I. Introduction

1. False Claims

A false claim is any request for money or property that:

we are not entitled to under the contract or the law, or

is supported by incorrect statements, facts, or figures that you know are incorrect or willfully fail to ascertain are correct where such information is reasonably available to you or to those under your authority, or

is supported by correct, but misleading information; i. e., the information provided is not current, does not accurately represent the situation at hand, or is not complete and you know that such information was not current, accurate or complete or you willfully fail to ascertain that it is where such information is reasonably available to you or to those under your authority.

2. Responsibility

As a representative of our company, you are responsible for assuring that we are paid pursuant to the contract and the law for all the work that we have performed. This means that you will be preparing and submitting payment requests for contract work, extra work, changed work, and additional costs incurred as a result of some event for which we are entitled to compensation. In other words, you will be submitting claims and you will often be required to certify these claims.

If you are preparing or certifying a claim, you are responsible for assuring that:

we are entitled under the contract or the law to make the claim;

the information in the claim is correct;

the information in the claim is not misleading and is current, accurate, and complete.

If you fail in this responsibility, you and the company could be subject to criminal and/or civil penalties, including debarment.

3. This Manual

Once a false claim is submitted, the crime or civil violation is consummated. It's too late! The deed is done! Unfortunately, it's one of the few things in this life that can ever be classified as *"done*." It is imperative therefore that those who are responsible for preparing and/or certifying claims know what their responsibility is and conscientiously carry it out.

The purpose of this manual is to provide you with:

A general understanding or BACKGROUND of the false claims problem;

Statutes concerning false claims;

Government Administration Penalties and Sanctions;

What the government looks for in audit;

Guidelines for preparing a claim;

Tips in reviewing a claim; and

Guidelines for proper disclosure.

If this manual does not answer your questions, or if you have any concerns or doubts, **ASK BEFORE SUBMITTING OR CERTIFYING YOUR CLAIM**. Second thoughts, sudden attacks of conscience, and true confessions are difficult to deal with after the fact.

II. Background

1. History of the Problem

In the 1950s and the early 1960s, the General Accounting Office (GAO) discovered numerous instances of "overpricing" by Government contractors on negotiated contracts. The GAO report, submitted to Congress on May 29, 1959, detailed many overcharges on negotiated contracts with the Department of Defense (DOD), particularly those involving airplane and missile procurements. The GAO believed the overcharges resulted from the failure of the contractors to disclose complete, accurate, and current pricing data to the Government negotiators prior to negotiation. The GAO report did not express concern about overcharges on construction contracts since the vast majority of them were awarded after competitive bidding.

In 1962, Congress enacted the Truth In Negotiations Act (TINA). In essence, TINA requires contractors to submit cost or pricing data and certify, to the best of their knowledge and belief, the cost or pricing data submitted is accurate, complete, and current.

TINA is but one of many statutes designed to eliminate or reduce contractor fraud. Other statutes that will be discussed in this training program include: 1) Civil False Claims Act (31 U.S.C. §3729); 2) Criminal False Claims Act (18 U.S.C. §287); 3) Program Fraud Civil Remedies Act (31 U.S.C. §3801); 4) the Fraudulent Claims section of the Contractor Disputes Act (41 U.S.C. §604); 5) False Statements Act (18 U.S.C. § 1001); 6) Racketeer Influenced and Corrupt Organization Act (18 U.S.C.§1961); and 7) Obstruction of Federal Audit (18 U.S.C. §1516).

There has been an evolution of how the Government has handled alleged fraud by contractors. In the past, the Government relied upon the criminal justice system to combat fraud by the contractors. The Government learned, however, that such reliance was not the solution to the problem since more than two thirds of all fraud cases referred to the Department of Justice (DOJ) were declined for criminal prosecution by the DOJ. One of the reasons the DOJ declined the prosecution is the constitutional requirement of proving criminal cases beyond a reasonable doubt.

More recently, the Government has turned to civil remedies provided for in the statutes, as well as debarment and suspension as means of combating alleged fraud on the part of contractors. Amendments to the Civil False Claims Act enacted by Congress in 1986 make it easier for the Justice Department to prove its case. In addition, the Justice Department and the Inspector Generals of various agencies learned they could justify their work and even make a case for hiring more investigators by obtaining fines and settlements from contractors.

The amount collected in False Claims judgment and settlements has gown from $27 million in 1985 to $257 million in 1990, an increase of almost 1,000 percent.

1985	$ 27 million
1986	54 million
1987	83 million
1988	176 million
1989	225 million
1990	254 million

The Justice Department was so pleased with its efforts that it issued a Press Release dated Monday, November 26, 1990, entitled *"Department of Justice Obtains Civil Fraud Settlements and Judgments of $257 Million in Fiscal 1990."* During the same time period, suspension and debarment of contractors by the DOD rose from 582 in 1985 to 1455 in 1990.

The success of its efforts generated a great deal of favorable publicity due to the public's interest in eliminating fraud, waste, and abuse in Government. As a result, Government auditors have been instructed to look for fraud.

The Office of Inspector Generals of various federal and state agencies has also increased its interest in combatting perceived fraud in construction contracts. At the federal level, this is particularly true of contracts awarded by the Army Corps of Engineers and the Naval Facilities and Engineering Command. At the state level, a great deal of interest has been generated by state DOTS and the Attorney Generals Office.

One primary reason for the increased scrutiny of construction contracts by the federal and state Government is the bid rigging scandals of the 70s and 80s. Those scandals covered a wide range of the industry, including electrical contracts, highway construction contracts, and dredging contracts. Government investigators and prosecutors were alarmed by the pervasiveness of the bid rigging. Many of those investigators and prosecutors concluded that if contractors were willing to commit illegal acts to obtain work, they would also be willing to commit illegal acts while performing the work, including submitting false and/or inflated claims.

2. ***Today's Environment***

Today, many contractors complain that the federal and state Government defends claims by alleging some type of fraud in the claim. Contractors further claim they are being forced to drop legitimate claims involving substantial sums because of some trivial overstatement of a portion of the claim. Suffice it to say, in today's environment both federal and state Government agencies will be searching for any possible overstatement they can claim to be fraud. The DOD Inspector General has even issued a handbook for auditors identifying "fraud indicators."

The best example of today's environment is United States v. Barker, a case that will be discussed in greater detail in Section V. The case involved Lionsgate Corporation, a small family construction business owned by the Barker family. Lionsgate had a $2.4 million contract to construct a quarter mile concrete flood control channel. At the end of the project, Lionsgate filed 74 claims against the Corps of Engineers totalling $2.6 million. With a large part due to bad

blood between Lionsgate and the Corps, the Government retaliated by filing criminal false claim charges against Kenneth Barker. Sixty four counts, involving 104 separate felonies, were alleged to have been committed by Barker, totaling alleged false claims in the amount of $769,078. After a prolonged trial, the jury convicted Barker on only three of the counts amounting to $6,000. Barker appealed his conviction to the Ninth Circuit Court of Appeals. He lost his first appeal, but ultimately the conviction was overturned. It was overturned on the basis that there was insufficient evidence to prove the falsity of the claim beyond a reasonable doubt and insufficient evidence to prove the criminal intent of Barker. There was an incredible amount of expense, time, and worry involved in obtaining justice on the criminal side. This is a frightening case. The Government did not meet the standard of proof required for a criminal conviction. The standards of proof, however, the Government was required the meet, would not have been necessary if the case had been brought as a civil false claim. If it had been brought as a civil case, this court may very well have not overturned the lower court's decision.

This example of data submitted to support a claim being used by the Government as a tool to harass a contractor will undoubtedly be repeated in the future. In an effort to curb waste, fraud, and abuse in Government contracting, statutes created by Congress and the courts' interpretation of those statutes gives great power to the auditors and offices of Inspector Generals of the various agencies, as well as to the Government trial attorneys.

What will the Government look for? Undoubtedly, there are many things. For example, they will look for overstatements and/or mischarges of labor hours, equipment costs, and duplication (double dipping) of costs. When reviewing field and home office overhead cost, they will look for unallowable costs, improper allocations of cost, and statements of cost that are not current. For example, there may be an overhead item of cost that was estimated when the bid was submitted, but was known at the time that a change order proposal was submitted. These are only a few of the errors and misstatements the Government will look for in an effort to negate an otherwise valid claim.

It has always been illegal to commit fraud in connection with federal, state, and local Government contracts. However, Government's view of what constitutes fraud has changed greatly over the years. It wasn't long ago that the strategy used by contractors on claims was to ask for at least double the amount wanted and then negotiate. Today, such a strategy raises the specter of criminal indictment; prosecution; conviction; jail sentence; civil fraud suits seeking double and triple damages plus penalties; interest; attorneys fees and costs, and debarment; suspension; forfeitures of claims, and contract termination. The concept of fraud has also changed from an intentional act to one done with a reckless disregard (i.e. sloppy bookkeeping and/or claim preparation).

3. ***Impact on Kiewit***

The impact of this change on our company has been tremendous. Each element of our contract claims for additional compensation and time extension is being placed under a bright light and examined with a high powered magnifying glass. The size of our seriously disputed claims has risen substantially. We are frequently faced with Government officials either refusing to settle claims that cannot be completely substantiated, or worse yet, raising fraud as both a defense to the claim and a weapon against us.

We cannot ignore valid claims for additional compensation and/or time extensions. Instead, we must be prepared to substantiate with detailed records both entitlement and the dollar amount and/or time extension requested. We must be able to establish our original plan and schedule, identify, and document events giving rise to a claim, and accurately record the impact of such events on our costs and schedule.

It is understandable that most, if not all, construction people hate paperwork. The importance of properly documented claims, however, cannot be overstated. If our documentation is lacking, we will be forced to either reduce claim amounts to only those that are thoroughly supportable by our documentation, or face the drastic penalties as discussed above.

III. Statutes Involved In Government Contract Fraud

1. Truth In Negotiations Act (10 U.S.C. §2306(a))

The cost or pricing data provisions of the Truth In Negotiations Act (TINA) and Federal Acquisition Regulations (FAR) apply to the federal Government contracts. As originally enacted, the Act was designed to require disclosure of cost or pricing data, and contractual remedies for failure to do so. It provides, in part, that a prime or subcontractor shall be required to submit cost or pricing data and shall be required to certify that, to the best of its knowledge and belief, the data is accurate, complete, and current. In its efforts to curb fraud, waste, and abuse, the Government has brought criminal charges and civil fraud suits under other statutes against contractors who engage in defective pricing with fraudulent intent. Those statutes will be discussed later.

Requirements for the Submission of Cost or Pricing Data

The dollar amount threshold for the requirement of submission of cost or pricing data has vacillated in the versions of the Act between an amount exceeding $100,000 and $500,000. The current version of the Act includes provisions for both thresholds depending on the date of the contract and/or modification to the contract.

The Act also requires subcontractors to submit cost or pricing data before the award of subcontracts and before the pricing, change, or modification to a subcontract expected to exceed $100,000 or $500,000 (or such lesser amount as may be prescribed by the head of the agency). Suffice it to say, the contract itself will specify when the submission of the cost or pricing data is required.

It is important to note that under the Court of Claims interpretation of the Act, a prime contractor, although not at fault, may still bear the responsibility, as far as the Government is concerned, for the overstatement of cost by a subcontractor. The Court of Claims reasoned that the Government's contract is with the prime contractor and the Defective Pricing Clause in the prime contract deals with all overstatements, whether or not the inaccurate data was originally furnished by the contractor or subcontractor.

Definition of Cost or Pricing Data

The Act defines cost or pricing data as follows:

> *Cost or pricing data defined. In this section, the term "cost or pricing data " means all facts that, as of the date of agreement on the price of a contract (or the price of a contract modification), a prudent buyer or seller would reasonably expect to affect price negotiations significantly. Such term does not include information that is judgmental, but does include factual information from which a judgment was derived.*

The FAR defines cost or pricing data as follows:

> *"Cost or pricing data " means all facts as of the time of price agreement that prudent buyers and sellers would reasonably expect to affect price negotiations significantly. Cost or pricing data are factual, not judgmental, and are therefore verifiable. While they do not indicate the accuracy of the prospective contractor's judgment about estimated future costs or projections, they do include the data forming the basis for that judgment. Cost or pricing data are more than historical accounting data; they are all the facts that can be reasonably expected to contribute to the soundness of estimates of future costs and to the validity of determinations of costs already incurred. They also include such factors as: (a) vendor quotations; (b) non recurring costs; (c) information on changes in production methods and in production or purchasing volume; (d) data supporting projections of business prospects and objectives and related operations costs; (e) unit cost trends such as those associated with labor efficiency; (1) make or buy decisions; (g) estimated resources to attain business goals; and (h) information on management decisions that could have a significant bearing on costs.*

The question of what is considered fact versus judgment has been raised in a number of contexts. In one case, the contractor failed to disclose six lower quotes it had received from subcontractors. It attempted to justify its failure to disclose on the grounds that the subcontractors were too risky and on that basis it did not use the subcontractor's quotes. The Board of Contract Appeals found that the vender quotations themselves were cost or pricing data and that the contractor's judgmental decision, not to base its proposed price on such quotations, was not cost or pricing data. Therefore, the contractor could have complied with TINA by submitting the same proposed price it did, but disclosing the low quotes and explaining why it was not using them for pricing purposes.

<u>Price Reduction, Interest, and Penalties</u>

If the Government can show that the contractor or subcontractor failed to disclose accurate, complete, and current cost or pricing data, it is entitled to reduce the contract price to the amount it would have been but for the defective pricing. This obviously involves a great deal of speculation, given the environment of uncertainty on how the Government would have dealt with the undisclosed data had it been disclosed. The Government is also entitled to interest in the amount of overpayment from the date of overpayment to the date of repayment.

Finally, as part of the 1986 Defense Authorization Act (PL99-661), a penalty in the amount equal to the overpayment can be assessed against the contractor which knowingly submits defective cost data in addition to the price reduction. In other words, the knowing submission of defective cost or pricing data subjects a contractor to double damages under the Act.

Fraudulent Defective Pricing Indicators

If the Government decides the contractor fraudulently submitted defective pricing data, it will likely seek criminal charges, or even more likely file a civil fraud suit. The DOD Inspector General has identified the following "indicators" as fraudulent defective pricing:

(a) Indications of Falsification or alteration of supporting data.

(b) Failure to update costs or pricing data even though it is known that past activity showed that costs or prices have decreased.

(c) Failure to make complete disclosure of data known to responsible contractor personnel.

(d) Distortion of the overhead accounts or base line information by transferring changes or accounts that have a material impact on Government contracts.

(e) Failure to correct known system deficiencies which lead to defective pricing.

(f) Protracted delay in release of data to the Government to preclude possible price reductions.

(g) Repeated denial by the responsible contractor employees of the existence of historical records that are subsequently found.

2. ***Criminal False Claims Act (18 U.S.C. §287) and Civil False Claims Act (31 U. S. CV 729***

One of the primary tools used by the Government to prevent false claims by contractors on federal, state, or local contracts that are federally-funded in part is the Criminal and Civil False Claims Act.

The Criminal False Claims Act is found in 18 U.S.C. §287. It provides:

Whoever makes or presents to any person or officer in the civil, military, or naval service of 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 to be false, fictitious, or fraudulent, shall be fined not more than $10,000 or imprisoned not more than five years, or both.

Under the Criminal False Claims Act, the Government can obtain a conviction if it can prove beyond a reasonable doubt that the contractor submitted a claim knowing it to be false, fictitious, or fraudulent. The Criminal False Claims Act requires the Government to prove the contractor acted with specific intent. As discussed below, the Civil False Claims Act does not require the Government to prove specific intent.

The Civil False Claims Act has been in existence for many years. In 1986 Congress amended the Act to make it easier for the Government to obtain judgments against contractors. Since the 1986 amendments, the Civil False Claims Act has been used extensively against contractors on a variety of issues ranging from inflated claims for additional compensation to inflated DBE participation.

The Civil False Claims Act is found in 31 U.S.C. §3729. It provides:

> *(a) Any person who - -*
>
> *(1) knowingly presents, or causes to be presented, to an officer or employee of the United States Government . . . a false or fraudulent claim for payment or approval;*
>
> *(2) knowingly makes, uses or causes to be made or used a false record or statement to get a false or fraudulent claim paid or approved by the Government;*
>
> . . .
>
> *is liable to the United States Government for a civil penalty of trot less than $5,000 and not more than $10,000, plus three times the amount of damages which the Government sustains because of the act of that person . . . A person violating this subsection shall also be liable to the United States Government for the costs of a civil action brought to recover why such penalty or damages.*
>
> *(b) For purposes of this section, the terms "knowing " and "knowingly " mean that a person, with respect to information*
>
> *(1) has actual knowledge of the information;*
>
> *(2) acts in deliberate ignorance of the truth or falsity of the information; or*
>
> *(3) acts in reckless disregard of the truth or falsity of the information, and no proof of specific intent to defraud is required.*
>
> *(c) For purpose of this section, "claim" includes any request or demand, whether under a contract or otherwise, for money or property which is made to a contractor, grantee, or other recipient if the United States Government provides any portion of the money or property which is requested or demanded, or if the Government will reimburse such contractor, grantee, or to the recipient for any portion of the money or property which is requested or demanded.*

31 U.S.C. §3731

. . .

> *(d) In any action. . . , the United States shall be required to provide all essential elements of the cause of action, including damages, by a preponderance of the evidence.*

As previously stated, the Civil False Claims Act does not require specific intent. It prohibits the submission of false or fraudulent claims, records, or statements when the contractor knows they are false, or acts in deliberate ignorance or in reckless disregard of their truth or falsity. Any of the following three actions or attitudes are proscribed in submitting a claim and its back up: (1) I know it is false or fraudulent; (2) I don't know if it is true or false, and don't tell me; and (3) I don't know if it is true or false, and I am not going to try to find out. While no guidelines are stated in the statute or in any reported cases, the legislative intent is crystal clear - contractors must make at least a limited inquiry to be reasonably certain they are entitled to the money they seek. Contractors may no longer adopt an "ostrich like" attitude in submitting claims, nor may they inflate claims for the purpose of ultimately negotiating a settlement at the low level to which they think they are actually entitled.

The False Claims Act not only applies to claims submitted to the federal Government, but also to claims submitted to state or local Government grantees of federal funds (e.g., state DOTS on federal aid highway projects and local governments on EPA funded waste water treatment plants). The Act also applies to claims submitted by subcontractors to prime contractors on federally funded projects.

The DOJ typically uses the threat of a criminal prosecution as leverage to obtain a civil settlement. Part of the reason for this strategy is that a criminal conviction can be used to establish. civil liability under the Civil False Claims Act. The 1986 amendments to the False Claims Act expanded the Government's ability to use a criminal conviction to prove civil liabilities. When the final judgment in any criminal proceeding charging fraud or false statements is rendered in favor of the Government, it stops the defendant from denying the essential elements of the civil offense. This happens regardless of whether the final judgment favoring the Government resulted from verdict after trial or a plea of guilty or nolo contendre, and may be true even in instances where the company employees face criminal convictions.

Damages

The 1986 amendments to the Civil False Claims Act substantially increase the damages and penalties recoverable by the Government. Under the amendments, the damages rose from double to triple the amount of the Government's loss. The 1986 amendments also increased the civil penalty from $2,000 per false claim to not less than $5,000 and not more than $10,000 per false claim.

3. *Program Fraud Civil Remedies Act (31 U.S. C. 63801 et. sea.)*

The Program Fraud Civil Remedies Act was enacted by Congress in 1986. It established an administrative procedure for handling false statement and false claim cases under $100,000. From a substantial standpoint, the Program Fraud Civil Remedies Act is essentially the same as the False Claims Act. Under it the Government must show that the contractor submitted a claim that it knew or had reason to know was false, fictitious, or fraudulent. Under the Act, the Government may recover a penalty of not more than $5,000 for each false statement and an assessment in lieu of damages of not more than twice the amount of such claim, or a portion of such claim that is determined to be in violation of the Act. The Act provides for a detailed administrative investigative and review procedure.

4. *Contract Disputes Act (41 U.S.C. $604)*

The Fraudulent Claim provision of the Contract Disputes Act provides as follows:

> *If a contractor is unable to support any part of his claim and it is determined that such inability is attributable to misrepresentation of fact or fraud on the part of the contractor, he shall be liable to the Government for an amount equal to such unsupported part of the claim in addition to all costs to the Government attributable to the cost of reviewing said part of his claim. Liability under this subsection /section] shall be determined within six years of the commission of such misrepresentation of fact or fraud.*

As seen above, if a contractor is unable to support any part of its claim it is liable to the Government for an amount equal to such unsupported part of the claim. In addition, the contractor is liable for all costs the Government attributes to reviewing the unsupported portion of the claim. The Contract Disputes Act applies to Federal Government contracts.

Under Section 605 of the Contract Disputes Act, on claims of more than $50,000 contractors are required to certify that the claim is made in good faith, the supporting data is accurate and complete to the best of its knowledge and belief, and that the amount requested accurately reflects the contract adjustment for which the contractor believes the Government is liable. The Board of Contract Appeals has found statements in a contractor's certification that qualify certification of an item of the claim pending final analysis of the matter negates the certification.

5. *False Statements Act (18 U.S.C. § 1001)*

The False Statements Act is a criminal statute making it illegal to: 1) falsify, conceal, or cover up by any trick, scheme, or device; 2) make a false, fictitious, or fraudulent statement or representation; or 3) make or use a false statement or document. The statute provides for a fine not more than $10,000 and imprisonment of not more than five years.

Several of the Government agencies are also covered by the False Statements Act. For example, under 18 U.S.C. §1020, highway projects are covered. That section makes it a crime

for any person, association, firm, or corporation to knowingly make a false statement, false representation, or false report as to the character, quality, quantity, or cost of the material used or to be used, or of the quantity or quality of the work performed or to be performed, or the cost thereof. 18 U.S. C. § 1020 also provides for a fine of not more than $10,000 or imprisonment of not more than five years, or both.

6. ***Racketeer Influenced and Corrupt Organization Act (RICO) (18 U.S. C. § 1961 et. seq.)***

RICO is both a federal criminal statute authorizing a broad range of criminal penalties including forfeiture, fines, and imprisonment and a civil statute permitting the recovery of damages. In a 1985 decision, the Supreme Court sanctioned the expansive and aggressive use of RICO on civil claims. Since that time, private and Government plaintiffs have used RICO in connection with a garden variety of business and contract frauds. In the Supreme Court case, the court invited Congress to restrict the use of RICO. Congress has thus far ignored the invitation. As a result, RICO continues to be the favorite of business litigators since plaintiffs are entitled to recover trouble damages plus attorneys' fees and costs.

In order to state a RICO claim, a plaintiff must allege the conduct of an enterprise through a pattern of racketeering activity. Thus, a plaintiff must prove: 1) there was an existence of an enterprise; 2) there was a pattern of racketeering activity, meaning there must be at least two predicate acts; and 3) plaintiff must show there was racketeering activity. Fraudulent claims submitted to the government would easily fall within the courts' broad definition of racketeering activity.

7. ***Obstruction of Federal Audit (18 U.S.C. § 1516)***

In 1988, Congress created the new crime of "obstructing a federal audit." The statute provides as follows:

> *(a) Whoever, with intent to deceive or defraud the United States, endeavors to influence, obstruct, or impede a Federal auditor in the performance of official duties relating to a person receiving in excess of $100, 000, directly or indirectly, from the United States in any 1 year period under a contract or subcontract, shall be fined under this title or imprisoned for more than S years, or both.*
>
> *(b) For purposes of this section the term "Federal auditor " means any person employed on a full or part time or contractual basis to perform an audit or a quality assurance inspection for or on behalf of the United States.*

The statute is intended to deter destruction or fabrication of documents or intimidation of contractor employees to prevent a Government auditor from uncovering irregularities. It does not, in any way, increase or enhance the Government's audit rights. The statute covers all Government auditors including those from the Defense Contract Audit Agency (DCAA), Inspector General Offices and the General Accounting Offices (GAO). In addition, the term "federal auditor" includes those performing "quality assurance" inspections.

IV. Government Administrative Penalties and Sanctions

Historically, the Government has relied on the Criminal Justice System to police fraud by its contractors. Thus, in many instances, administrative and contractual actions were postponed until the criminal case was completed. Today, such a postponement is no longer the case. Now, it is not unusual for the Government to take contractual and administrative actions when a contractor is indicted or when a contractor is sued by the Government in a civil fraud case. In this section, the Government's contractual and administrative remedies will be discussed.

1. Suspension and Debarment

The federal Government may suspend or debar contractors from doing business either directly with the Government or contracting with state or local agencies on federally funded projects. Under the suspension and debarment procedures, contractors convicted, or even accused, of offenses involving a lack of integrity may be suspended or debarred for a period of time.

A contractor may be suspended for up to 18 months while an investigation is under way. Once an indictment or civil suit is filed, the contractor can remain suspended until completion of all legal proceedings. Suspension is an intro measure based on adequate evidence of fraud, or some other act indicating a lack of business integrity.

A contractor can be debarred for conviction of , or civil judgment for, an offense relating to obtaining or performing a public contract or subcontract, or any other offense reflecting a serious lack of business integrity. Debarment may also be imposed for willful or repeated failure to perform prior government contracts, or for violations of various statutes.

Debarment and suspension are Government wide, including contracts with recipients of federal funds. Debarment and suspension includes all the divisions of a company, unless the suspending or debarring official limits the scope to specific divisions. Debarment and suspension also may include affiliates of a company if it is specifically named and given notice of an opportunity to respond to the charges.

2. Nonresponsibility Determination

Federal, state, and local contracts typically provide that awards may be made only to responsible contractors. One element of responsibility is a satisfactory record of integrity in business ethics. A federal Government contracting officer or a state or local Government official has wide discretion in determining whether or not a contractor is responsible. Typically in such circumstances, a finding of nonresponsibility will only be overturned by a court if it finds that the officials acted arbitrarily or capriciously. An illustration of this difficulty is Schiavone Construction Company (Schiavone). After Schiavone executives were indicted by the Bronx District Attorney, the New York Department of Transportation refused to consider bids submitted by Schiavone. The New York court upheld the DOT's finding of nonresponsibility, concluding that the indictment was sufficient reason for the finding of nonresponsibility.

3. ***Suspension of Contract Payments***

When a contractor is under investigation for illegal activity regarding an existing contract, the Government may suspend contract payments pending the outcome of the investigation.

4. ***Termination for _Default***

If the Government finds that a contractor has submitted a false claim or statement, it may terminate the contract for default. In such an instance no criminal conviction is necessary. Instead, the Government need only establish facts justifying the termination similar to those necessary to prove nonresponsibility.

5. ***Forfeiture or Fraudulent Claims***

Under 28 U.S.C. §2514, a claim against the United States is forfeited to the United States by any person who corruptly practices or attempts to practice any fraud against the United States in the proof, statement, establishment, or allowance of the claim. This tool is being used with increasing frequency by the Government. This statute applies only to claims brought before the United States Claims Court, but the results can be quite harsh. Even though only a small part of a claim is tainted by fraud, the entire amount is forfeited.

6. ***Refusal to Decide Claims***

The Contract Dispute Act includes a provision for decision of claims by the contracting officer (41 U.S.C. §605). Under that section all claims by the contractor against the Government are to be decided by the contracting officer. However, the section specifically does not authorize any agency head to settle, compromise, pay, or otherwise adjust any claim involving fraud. As a result, it is not unusual for the government to move to dismiss claims based on lack of jurisdiction when suit is filed in the Claims Court or an appeal is taken to a Board of Contract Appeals. Even though there are legal arguments that can be made by the contractor, the Government's Motion to Dismiss places the issue of fraud as a hurdle the contractor must get over before the claim is considered on its merits.

V. What the Government Looks For In Audits of Claims

When the Government audits the statement of cost submitted by a contractor in support of a claim for an equitable adjustment, it seeks to determine the allowability, allocability, and reasonableness of the cost claim. On federal contracts, the Federal Acquisition Regulations (FAR) specifically provide that certain overhead costs are not allowable. Those costs include bad debts, contributions and donations, entertainment, fines and penalties, interest and finance cost, lobbying costs, losses on other contracts, organization costs, and cost in defensive fraud proceedings.

The accuracy of claim calculations depends directly on the accuracy of the company's job cost records. The accuracy of the job costs records depends in part on the reliability of the company's internal accounting control procedures. When the Government audits a claim it looks not only at the costs, but also at the company's internal accounting control procedures and identifies deficiencies that the auditors believe could adversely affect the company's ability to record, summarize, and report financial data. The auditors seek to determine whether the company's accounting control procedures ensure that:

> The breakdown of costs within the accounting system is adequate for cost determination purposes.
>
> Specific cost elements are afforded consistent treatment regarding Government and non Government cost objectives.
>
> Allowable and unallowable costs are routinely identified and segregated in the accounting system.
>
> Adequate source documentation supports all costs.
>
> Assets are safeguarded against loss or unauthorized use or disposition.
>
> Defective Pricing and False Claims
>
> All accounting data are accurate, reliable, and traceable to underlying source documentation.
>
> Contract terms and conditions are known by appropriate personnel and the effects of contract terms and conditions are properly reflected in the accounting records.

1. Case Studies

1. United States v. White, 765 F.2d 1469 (11th. Cir. 1985)

Misallocation of costs can occur either purposely, or more frequently, by sloppy documentation and bookkeeping. An example of the purposeful misallocation is found in United States v. White. In that case four construction contracts were awarded to Mayfair Construction Co. (Mayfair) at the Kennedy Space Center. Mayfair entered into several subcontracts and joint

venture agreements with a gentleman by the name of Phillip Akwa (Akwa), Capitol Communication Corporation (Capitol). In essence, these agreements provided that Akwa would have the authority, subject to a limited review, to bid and perform on the behalf of Mayfair and would share in the profit or loss of any such project.

Before submitting Mayfair's bid to National Aeronautics & Space Administration (NASA), Akwa accepted subcontracting bids from various concerns including New World Construction Company (New World). New World's bid was for steel erection and related tasks and assumed that another subcontractor, Industrial Steel Corporation (Industrial), would supply aluminum and steel for the construction.

After Mayfair's bid was accepted by NASA, Akwa set up different arrangements with the subcontractors. Akwa modified the arrangement to make Industrial a second tier subcontractor under New World rather than a first tier subcontractor under Mayfair. As a result, New World was financially responsible for its own and Industrial's costs overruns.

The NASA contracts required Mayfair's prime contractor to perform 20% of the actual labor. Mayfair represented it would perform the direct labor involved in erecting the steel. In reality, Mayfair executed a separate subcontract agreement with New World which required that entity to perform the steel erection. In addition, Mayfair represented to NASA that New World would be providing the steel fabrication, which in fact was contracted to be provided by Industrial.

Once work began, NASA found it necessary to issue a number of change orders -- a total of over 500 before the projects were completed. Mayfair submitted claims for equitable adjustments described inks cover letters as "cost proposals." The documents supporting these claims containing "Detailed Cost Breakdowns" were entitled "Estimate Summary For Change Orders." The "Detailed Cost Breakdown" specified the number of labor hours devoted to each change order and the additional charges for equipment and rental expenses.

During the negotiations of some of the change orders, Akwa represented that the itemized expenses were not estimates but "hard dollar hours" and actual costs. Each cost breakdown contained a "Field Support" category, which was uniformly billed at 20 percent of the direct labor costs. The Government's evidence showed that these field support charges were intended to surreptitiously cover New World's overhead and profit. This false entry, which was listed as a cost of Mayfair, was necessitated by the form of the cost proposal submitted to NASA representing that Mayfair, not New World, was providing the direct labor. The procedure was that New World would submit its change order draft to Mayfair. Akwa then adopted New World's labor and equipment charges, deleted New World's overhead and profit costs, and substituted markups of 30 percent for Mayfair's overhead and profit, then added a 20 percent field support charge. Akwa then submitted the rewritten proposal to NASA. In essence, Mayfair sought to collect double overhead by adding in a field support charge to cover New World's overhead for direct labor which was falsely being attributed to Mayfair.

Overinflated Labor and Equipment Charges

Two change orders involved work on a structure in which the space shuttle is cleaned and its radio equipment calibrated after it returns from a space flight. Work began in January and was substantially completed by December 1977. The two cost proposals submitted involved change work on the structure. In August 1977, it became apparent that the change work needed to be performed and by mid November it was completed. On January 20, 1978, Mayfair submitted retrospective cost proposals on the two changes. On one of the changes Mayfair indicated an expenditure of 887 labor hours. On the second change, it claimed 3,373 labor hours. Mayfair and New World's timecards showed that, at most, the first change took 470 and at most the second change took 2,373 hours.

With regard to equipment on the two change orders, Mayfair claimed a pickup truck was used 675 hours and claimed 540 hours for use of a crane and wages to the crane operator. At the trial, Mayfair's job superintendent testified that he had no pickup truck on the site. In addition, the certified payroll records showed that the crane operator worked only 395 hours during the entire period of the change work and that the crane was rarely used on those change order jobs.

For another change order, Mayfair claimed 610 labor hours. After the cost proposals were submitted, NASA told Mayfair's engineer that the costs were inflated. One of the may fair representatives indicated to another Mayfair representative that the submission was about "10 times" what the change involved. Mayfair then prepared a new detailed cost breakdown which was submitted to NASA. Where the original submission had requested almost $19,000, the second request asked for approximately $8,000. Another change order that was subjected to the Government's scrutiny involved a cost proposal claiming 629 labor hours. The evidence at trial showed that the job was not difficult, and that only two iron workers worked three to four days on the changed work. Timecards showed that total labor on the entire project during the relevant time period amounted to only 540 hours, 89 hours fewer than claimed for the changed work.

Mayfair submitted a claim for extended overhead and impact costs resulting from a loss of efficiency. In the claim, Mayfair allocated 12,457 impact hours specially attributable to ironworker labor, and separately allocated more than 3,000 supervisor and foremen hours. In fact, the 12,457 hours included all categories of work, including foremen and supervisors. As a result, Mayfair double charged NASA for the 3,000 additional supervisor and foremen hours.

The White case presents an extreme example of overstated costs. Perhaps Akwa and representatives of New World who prepared the cost proposals did so with a mind that NASA would negotiate the labor hours and equipment costs. Instead of negotiating, the Government filed criminal false claims and false statements against the individuals and the companies. In addition, the contracting officer for NASA determined that Mayfair was nonresponsible because of lack of integrity. This finding was reached May 1978, after the Assistant United States Attorney authorized the Federal Bureau of Investigation (FBI) to conduct a preliminary investigation of Mayfair and the others. That FBI investigation was over the alleged falsification of certificates of competency for welders and weld inspectors who were used on the projects.

Lessons to be learned from the White case are:

Make sure that labor hours requested for change work are supported by timecards and daily reports.

Specifically identify on timecards and daily reports when work is being done or changed, or when additional work is being done and establish a separate cost code for such work.

Specifically identify estimates or labor hours when such estimates are being used.

Do not charge equipment for the entire time period when such equipment is being used for unchanged work as well as changed work.

Make sure that foremen and supervisory personnel are not double charged by including them in direct labor as well as field overhead.

Do not mislabel costs.

2. ***United States v. Barker, 942 F 2d 585 (9th. Cir. 1991)***

In 1985, Lionsgate Corporation (Lionsgate), a construction firm owned by Kenneth Barker, wife and sons, bid on a United States Army Corps of Engineers (Corps) project. After Lionsgate was awarded the project and Barker had inspected the site, he discovered substantial changes had occurred between the time of his bid and the award. He immediately notified the Corps that the changes in the site required changes in the contract. A dispute arose which led to Lionsgate beginning work on the project in an atmosphere of animosity. Relations with the Corps did not improve. As a result, Barker made an end run around the local Corps officials, which made them even more upset. Lionsgate filed 76 claims for additional compensation. The Corps responded by alleging false claims against Barker and convincing the DOJ to indict him on 64 counts of making false claims against the Government. He was alleged to have: falsely claimed rates for equipment; falsely inflated costs of lease vehicles; falsely claimed for equipment which was not used the number of hours claimed; falsely claimed for equipment on standby when it was not on standby; falsely charged time for the same vehicles and equipment; falsely inflated costs for employees; falsely claimed overtime paid to employees who were not paid; falsely claimed twice for the same employees; falsely claimed for a person not employed on the project; falsely claimed for standby time when employees were not standing by; and falsely double billed overhead. The total of the alleged false claims was $769,078.

At the end of a four-day trial, the jury found Barker guilty on three counts, was unable to reach a verdict on twenty-two counts, and acquitted him on the remaining counts. The three counts amounted to approximately $6,000. Although this was less than one percent of the claims the Government said were false, and only three one hundredths of one percent of the $2.6 million in change orders submitted on the project, Barker was found guilty of having committed multiple felonies.

The Government's principle witness was a civil engineer who had no formal training in accounting. He had worked for seven years in the contract administration section of the Corps as a "claims analyst."

The first count on which Barker was convicted involved a claim made by Barker that he and his sons had worked on Sunday, May 25,1990. The Government introduced documentary evidence which it contended proved they had not worked on that day. The first document introduced by the Government was the Daily Construction Quality Control Report for that date. The document was prepared by Barker's son, Wayne, and showed that one supervisor and three pickup trucks had been at work on that date. The second document was the Daily Job Report for May 24, 25, and 26. The report showed Wayne Barker as "supervisor." It also showed Kenneth Barker and his two sons, Wayne and Paul, as "employees" all three days. The initials K.B., W.C.B., and P.B., and the number 8 x 3 all appeared on the sheet. The third document was the Daily Job Report for Tuesday, May 27, 1990. Under changes, it had a note reading: "K.B., W.C.B., P.R.B. survey Sat. - Mon., W.C.B. recalculates elev. on Sunday due to directive from Corps about materials." On the following page of the Tuesday report under the space for Additional Comments, it was written "Extra Work... surveying over weekend W.C.B., P.R.B., K.B." On the basis of those three documents, the Government's engineer testified that all three Barkers had worked only Saturday and Monday.

For the other two counts the Government's engineer testified that in each of the documents there were charges under "labor" for the time of the general manager that were "improperly" there. Each was "a duplicate charge." The engineer reached this conclusion because according to Lionsgate's accountant, the general manager is always in the overhead. The evidence reflected that Ken Barker's salary was divided between "direct," "indirect," and "home office." In cross examination, the Government's engineer was unable to identify whether the amount he said was double billed was included in the amount that had been reflected as direct costs and not included in overhead. He also was unable to determine whether the accountant had spoken of home office overhead or job site overhead.

Although the district court and court of appeals expressed doubt as to the sufficiency of the evidence upon which these convictions were based, both the trial court and the appellate panel left the convictions intact because the evidence was viewed as "open to an alternative interpretation" and "not so unreliable as to cause [the court] to depart from the rule that determining creditability of witnesses and assessing conflicting evidence as a matter for the jury." Nonetheless, the trial judge expressed shock and dismay at the convictions as did Judge Noonan of the Court of Appeals who, in a sharply worded dissent, felt compelled to attempt to "right the wrong done by the judicial system" to Barker. Judge Noonan's efforts apparently paid off because upon rehearing, the Court of Appeals reversed the conviction on the basis that the standard of proof required for a criminal conviction had not been meet. The reversal of this case gives us little comfort. The Government could, for the most part, obtain the same results by filing a civil action.

Besides being a sobering example of a claim gone bad, the Barker case indicates that the Government is moving away from the "partnering" approach to construction contracting. More disturbing is the Corps' desire and initial success at applying a strict standard of absolute liability regardless of intent. Under the court's theory, if a contractor submits supporting data for a claim,

and that supporting data is not accurate, then the claim is criminally false -- that the very existence of inaccuracy establishes knowledge and therefore the intent to falsify the claim. This approach, while unsuccessful in the Barker case, is being utilized by the Government.

Lessons learned by the Barker case:

> Daily reports must accurately reflect the number and names of people working on the project.
>
> Daily reports must accurately reflect the equipment working on the project.
>
> Daily reports must accurately reflect the items of work (cost codes) being performed by the labor and equipment.
>
> Be careful not to allocate foremen and supervisors to both direct costs and field overhead in a claim submission.
>
> A very small error or overstatement of costs can lead to a very big problem.

3. Aerodex, Inc., 469 F.2d 1003 (5th Cir. 1972)

Aerodex, Inc. contracted to sell certain aircraft parts to the Navy Department in 1962. Included in the sale contract were 300 master rod bearings. The contract called for only new, unused parts conforming to specific serial numbers and requirements. Aerodex delivered reworked, non conforming bearings that did not meet contract specifications. When the Navy discovered that the bearings were not the ones contracted for, it removed those it had installed in aircraft engines. This retro fit operation cost the Navy $160,919.18.

Subsequently, the Navy brought an action for false claims against Aerodex. As a defense, Aerodex asserted that it did not know that bearings labeled 117971 were not interchangeable for those called for in the contract. Evidence showed that the difference between the bearings delivered and those called for in the contract was barely distinguishable. However, failure of the bearings to perform in their intended use and capacity could result in total engine failure to an aircraft.

Defendants asserted that they in fact believed that the reworked bearings were interchangeable for those called for in the contract. They also felt that they could have easily requested permission from the Navy to deliver the substituted parts, or at least, could have disclosed to the Navy the manner in which they felt they could comply with the contract. The court felt that the failure to inform the Navy indicated nothing less than the intention to deceive.

The court decided that to show a violation of the False Claims Act, the evidence must demonstrate guilty knowledge of a purpose on the part of the defendant to cheat the government. The court felt that Aerodex's actions were consistent with this standard of knowledge. The mere fact that the items supplied to the United States under the contract are as good as the ones contracted for does not relieve suppliers of liability under the False Claims Act.

If it can be shown that these suppliers attempted to deceive a government agency, their liability will be imposed. In this case, deliberate mislabeling of aircraft engine bearings, coupled with the fact that parts delivered to the United States Government Agency did not actually meet specifications of the contract, compelled a finding of liability under the False Claims Act. In addition, the court found that the inspection clause of the contract, calling for a 100% final inspection, did not insulate the defendants from liability for fraud.

VI. Guidelines For Preparing A Claim.

1. Overview

Requests for additional compensation on federal Government contracts and state and local Government contracts aided with Federal Grant Funds are governed by the Federal Acquisition Regulation (FAR) Part 31 -- "Contract Cost Principles and Procedures" (referred to as cost principles). Some state and local Governments have adopted their own set of cost principles. Requests for additional compensation on state DOT highway and bridge construction projects are typically governed by the Force Account Provisions in the contract.

In submitting a request for additional compensation, we must first demonstrate the baseline of understanding upon which we relied in preparing our bid. Then we must identify the variance from that baseline that occurred during construction and prove the impact of the variance on our costs, schedule, and plan of operations. This process is discussed in detail in the Peter Kiewit & Sons, Inc.'s *Contract Administration and Claims Avoidance Workshop* manual.

This section will specifically address cost principles included in the FAR and state and local contracts. It is designed to help you prepare requests for additional compensation that seek recovery of all allowable and allocable costs while not subjecting the company to False Claims or Defective Pricing accusations. Keep in mind such accusations generally can be avoided by honesty, consistency, reasonableness, and thoroughness.

Our companies have adopted standard practices regarding common claimable cost. This section explains how the company standard costs are computed. Managers are expected to assure that such costs are computed in that manner and use the language provided in this section to explain the company's standard costs whenever they are used. Any variations from the standard cost must be documented and explained.

Claims for additional compensation in excess of $50,000 on federal Government contracts must be certified. This is required by the Contract Disputes Act. The certification states that the claim is made in good faith, the supporting data is accurate and complete to the best of the contractor's knowledge and belief, and the amount requested accurately reflects the contract adjustment for which the contractor believes the Government is liable. Subcontractor claims in excess of $50,000 must also be certified by the contractor. Certification plays a vital role in the contractor's potential liability for submitting a fraudulent claim.

2. Important Guidelines

The contract, and any cost principles referenced in the contract, is the law. You must be thoroughly familiar with contract clauses on changes, extra work, delays, suspension of work, differing site conditions, change order accounting, force account, submission of claims, etc.

Consistency in estimating, recording, and reporting costs is a key point. The bid estimate, budget, cost report, and claim or request for additional compensation should be consistent. Any inconsistencies must be documented and explained.

To the extent possible, use actual costs rather than estimated costs.

Describe in detail the source documents from which the costs were obtained and how the costs were calculated.

When asked to forward price change orders, be able to support amounts requested with cost data on similar work from prior projects.

To the extent possible, segregate the costs claimed from costs incurred to perform the original contract work. When claimed costs are grouped with original contract costs, explain why they could not be segregated.

Make certain costs have been properly charged.

Be able to reconcile the claim costs to the cost report, and the cost report to the daily report; the daily report to the timecard and foreman diary if applicable.

Make sure the costs claimed are allowable under the cost principles and are reasonable.

Avoid changing original entry documents. If changes are made, explain why (e.g., cost codes on time cards).

Check mathematical calculations. Errors in math, particularly those that increase the amount of the claim, destroy credibility.

Avoid duplication. When the same item is included in two separate claims make that fact known and explain why it is necessary.

Keep in mind you are certifying that you believe you are legally entitled to the amount claimed. It cannot be an artificially high number from which you intend to negotiate.

Once a certified claim is submitted, you cannot say, "Oops, we goofed." A false claim cannot be taken back. The Government looks to see if the contractor had actual knowledge, or acted in deliberate ignorance of the truth or acted in careless disregard of the truth of the information in the claim. Thus, it is important not to make careless mistakes.

Keep in mind your claim will be audited. Make sure cost records are accurate and reliable.

If you submit a claim that you later find has errors, advise the PKS legal department immediately.

VII. *Tips In Reviewing A Claim*

When a Request for Additional Compensation or a claim is submitted, we must demonstrate both entitlement -- that we are entitled to additional compensation, and the quantification of the claim -- the amount of additional compensation to which we are entitled.

These tips are for managers reviewing a claim before final submission. They are designed to ensure we have shown both entitlement and quantification in our request or claim.

1. Have we established our baseline of understanding based on contract representations and implied duties of the owner?

2. Have we established reliance on that baseline of understanding when we prepared our bid estimate? Do our bid documents support our reliance?

3. Review the portion of the claim describing the actual conditions encountered during construction.

    a. Were the conditions we encountered different from those we should have anticipated from our baseline of understanding?

    b. Did we document the actual conditions encountered?

    c. Did we give timely notice to the owner in accordance with the contract provisions?

4. Does the claim clearly show the impact of the actual conditions encountered on our plan of operations, schedule, and cost of performing the work?

5. Is the legal basis for the claim clearly stated?

    a. Does the claim identify the remedy granting clause in the contract? (e.g., Differing Site Conditions, Changes.)

    b. If not, does the claim identify the noncontractual legal basis for the claim?

6. For federal contracts subject to Federal (FAR) Part 31 --"Contract Cost Principles and Procedures," make sure costs claimed are allowable. Such costs must meet <u>all</u> of the following tests:

    a. reasonableness;

    b. allocability;

        in accordance with generally accepted accounting principles and cost accounting standards if applicable; and

not limited or excluded by the terms of the contract or the cost principles.

7. Are any of the costs claimed specifically unallowable either under the terms of the contract or applicable cost principles?

8. Are any of the costs claimed or included in overhead specifically unallowable under the applicable cost principles? (Examples of unallowable costs on Federal contracts covered by FAR include bad debts, contingencies, contributions or donations, entertainment costs, fines and penalties, lobbying costs, losses on other contracts, and organization.)

Labor Costs

Most requests for additional compensation and claims include increased labor costs.

1. Labor overruns --

   a. Is the claimed overrun of labor hours supported by our records?

   b. Is the amount of estimated labor hours reflected in the bid estimate and any estimates for forwarded priced changes?

   c. Is the amount of actual labor hours reflected in the payroll records including timecards?

   d. Does the request or claim show that the amount of the claimed overrun was caused by the claimed event?

   e. Have the increased labor hours been segregated by date and craft?

2. Wage rates --

   a. Have the actual rates been used for each wage craft?

   b. If average wage rates have been used, is there anything in the contract requiring actual wage rates? Have we explained our use of the average wage rate?

3. Labor Add-ons --

   a. Have the correct composite add-ons for payroll taxes, insurance, and merit shop medical benefits rates been included in the claim?

   b. Does the health and welfare costs claimed accurately reflect the negotiated rates for each craft in effect at the time the work was done?

   c. Are any of the labor add-ons duplicated elsewhere in the request or claim?

4. Escalation of the wage rate --

   a. Is the anticipated wage rate supportable by the estimate?

   b. Is the actual wage rate supported by the payroll records?

   c. Is there any duplication of the wage rate escalation costs and the amount claimed for labor overrun?

   d. If the claim involves several different wage periods, is the escalation calculation segregated by time period?

5. Loss of Productivity --

   a. Is the anticipated productivity stated and supported?

   b. Is the actual productivity supported by our time cards?

   c. Have we shown that the difference between anticipated and actual productivity was caused by the claimed event?

<u>Equipment Costs</u>

Increased equipment costs may include equipment used for an extended period of time, equipment idle because of delays, and additional equipment brought to the project to perform extra work or accelerate the performance. The equipment costs claimed should be analyzed to determine:

1. Is the rate used consistent with the rate specified with the contract (e.g, rental rate blue book was specified in the contract).

2. Have any adjustments to the rate been made if required by the contract?

3. If the claim is based on the equipment being on the project for an extended period of time, is the claimed estimated equipment hours, weeks, or months, supported by our bid estimate?

4. Is the actual equipment used supported by the timecards?

5. Where additional equipment was brought to the project, does the claim justify the reasons the additional equipment was necessary?

6. Where rates are based on the blue book or other guides, have any assumptions, interpretations, or adjustments to the published rates not been explained? Where rates are based on company internal rental rates, has the basis of the determination of those rates been explained?

7. Where rates are based on guides, is there any duplication elsewhere in the claim or for work not covered by the claim (e.g., blue book rates including mechanic's time)?

8. Are the claimed equipment hours consistent with the internal rental hours? If not, has that fact been disclosed? Has an explanation for the reason been given?

Small Tools and Supplies (STS)

1. Is there anything in the contract prohibiting separate recovery for STS?

2. If an amount is being claimed for STS, is there any contract provision that requires STS be included in overhead or some other cost item?

3. Has the amount of anticipated STS been subtracted from the total amount of STS?

4. Is there support for the position that the increased STS was caused by the claimed event?

5. Is the amount being claimed or STS supported by actual costs records?

Increased Material Costs

There are a variety of increased material costs that may be included in a request for additional compensation or a claim. Those costs include additional materials to perform extra work, material escalation costs when materials are purchased at a later period of time than anticipated, additional transportation costs, additional material handling and storage costs, and additional costs for material deterioration. In reviewing claims for additional material costs, analyze the following:

1. For claims including additional materials, have we substantiated that the additional materials were made necessary as a result of the claimed event?

2. If the claim includes additional material quantities, is the estimated material quantity substantiated by our estimate and is the actual material quantity substantiated by our cost records?

3. If the claim includes material escalation costs, is there a contract clause covering such; and if so, is the amount requested in the claim consistent with the clause?

4. If the claim includes material escalation costs, have we established that we timely ordered materials based on the facts known at the time?

5. Has the amount of material costs been adjusted for trade discounts, refunds, rebates, allowances, and cash discounts?

On Site Overhead

1. Does the claim disclose the basis for the determination of the on site overhead rate used?

2. Is the rate or amount claimed consistent with the cost report, and if not, is there an adequate explanation of the differences?

3. If the claim includes increases in the rate of on site overhead, are those increases adequately explained?

4. If the claim includes increases of on site overhead for an extended period of time, is the rate used consistent with the time period for which the extension is claimed?

5. Is the rate of on site overhead claimed consistent with the rate of on site overhead in the bid estimate; and if not, is there an explanation for the differences?

Home Office Overhead (General Administrative Expenses)

1. Is the rate used in the claim consistent with the rate audited by Coopers & Lybrand?

2. Is the rate used in the claim consistent with the rate published in the Heavy Estimating Manual? Note: We are requested to use actual facts not estimates.

3. Is the amount of overhead claimed consistent with any limitations on overhead claims in the contract?

4. If extended home office overhead is claimed, is there any duplication with other claims involving markups for home office overhead on specific charges for items normally changed to overhead.

5. If the claim involves extended home office overhead, ha re we demonstrated that the costs were incurred as a result of the delay and/or disruptions for which the owner is responsible?

6. If the claim involves extended overhead, ___ that the delay and/ or disruption caused it, and did we undertake _____ performance of other work to mitigate the damages?

7. If the claim involves extended home office overhead, have we shown that we reserved our rights to bring the claim?

Bond

1. Is the amount of the adjustment for increased bond cost included in the claim consistent with any limitations and contract provisions?

2. Have you contacted Midwest Agencies to verify the rate in claim?

3. Does the claim reflect the fact that the bond rate may have declined as a result of increased claims and change orders?

4. Is the rate contained in the claim consistent with the rate in the bid estimate? If not, has the inconsistency been disclosed and explained?

Schedule

If we are making a claim for delay, extended overhead, lost efficiency, etc., are we using an accurate schedule to depict the effect of the delay on our work.

> Is the schedule that we depict as "as bid" a document that was prepared at the time of bid. If not, did we disclose when and on what basis it was prepared.
>
> Is our "as built" schedule supported by contemporary documents; i.e., timecards, receiver's reports, diaries, etc.
>
> Is our time impact analysis made on the basis of a current, fully up dated schedule prepared at the time of the impact.

Profit (Margin)

1. Does the claim describe the basis for the margin rate?

2. Is the profit percentage consistent with any contract provision limiting the percentage of profit? If not, is there an explanation of the difference?

3. Is the profit percentage fair and reasonable?

VIII. Guidelines For Proper Disclosure

This section provides proper disclosure statements for each cost category. The disclosure statements are in bold text below. Consider including this disclosure in the claim documents. Claim preparers and responsible managers must address whether the disclosure is consistent with the claimed costs. Comments have been provided to assist in understanding the elements of the costs and common pitfalls in preparing claims.

1. Labor Add-ons

Labor add-ons are comprised of three factors: Payroll Taxes, Insurance, and Union Fringe Benefits or Merit Shop Medical Benefit costs. A separate disclosure should be made for each component.

1. Payroll Taxes --

A "composite" or average rate is included for each labor dollar incurred without regard to wage limitations. This composite rate is comprised of social security taxes, federal and state unemployment insurance, and state disability tax factor rates based on either the appropriate rate or estimated rates for the company and its affiliated companies operating in this particular state. This rate was established at the time the contract was awarded.

2. Insurance --

A "composite" or average rate is included for each labor dollar incurred. This rate was developed to ensure that sufficient costs will be charged to the projects covering current costs and estimated future insurance claims. This rate includes factors for Workers' Compensation, General Liability, Auto Liability, and Group Medical, Life and Disability for staff personnel. This rate is an estimate because of the uncertainty of knowing what future insurance claims will be, and because the corporation is self insured in many cases.

3. Fringe Benefits --

Fringe Benefits costs are based on negotiated rates dictated by collective bargaining agreements for each craft. These costs represent cash paid to the applicable union plan administrators.

4. Merit Shop Medical Benefits --

A "composite" or average rate is included for each labor hour incurred. This rate was developed to ensure that sufficient costs will be charged to projects covering current insurance costs and estimated future insurance claims. This rate covers the medical program for merit shop craft personnel. This rate is an estimate because of the uncertainty of knowing what future insurance claims will be, and because the corporation is self insured in many cases.

COMMENTS:

For additional information, contact Payroll Reporting (Tim Vavra) in the home office regarding payroll taxes and fringe benefits. Contact Risk Management (Bob Lembke) regarding insurance.

2. Bond Rates

The rates included in the claim for performance and payment bonds are industry standard rates based on the "Surety Association of America" filed rates. The bonds provided for the project were provided by a wholly owned affiliate or Aetna Casualty & Surtey Company with reinsurance by the affiliate.

COMMENTS:

The bond rate on the original contract and all related claims and change orders should be considered as a single contract when determining the appropriate bond rate. Therefore, as the contract amount is increased by claims and change orders, the rates may incrementally decline. Managers should take this into consideration when selecting the appropriate rate for the claim.

If the bid estimate was based on a rate inconsistent with the rate subsequently charged in the cost report, managers should disclose this fact and document the reason in the files.

If there are any questions on which rate to use contact Risk Management (Bob Lembke)

3. General & Administrative Rate

The General and Administrative rate used in this claim was prepared in conformity with Federal Acquisition Regulation Subpart 31.2, and has been audited by Coopers & Lybrand. Certain allocations of corporate costs have been made in establishing this rate. This rate is based on expenses incurred for the year ending December XX, 199X (previous year from work performed and may be multiple years if a multiple year job).

COMMENTS:

Some owners may challenge the company's use of the G&A rate, which is a composite for all our construction companies. This rate may or may not represent the G&A rate for a specific subsidiary company. It also will not represent the rate for a joint venture which some owners believe should be a blend of the Partner's individual rates. The company's position is that all general and administrative support is provided by the managing partner. The managing partner's G&A rate should be the appropriate rate.

4. <u>*Change Orders*</u>

COMMENTS:

It is very important not to duplicate a request for remuneration by including costs in the claim that have been previously included in change orders and/ or previous claims. An analysis should be made of the cost report items included in the current claim to identify any costs previously claimed in change orders or claims.

The owner's representative or auditor may request the cost report for the job. Be prepared to explain that the costs in the approved change older classification (Department 7000) do not include the teal change order impact. **A CHANGE ORDER is a CLAIM and needs to be prepared as accurately as a claim.**

5. <u>*Equipment Rental Rates*</u>

There are several potential equipment rates. The claim preparer must be sure to use the rate specified in the contract. If no rate is specified, the claim preparer must make sure the rate in the claim is consistent with the rate used in the bid estimate and cost reports. One of the following disclosures should be included in the claim depending on the rate used in the claim.

(Blue Book). <u>Rental Rate Blue Book</u>, published by Dataquest, is the basis for the equipment rates in this claim. The rates are guidelines that parallel the amounts an equipment owner should charge to recover equipment related costs on a single shift basis. The rates do not include a credit for salvage value. The rates have three categories: ownership costs, operating costs, and adjustments. (Disclose any assumptions, interpretations or adjustments made to the rates.)

(Cost Reference Guide for Construction Equipment). <u>The Cost Reference Guide for Construction Equipment</u>, published by the Associated General Contractors, is the basis for the equipment rates in this claim. The rates are intended to reflect internal ownership and operating costs under normal job conditions. (Disclose any assumptions, interpretations or adjustments made to the rates.)

(Company Rates). The company internal rental rates of charge are the basis for the equipment rates in this claim. These rates may or may not reflect the actual cost of a piece of equipment. These rates are based on a single shift operation under normal job conditions. This may not accurately reflect what was experienced for a piece or fleet of equipment utilized on this project.

COMMENTS:

Care must be taken when using rates so that duplication of covered costs does not occur. For instance, if Blue Book operating rates are used, mechanics' time should not be included elsewhere in the claim. The claim preparer should completely understand the factors included in the rates.

For additional information, contact Equipment Records (Kevin Renner) in the home office.

6. ***Equipment Rental Hours***

Equipment rental hours shown in the cost reports are an internal reporting practice to charge the appropriate jobs with a factor to recognize the use of the equipment. This may not accurately reflect the experience for a piece of equipment utilized on this project. The method normally used on this job was (choose the correct one or identify your job's practice) a minimum of 40 hours each week, one hour for each hour worked up to 40 hours plus a half hour for each additional hour worked. That statement must be consistent with the estimate. The claim was prepared on a basis of (explain the basis for the claim. Remember the method must be current, accurate, and complete.)

COMMENTS:

Be prepared to provide substantiating documentation if the equipment utilization included in the claim varies from the reported equipment rental hours. An owner representative may assume that the job records accurately reflect the equipment use unless accurate documentation of use is available.

7. ***Margin Percent***

The claim should disclose the basis for the margin assumed in the claim. This will vary in the individual claims.

COMMENTS:

Margin should be recognized based on the risk being taken (forward pricing) or already taken on the project (this may already be reflected in the cost).

Managers should address the consistency of the margin between the bid and claim.

8. ***On site Overhead Rates***

The claim should disclose the basis for the on site overhead rate used in the claim. This will ___ by the individual contract.

COMMENTS:

The methodology used to derive the rate must be adequately documented and available ___ the owner's representative.

Be prepared to provide substantiating documentation.

Develop a daily or hourly rate for on site overhead. Document explanations if the rate or amount is not consistent with the cost report.

9. ***Cash Discounts On Vendor Invoices***

Cash discounts included in this claim have been computed using a company wide rate of cash discounts earned based on total payments. This rate has been applied against total direct cost excluding labor, labor add-ons, subcontracts, and equipment rental, to arrive at an approximation of the discounts earned.

COMMENTS:

Company policy considers cash discounts a function of cash management and are not credited to the job. A company wide rate for cash discounts will be published each year to be applied against direct costs as defined above. This rate is computed based on total net cash discounts divided by the total applicable gross payments, company wide.

Joint venture jobs should use the cash discounts from the financial statements to develop their own rate. The disclosure should substitute "joint venture" for "company wide".

For additional information, contact Accounts Payable (Bill Thommes) in the home office.

10. ***Adjustment Explanations (Budget &Cost)***

The claim must disclose the method for developing the costs. Has the claim been developed based on the bid estimate, budget, actual costs, projected costs, or representative costs?

COMMENTS:

IF YOU REPRESENT THE "COSTS" AS ACTUAL, THEY MUST BE ACTUAL! NOT COMPOSITE RATES! NOT ESTIMATED! NOT BUDGET! NOT PROJECTED!

11. ***Non Sponsored Joint Ventures***

COMMENTS:

As a joint venture partner, a manager has a duty of " reasonable inquiry." If the manager is required to sign the certification as a non sponsored partner, the responsibility substantially increases from that of "reasonable inquiry." If the manager has any doubts about the claim or is requested to sign the certification, the legal department should be consulted before taking any action.

12. Subcontractors' Claims

Cost of claims for work performed by subcontractors is included in this claim. The subcontractors have certified their claims to our company as we in turn are required by the contract. The subcontractor's claim has been read and no errors or inconsistencies have been noted.

COMMENTS:

Kiewit has two obligations in regard to subcontractors' claims:

1. Obtain the same certification from the subcontractor's officer/ owner as we are required to provide;
2. A duty of **"reasonable inquiry,"** which includes the same review that we would give our own claims.

If the required certification cannot be obtained, consult the PKS legal department before submitting the subcontractor's claim.

If the subcontractor's claim does not appear reasonable, consult the PKS legal department before proceeding further.

SUMMARY

DEFECTIVE PRICING AND FALSE CLAIMS

General

1. A claim is any request for money. This includes progress payments, change orders, claims, etc.

2. A false claim is any request for money or property that:

   - We are not entitled to under the contract or the law; or
   - Is supported by incorrect statements, facts or figures; and/or
   - Is supported by correct but misleading information.

3. You are responsible for assuring that we are paid pursuant to the contract and the law for all the work that we have performed.

4. Submit only legitimate, accurate, supportable claims.

Applicable Statutes

1. Truth In Negotiations Act (TINA). What you should remember about TINA is that it:

   - Applies to negotiating a contract or price;
   - Applies to direct government procurement; and
   - Provides that a prime or subcontractor shall be required to submit costs or pricing data, and shall be required to certify that to the best of its knowledge and belief, the data is accurate, complete and current. Definition of "Cost or Pricing Data" is pretty broad (see Section III of the manual).

2. Other Applicable Statutes. There are a number of other statutes (civil and criminal) which apply to requests for money. It is not imperative that you know the particular law in detail, or the situations in which it applies, if you follow the following guidelines and suggestions. These guidelines should be followed when requesting any money, regardless of the law applicable.

Guidelines

- Do not submit false or fraudulent claims, records or statements when you know they are false.
- You must be certain that you are entitled to the money you seek.

- Margin should be recognized based on the risk we are taking or that we took on the project.
- The contract, and any cost principles referenced in the contract, is the law. You must be thoroughly familiar with contract clauses on changes, extra work, delays, suspension of work, differing site conditions, change order accounting, force account, submission of claims, etc.
- Consistency in estimating, recording, and reporting costs is a key point. The bid estimate, budget, cost report, and claim or request for additional compensation should be consistent. Any inconsistencies must be documented and explained.
- To the extent possible, use actual costs rather than estimated costs. If you represent the costs as "actual" they must be actual. Not composite rates, not estimated, not budget, not projected, but ACTUAL.
- Describe in detail the source documents from which the costs were obtained and how the costs were calculated.
- When asked to forward price change orders, be able to support amounts requested with cost data on similar work from prior projects. Representative costs from past work and adequate margin should be given full consideration on forward pricing of work.
- To the extent possible, segregate the costs claimed from costs incurred to perform the original contract work. When claimed costs are grouped with original contract costs, explain why they could not be segregated.
- Make certain costs have been properly charged.
- Be able to reconcile the claim costs to the cost report, and the cost report to the daily report; the daily report to the time card and foreman diary if applicable.
- Make sure the costs claimed are allowable under the cost principles and are reasonable.
- Avoid changing original entry documents. If changes are made, explain why (e.g. cost codes on time cards).
- Check mathematical calculations. Errors in math, particularly those that increase the amount of the claim, destroy credibility.
- Avoid duplication. When the same item is included in two separate claims make the fact known and explain why it is necessary.

- Keep in mind you are certifying that you believe you are legally entitled to the amount claimed. It cannot be an artificially high number from which you intend to negotiate. Do not inflate the claims for the purpose of ultimately negotiating a settlement at the level to which you think you are actually entitled.

- Keep in mind your claim will be audited. Make sure cost records are accurate and reliable.

- If you submit a claim that you later find has errors, advise the PKS Legal Department immediately.

- In non sponsored joint ventures, a manager has a duty of "reasonable inquiry". If the manager has any doubts about ' the claim or is requested to sign the certification, the PKS Legal Department should be consulted before taking any action.

Disclosure

There are several components to a request for money which may require some disclosure to make our request clearer. These components could include:

1. Labor Add-ons
2. Bond Rates
3. General and Administrative Rates
4. Change Orders
5. Equipment Rental Rates
6. Equipment Rental Hours
7. Margin Percent
8. On-site Overhead Rates
9. Cash Discounts on Vendor Invoices
10. Adjustment Explanations (Budget and Cost)
11. Subcontractor's Claims

Please refer to Guidelines for Proper Disclosure, Section VIII, of the manual.

If you have any questions at all, please contact an attorney in the PKS Legal Department.

Notes: