Government Contracts Advisory

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CONTACTS

For further information regarding the topic discussed in this update, please contact one of the professionals below, or the attorney or public policy advisor with whom you regularly work.

Raymond B. Biagini
202.496.7687

David Kasanow
202.496.7194

Jason N. Workmaster
202.496.7422

Alejandro L. Sarria
202.496.7751

John W. Sorrenti
202.496.7616

U.S. District Court for the District of Columbia Issues Significant False Claims Act Decision

On August 3, 2011, the U.S. District Court for the District of Columbia issued an opinion on a motion to dismiss in the civil False Claims Act ("FCA") case *United States v. Kellogg Brown & Root Servs., Inc. ("KBR")*, **No. 10-cv-530**. (Slip Op.). The opinion is significant for at least two reasons. First, it highlights the importance of the decision of the D.C. Circuit in *United States v. Science Applications Int'l Corp (SAIC)*, 626 F.2d 1257 (D.C. Cir. 2010), regarding the "implied certification" theory of FCA liability. Second, although the district court denied KBR's motion to dismiss the FCA count of the complaint, the opinion reinforces existing case law that demonstrates a reluctance by the courts to transform contract interpretation disputes into fraud cases, particularly where there is evidence the government knowingly paid claims of the type that it later alleges were false.

Background

The case arises out of KBR's Logistics Civil Augmentation Program ("LOGCAP III") contract with the Army under which KBR has provided logistical services and support to military operations around the world, particularly in support of the war in Iraq. According to the government, the contract required the military to provide any necessary force protection and prohibited KBR and its subcontractors from using, and billing for, armed private security unless certain conditions were met. The government further alleges that KBR and its subcontractors used unauthorized armed private security in support of their work under the LOGCAP III contract in Iraq and that KBR knew that such usage was prohibited but billed the government for it anyway. In response, KBR contends, among other things: (1) that LOGCAP III did not prohibit the use of armed private security as suggested by the government or, at the very least, that KBR had a reasonable interpretation of the contract on this point; (2) that KBR did not bill the government for armed private security in the manner the Government contends; and (3) that the government knew, due to the inability of the government to provide sufficient force protection, that KBR and its subcontractors were using armed private security in Iraq.

KBR's Motion to Dismiss

Upon the filing of the government's complaint, KBR moved to dismiss. With respect to the complaint's FCA count, KBR first argued that the government improperly relied upon an "implied certification" theory of FCA liability. The "implied certification" theory is used by the government (or a *qui tam* relator) to assert that, even though a given claim for payment (such as an invoice) contains no false statements on its face, the claim nevertheless has the

potential to be a "false claim" because, by submitting the invoice, the contractor implicitly certifies that it has complied with material terms of its contract. In its motion to dismiss for improper application of this theory, KBR argued that, unless the contract term in question was an "express" condition of payment, non-compliance with that term could not result in the submission of a "false claim" within the meaning of the FCA. KBR further argued that none of the terms at issue in the case were such "express condition of payment" terms.

KBR also argued that the government's complaint should be dismissed because the government had failed to plead sufficient facts in support of its scienter allegations. In this regard, KBR argued that the facts as pled demonstrated that KBR had (at the very least) a reasonable interpretation of the contract and that the government knew of the widespread use of armed private security in Iraq during the relevant time period.

The District Court's Opinion

The district court addressed KBR's implied certification argument at length. The court noted that, up until the D.C. Circuit's *SAIC* decision, it was "uncertain" in the D.C. Circuit whether a particular contract term had to be an express condition of payment in order for non-compliance with that term to give rise to FCA liability upon the submission of an otherwise-accurate invoice. Slip Op. at 19-20. The court further noted that the Second Circuit had answered this question in the affirmative in *Mikes v. Straus,* 274 F.3d 687 (2d Cir. 2001), and *United States ex rel. Kirk v. Schindler Elevator Corp*., 601 F.3d 94 (2d Cir. 2010). If the Second Circuit's rule were applied, the court stated, KBR would "likely prevail" because none of the LOGCAP III contract terms at issue in the case "expressly" condition payment to KBR upon compliance with contract terms. *Id.* at 20. However, the court went on to find that the D.C. Circuit, in *SAIC*, had chosen not to adopt the Second Circuit's test but rather had found that, even if a particular contract term was not an "express" condition of payment, non-compliance with that term could still give rise to FCA liability if it was a "material" term and the defendant acted with the requisite "scienter." *Id.*

Finding that the holding of *SAIC* "controlled" the *KBR* case, the court turned to whether the government had pled sufficient facts in support of its contention that the contract terms in question were material and that KBR had acted with the necessary scienter. On these two issues, the court found the government's pleading survived KBR's motion to dismiss. However, the court found "persuasive" KBR's argument that it could not have acted with the requisite scienter so long as it had a reasonable interpretation of the contract. *Id.* at 23. This is because claims involving "only a contractual dispute" are not false with the meaning of the FCA. *Id.*

The court also addressed the issue of the government's knowledge of the alleged false claims. Here, the court noted that there are "'occasions when the government's knowledge of or cooperation with a contractor's actions is so extensive that the contractor could not as a matter of law possess the requisite state of mind to be liable under the FCA.'" *Id.* (quoting *Shaw v. AAA Eng'g & Drafting, Inc*., 213 F.3d 519, 534 (10th Cir. 2000). Applying this rule to the *KBR* case, the court found that, if KBR demonstrates that the government knowingly paid claims that had contained armed private security expenses, that showing "will cut strongly in KBR's favor." *Id.*

Conclusion

The *KBR* decision drives home the significance of *SAIC* in the development of

the theory of “implied certification,” particularly in the D.C. Circuit. It also serves as a reminder that showing: (1) that an allegation of fraud is really a contract dispute, or (2) that the government knew about the alleged fraud and paid the contractor’s claims anyway, are powerful tools in defending an FCA case.