actual damages are necessary to sustain a criminal conviction or civil liability under the False Claims Act. On the other hand, not all violations of the Truth in Negotiations Act necessarily constitute violations of the False Claims Act as well. Only in those instances where a party submitted defective data to the government during contract price negotiations with the requisite intent, can liability also be imposed under the False Claims Act.
# APPENDIX A

## Breakdown and Comparison of the Elements Comprising a Violation of the Truth in Negotiations Act and the False Claims Act

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<tr>
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<tbody>
<tr>
<td>1 Certificate Accompanied By Cost Or Pricing Data</td>
<td>Statement</td>
<td>Claim</td>
<td>Claim</td>
</tr>
<tr>
<td>3 Cost Or Pricing Data Was Defective, i.e., Inaccurate, Incomplete, Or Noncurrent</td>
<td>Statement Was False</td>
<td>Claim Was False</td>
<td>Claim Was False</td>
</tr>
<tr>
<td>4 Defective Cost Or Pricing Data Was Relied On By The Government Negotiators</td>
<td>Statement Need Not Have Been Relied On</td>
<td>Claim Need Not Have Been Relied On</td>
<td>Claim Need Not Have Been Relied On</td>
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<tr>
<td>5 Contract Price Was Higher Than It Otherwise Would Have Been</td>
<td>Statement Had A Material Impact — But No Damages Need Be Proven</td>
<td>Damages Need Not Be Proven</td>
<td>Damages Need Not Be Proven</td>
</tr>
<tr>
<td>6 No Intent Required</td>
<td>Knowing And Willful Submission Of False Statement (Intent To Deceive)</td>
<td>Knowing Submission Of False Claim (Intent to Violate The Law)</td>
<td>Knowing Submission Of False Claim or Intent To Defraud</td>
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### Penalties

- Government Entitled To A Refund For Any Overstated Portion Of The Contract Price. Overstatement May Be Reduced By An Amount That Was “Negotiated Out” Of The Contract Price. Contractor Can Also Offset The Price Reduction By Establishing That It Understated Cost Or Pricing Data Submitted With Respect To The Same Pricing Action
  - Maximum 5 Years Imprisonment And/Or Up To $10,000 Fine
- Maximum 5 Years Imprisonment And/Or Up To $10,000 Fine
- Double Damages Plus A $2,000 Forfeiture For Each False Claim. Actual Damages Need Not Be Proven To Recover The Forfeiture Provision