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“Conditions of Participation” in False Claims Act Government Procurement Cases

By Kyle R. Jefcoat

The author of this article discusses “conditions of participation” in False Claims Act (“FCA”) cases and concludes that a failure to strictly comply with the myriad requirements that procurement contracts impose should not result in FCA liability where the government retains alternative ways to remedy the situation.

Government procurement contracts include hundreds of compliance requirements which creates an intricate web of statutory, regulatory, and contractual obligations on contractors. These include a multitude of Federal Acquisition Regulation (“FAR”) and other regulatory provisions which are often simply incorporated by reference—so you cannot know the applicable requirements based on a review of the contract itself. In addition, there are thousands of military standards and military specifications (“MilSpecs”) that may apply to a contractor’s performance. Contractors thus risk violating a multitude of complex regulatory and contractual requirements.

CONSEQUENCES

What should the consequences be for violating one of these many requirements? Beyond the normal contract remedies, should the contractor be liable under the False Claims Act, (“FCA”) just for that failure?

The courts agree that there should be limits to the reach of the FCA.

• “[W]ithout clear limits and careful application, the implied certification theory is prone to abuse by the government and qui tam relators who, seeking to take advantage of the FCA’s generous remedial scheme, may attempt to turn the violation of minor contractual provisions into an FCA action.”

• “If every dispute involving contractual performance were to be transformed into a qui tam FCA suit, the prospect of litigation in

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1 31 U.S.C. § 3729 et. seq.

government contracting would literally have no end.”

- “[F]raud requires more than breach of promise: fraud entails making a false representation, such as a statement that the speaker will do something it plans not to do. Tripping up on a regulatory complexity does not entail a knowingly false representation.”

However, the Circuit courts remain split on exactly how to address the question of materiality and whether a violation of a compliance requirement triggers FCA liability. For instance, the First Circuit will find FCA liability where compliance with an underlying statute, regulation, or contractual provision is material to the government’s decision to pay. In contrast, the Third Circuit requires that for an alleged violation of a regulatory or contractual provision to create FCA liability, “a plaintiff must show that if the Government had been aware of the defendant’s violations of the Medicare laws and regulations that are the bases of a plaintiff’s FCA claims, it would not have paid the defendant’s claims.”

“CONDITIONS OF PARTICIPATION” OR “CONDITIONS OF PAYMENT”?

Several circuits have addressed the critical distinction between “conditions of participation” and “conditions of payment.” “Conditions of participation” are typically viewed as requirements for which the government has other remedies and the consequence of a violation is the loss of the ability to participate in the government program. In contrast, a “condition of payment” is a requirement that “if the government knew they were not being followed might cause it to actually refuse payment.” Most of the Circuit courts that have addressed this distinction have not permitted FCA liability based on violating a “condition of payment.”

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4 United States ex rel. Main v. Oakland City Univ., 426 F.3d 914, 917 (7th Cir. 2005).
7 See, e.g., Mikes v. Straus, 274 F.3d 687, 701-02 (2d Cir. 2001); United States ex rel Hobbs v. Medquest Assocs., 711 F.3d 707, 714 (6th Cir. 2013); Ebeid ex rel. United States v. Lungwitz, 616 F.3d 993, 996-98 (9th Cir. 2010); United States ex rel. Conner v. Salina Reg’l Health Ctr., 543 F.3d 1211, 1220 (10th Cir. 2008).
8 See Conner, 543 F.3d at 1220.
9 Id.
“Conditions of Participation” in False Claims Act Government Procurement Cases

participation.” The Third Circuit in Wilkins explained the basis for the distinction:

[C]onsidering that the Government has established an administrative mechanism for managing and correcting Medicare marketing violations which includes remedies for violations other than the withholding of payment otherwise due, it is clear that, although the Government considers substantial compliance with the marketing regulations “a condition of ongoing Medicare participation, it does not require perfect compliance as an absolute condition of receiving Medicare payments for services rendered.” Conner, 543 F.3d at 1221. Furthermore, we think that anyone examining Medicare regulations would conclude that they are so complicated that the best intentioned plan participant could make errors in attempting to comply with them.

Notably, those “condition of participation” cases have primarily been limited to Medicare cases. Indeed, the Ninth Circuit has gone so far as to explain that the condition of participation versus condition of payment distinction is limited to Medicare FCA cases.

THE SIXTH CIRCUIT’S MATERIALITY TEST

The Sixth Circuit recently weighed in regarding the proper materiality test for FCA litigation applied to a claimed fraud in a government procurement case. While the Sixth Circuit does not use the term “condition of participation,” the case follows the logic explained in Wilkins. The plaintiff, American Systems Consulting Inc. (“ASCI”), and its CEO filed a suit as whistleblowers under the FCA claiming that its competitor, ManTech Advanced Systems International and its subsidiaries (“ManTech”) violated the FCA by proposing an individual to perform a contract which ManTech never actually intended to use.

As part of the proposal process, the government required that the offerors designate an individual to serve as the Program Manager for the procurement. The solicitation also required the government to approve any replacement for the Program Manager if the awardee wanted to change that position.

As part of its initial proposal and subsequent proposal revisions, ManTech included David Kendall-Sperry as its proposed Program Manager. However, at

11 Wilkins, 659 F.3d at 310.
12 See, e.g., Mikes, 274 F.3d at 701–02; Hobbs, 711 F.3d at 714; Conner, 543 F.3d at 1220; but see Vigil, 639 F.3d at 799 (applying to Federal Family Education Loan Program).
13 See Ebeid, 616 F.3d at 997; United States v. Univ. of Phoenix, 461 F.3d 1166, 1177 (9th Cir. 2006).
the time that ManTech submitted its Best and Final Offer, Mr. Kendall-Sperry had resigned from ManTech and entered the seminary. ASCI alleged that ManTech was aware that when it submitted its final proposal revision that Mr. Kendall-Sperry could not fulfill the role of Program Manager, but decided to keep him in the proposal.

As part of the proposal evaluation process, ManTech received the highest rating of “green” under the “Technical and Management Capability” while ASCI received a rating of “yellow” because ASCI “failed to address the specific skills of its proposed Program Manager at all.” Ultimately, DITCO awarded the contract to ManTech.

ASCI filed protests at the Government Accountability Office regarding the award decision, but those protests were denied or dismissed. ASCI then filed suit in district court alleging an FCA violation based on ManTech’s inclusion of Mr. Kendall-Sperry in its proposal when ManTech did not actually intend to use Mr. Kendall-Sperry as the Program Manager if it was awarded the contract.

The Sixth Circuit’s decision essentially boiled down to a review of materiality. First, the Sixth Circuit, relying on the deposition testimony of two members of the government’s proposal evaluation team, found that the resume and skills of the Program Manager were reviewed only to establish the “skill level, knowledge, and experience of the personnel that the bidder was capable of offering,” and that the review of the Program Manager resume indicated “a reliance interest in the general qualifications, not the specific identity, of the manager.” Second, and more importantly, the court determined that ManTech’s switch in Program Managers was not in fact material to the agency. For instance, the agency knew of the switch before contract performance began and still worked with ManTech rather than terminate the contract and resolicit.

The court was careful to explain that its decision was not based on the subjective determinations of the government officials involved in this particular case to continue the contract with ManTech. Instead, the court said that the government’s decision to continue to contract with ManTech was simply another indicator of how a reasonable objective decision-maker would view the

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15 Id. at *5.
16 Id. at *10.
17 Id. at *13–14.
18 Id. at *15–16.
The court also cautioned that there are multiple reasons why an agency might continue to use a contractor which had made a material misrepresentation: “The government may make operational changes or investments in reliance on the agreement. Alternative contractors may enter other deals, reducing the supply of available contractors and making it more costly for the government to find a replacement. The costs associated with implementing another bidding process at the last minute also may be significant.”

The court then noted that none of those circumstances existed in the procurement in question and that the government’s determination to continue using ManTech served as evidence showing that the alleged misrepresentation was not material.

THE FIFTH CIRCUIT’S SPICER V. WESTBROOK DECISION

The Sixth Circuit’s ASCI decision has many similarities to last year’s Fifth Circuit decision in United States ex rel. Spicer v. Westbrook. In that case, the Fifth Circuit affirmed the dismissal of an FCA claim premised on an alleged failure of a contractor to comply with particular military specifications in its contract for the sale of military vehicles. In Spicer, the Fifth Circuit found that compliance with the particular military specifications was not a prerequisite for payment.

In fact, the Fifth Circuit looked to the fact that the government, under FAR provisions incorporated in the contract, had a range of remedies for noncompliance with the specifications as evidence that compliance with the particular military specifications was not a prerequisite for payment:

Here, FAR clause 52.246-2 provides in part that the United States “has the right to either reject or to require correction of nonconforming supplies. . . . [T]he Contracting Officer may require or permit correction in place, promptly after notice, by and at the expense of the Contractor.” 48 C.F.R. §§ 52.246-2(f)–(g). As in United States ex rel. Steury v. Cardinal Health, Inc., 625 F.3d 262 (5th Cir. 2010), the language establishing the United States’ ability to seek a range of remedies in the event of noncompliance suggests that payment was not conditioned on [contractor’s] certification of compliance.

Both ASCI and Spicer show courts attempting to find limits to prevent every government procurement regulatory or contractual failing from becoming the

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19 Id. at *16.
20 Id. at *18.
21 751 F.3d 354 (5th Cir. 2014).
22 Id. at 359.
23 Id. at 366–67.
24 United States ex rel. Spicer v. Westbrook, 751 F.3d 354, 366 (5th Cir. 2014).
basis of an FCA suit. Spicer made this point explicitly: “[n]ot every breach of a federal contract is an FCA problem.” More significantly, both of these cases fit within a broader development of not finding FCA liability where the alleged violation of statute, regulation, or contract is part of a circumstance where the government has discretion as to whether to continue to work with the contractor and has other remedies for violations. As discussed above, in the Medicare context, these types of violations—where the government retains other administrative remedies—have been termed “conditions of participation” and most of the Circuit courts that have addressed this distinction have not permitted FCA liability based on violating a “condition of participation.”

While neither ASCI or Spicer or use the term “condition of participation,” they both appear to fit squarely into that line of cases. In ASCI, the government retained multiple alternatives to enforce compliance—including terminating the contract—but chose not to exercise them. Spicer presented a very similar situation where the government could reject vehicles along with exercising a “range of remedies.”

**CONCLUSION**

Both of these cases indicate that the courts are willing to provide rational limits to the reach of the FCA. Medicare is not unique in this regard. The regulatory and contractual requirements in procurement contracts are also so complex that “anyone examining [them] would conclude that they are so complicated that the best intentioned [contractor] could make errors in attempting to comply with them.” A failure to strictly comply with the myriad requirements that procurement contracts impose should not result in FCA liability where the government retains alternative ways to remedy the situation—and cases like ASCI and Spicer which recognize this reality are welcome developments.

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25 See Spicer, 751 F.3d at 366 (quoting Steury, 625 F.3d at 268).
27 See Spicer, 751 F.3d at 366.
28 Wilkins, 659 F.3d at 310.