

## Military Contract Appeals Board Case Shows Risks Of Fraud

*Law360, New York (September 20, 2013, 11:55 AM ET)* -- The Armed Services Board of Contract Appeals again reminded the contracting community that honesty is the only policy when it comes to competing for federal projects. In Dongbuk R&U Engineering Co. Ltd., the ASBCA denied all of Dongbuk's claims for costs incurred during the performance of its contract despite the fact that the government received the bulk of the goods and services required by the contract.

The ASBCA found that Dongbuk was not entitled to payment for the services performed due to alleged fraudulent conduct of at least one of the company's officers. The government convinced the ASBCA that thanks to the CEO's alleged fraud, the company's contract was void and unenforceable. In essence, the ASBCA found that the alleged fraudulent activity extinguished Dongbuk's right to recover even the bare costs the company incurred in performing the contract, regardless of the quality of work or the government's satisfaction with the work provided.

The result in Dongbuk should come as no surprise, particularly in the current economic environment. However, the degree to which such scrutiny can impact a firm's ongoing business may raise some eyebrows. Dongbuk's claim amounted to nearly \$160,000 that the government withheld while the fraud claims were investigated and prosecuted (i.e., the government withheld monies for work that Dongbuk had actually performed due to the CEO's alleged fraud).

Given that criminal and civil actions can take years to resolve, those resources, which could be vital to a contractor's survival, could be withheld nearly indefinitely, crippling a company due to the bad actions of a single employee or manager. Thus, it is important to remember that actions of a single employee could cause a company to collapse, especially a small business.

Unfortunately, in light of the government's recent financial troubles, it is likely the government will try to expand its ability to recover payments made under contracts where allegations of fraud or false claims are raised — even if the alleged fraudulent actions amount to mere negligence.

A perfect example of how the government can change the rules in the middle of the game is the "deemed certification rule" found in the Small Business Jobs Act of 2010. Under that rule, should a contractor negligently or even inadvertently misrepresent its status as a small business, the representation will be deemed willful and intentional. That distinction is important because under the False Claims Act the alleged false claim must have arisen due to more than mere negligence.

However, with the stroke of a pen, the government changed the rules and made it so that intentional or reckless conduct was no longer required in order to penalize a contractor with significant civil penalties, which can include presumed damages of three times the value of the total contract. While the U.S. Small Business Administration has softened the strict liability of the "deemed certification rule" via regulation,

the provision in the Jobs Act is just the type of statutory change which could make mere negligence grounds for voiding an entire contract.

Indeed, certain members in Congress have made it clear that they feel it is time to crack down on contractors, and some in the media have followed suit, launching investigations into perfectly legal contractor actions where the representative or writer disagree with the current state of the law.

Lastly, and as noted above, contractors must be aware of the actions of their employees and the roles they play in the federal procurement process. While, in the Dongbuk case, it was the CEO's actions that cost his company dearly, the activities of lower-level employees can have a similar impact, especially for smaller companies.

It is difficult to watch the actions of every employee as closely as the government would like, so limit access to critical documents and company resources to those who absolutely need access to perform their jobs. Also, make sure that, whenever possible, a second or third employee has access to the work of any other single employee. This will help to keep fraud in check and catch problems early.

We have seen cases where long-time employees of a company fall into difficult times or otherwise decide to take actions that benefit themselves at the expense of the company. Some of these actions, if connected to federal contracts, can result in serious repercussions for the company as a whole.

Due to the combination of increased audits and investigations with the current atmosphere of fiscal austerity, contractors should keep an eye on the state of the law and ensure all representations in proposals or otherwise are entirely accurate to avoid suffering the types of extreme penalties levied against Dongbuk and others like it.

Further, companies should increase the oversight on all employees to mitigate the risk that a rogue employee could take actions which then severely impact the company's viability by exposing it to the risk of a voided contract. All of the issues discussed herein can be avoided, and with solid policies and procedures, any risk can be greatly reduced and nearly eliminated.

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