IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION

UNITED STATES OF AMERICA, ex rel. LEO DANIELIDES and, LEO DANIELIDES, individually	)	
Plaintiffs,	)	Case No. 1:09-cv-07306
v.	)	Judge Manish S. Shah
NORTHROP GRUMMAN SYSTEMS CORPORATION,	)	
Defendant.	)	

DEFENDANT NORTHROP GRUMMAN SYSTEMS CORPORATION'S MEMORANDUM IN SUPPORT OF ITS MOTION TO DISMISS RELATOR'S FIRST AMENDED COMPLAINT

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Defendant Northrop Grumman Systems Corporation ("Northrop Grumman") respectfully submits this memorandum in support of its Motion To Dismiss Relator's First Amended Complaint ("Complaint") under Rules 9(b) and 12(b)(6) of the Federal Rules of Civil Procedure.

INTRODUCTION AND SUMMARY OF ARGUMENT

Relator Leo Danielides attempts through this *qui tam* to transform a standard breach-of-contract action into a fraud claim. The Complaint asserts claims for violation of the False Claims Act ("FCA"), 31 U.S.C. §§ 3729-3733, but fails to allege the essential element of an FCA claim: an objectively false statement. Instead, Danielides bases his claims entirely on allegations that Northrop Grumman failed to use its "best efforts" to complete Phase III of a multi-phase government contract to develop a missile defense system for civilian aircraft ("the Counter-MANPADS project"). Danielides alleges that Northrop Grumman should have done more work (and spent more money) in furtherance of the contract's objectives, and should not be permitted to retain excess profits earned. At best, those allegations might support a breach-of-contract claim—which only the government could bring, and which the government has not asserted. But they are not cognizable under the FCA.

A. The Contract

As the Complaint explains, the Counter-MANPADS project proceeded in several phases. Compl. ¶¶ 1-4. At issue in this action is Phase III, the Operational Test and Evaluation Phase, implemented (in part) as Modifications 7 and 8 to the original contract between Northrop Grumman and the Department of Homeland Security ("DHS"). *Id.* ¶¶ 4, 19; Agreement Between Northrop Grumman and DHS ("Contract"), art. II, § A (attached as Ex. 1).[1] "The

[1] To avoid unnecessary repetition, the attached contract exhibits are all from Modification 8. The Modification 8 contract retains all the relevant language from Modification 7; all Modification 8 revisions are in bold italic script. The Court can consider the contract—as well as all other documents relied upon in the Complaint—at the motion-to-dismiss stage. *See, e.g.*, *188 LLC v. Trinity Indus.*, 300 F.3d 730, 735

emphasis" in Phase III was to build the Counter-MANPADS systems designed in Phase II, install the systems on commercial aircraft, and assess performance—all in accordance with a set schedule of tasks and deliverables. *See* Contract, Attachment 1: Statement of Work & Addendum 1, § 2.1 (attached as Ex. 2). Northrop Grumman was also to continue its engineering design work from Phase II to address identified improvements and enhance the reliability of the system. *Id.*

Pursuant to a "fixed price best efforts agreement," Ex. 1, art. VI, § A.1, Northrop Grumman agreed to perform the work specified in the Statement of Work and Task Description Document attached to the Phase III contract. Ex. 1, art IV, § A; *see also* Ex. 2; Contract, Attachment 2: Task Description Documents (attached as Ex. 3). DHS agreed to pay Northrop Grumman predetermined amounts in installments based on the transmission of specified deliverables or contractual "milestones." Ex. 1, art. IV, § A; *id.* art. VI, §§ A.1, B.1; Contract, Attachment 3: Schedule of Phase III Payments and Payable Milestones ("Payment Schedule") (attached as Ex. 4); Compl. Ex. 1. Northrop Grumman completed every task in the Payment Schedule and DHS paid the amounts provided for in the Payment Schedule. *See* Ex. 1, art. VI, § B.4; Compl. ¶ 15.

Under the contract, Northrop Grumman was not required to submit cost information—that is, detailed information on amounts actually expended—to DHS, and the agency was not permitted to withhold funds based on the costs Northrop Grumman incurred. Ex. 1, art. VI, §§ B.2–4. Rather, payment amounts were fixed and based on the achievement of pre-designated

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(7th Cir. 2002) ("[D]ocuments attached to a motion to dismiss are considered part of the pleadings if they are referred to in the plaintiff's complaint and are central to his claim.") (internal citation omitted); *Greifenstein v. Estee Lauder Corp., Inc.*, No. 12-cv-09235, 2013 WL 3874073, at *6 n.5 (N.D. Ill. July 26, 2013) (considering, at the motion-to-dismiss stage, documents the plaintiff "injected" into the case by relying upon them, even when not attached to the complaint).

milestones, as verified by DHS. *Id.* And so, throughout Phase III, DHS routinely paid Northrop Grumman according to the Payment Schedule even though Northrop Grumman did not regularly provide data on costs spent on particular tasks. Compl. ¶¶ 15, 97-102.

B. The Complaint

Danielides alleges that Northrop Grumman intended to and did earn excess profits by expending only minimal effort and resources on Phase III, all the while representing to DHS that it was putting forth its "best efforts." In particular, Danielides claims that Northrop Grumman did not devote available resources to a laundry list of "key tasks" supposedly required by the contract. *Id.* ¶¶ 79-94. And, Danielides says, Northrop Grumman refused to provide DHS with information about costs incurred in order to mislead DHS into believing that "best efforts" were being expended, and in order to obtain full payment from DHS. *Id.* ¶¶ 83, 91, 93.

Based on these allegations, Danielides asserts claims for violations of the FCA. *Id.* ¶¶ 123-32. The Complaint does not enumerate specific counts, nor does it specify a precise theory of liability. Although the FCA requires a relator to link allegedly false or fraudulent statements to specific claims for payment to the government, Danielides does not even attempt to do so for the vast majority of the contract's invoices. Instead, in an attempt to maximize his recovery and cast a wide net of fraud over *all* claims for payment submitted under the $62 million Phase III contract, *id.* ¶ 10, Danielides simply refers broadly to the allegations about Northrop Grumman's purported nonperformance of the contract and labels all of these a fraudulent failure to comply with (what he alleges to be) the "accepted" criterion for meeting the best efforts requirement, *id*. ¶¶ 38, 129.

When construed in the light most favorable to Danielides, the Complaint's imprecise allegations appear to assert two theories for his claim that all payments under Phase III were in

violation of the FCA: (1) a claim that *all* invoices submitted to the government for payment under the Phase III contract were false because Northrop Grumman impliedly certified that it had complied with the "best efforts" provision of the contract, despite knowing that it was in breach of that provision, *id.* ¶¶ 129(b)–(f); *see also id.* ¶ 19; and (2) a claim for fraudulent inducement based on allegations that Northrop Grumman induced the government to enter into Phase III by promising "to provide its best efforts in performing the contract" despite never intending to do so, *id*. ¶ 129(a); *see also id.* ¶¶ 50-61. The Complaint also singles out three specific invoices—totaling $5 million (out of $62 million invoiced in Phase III)—and alleges supposed inaccuracies in the Northrop Grumman reports identified on those invoices. *Id.* ¶ 128; Compl. Exs. 2, 3, 4.

The Complaint should be dismissed under Fed. R. Civ. P. 12(b)(6) and 9(b), for several independent reasons. *First,* each of Danielides's claims depends entirely on his unsupported assertion that "best efforts" required Northrop Grumman to exhaust all budgeted funding on each task completed over the course of the contract. But it is well-established as a matter of law that fraud claims under the FCA cannot rest on allegations about the subjective interpretation of a contractual term. *Second,* even if Danielides can rely (at this stage) on his preferred definition of "best efforts," he has failed to allege that every payment made to Northrop in connection with Phase III was procured through a *false claim*. His limitless theory of implied certification has never been accepted by the Seventh Circuit or by this Court. And his fraudulent inducement theory fails because Danielides does not allege facts demonstrating that at the time the Phase III contract was negotiated Northrop Grumman did not intend to use its best efforts to complete the contract's objectives. *Finally*, even for the three invoices he attaches, Danielides fails to state an FCA claim for much the same reason: The reports the invoices reference can be considered inaccurate only if the Court accepts Danielides's subjective interpretation of "best efforts," and,

with regard to the largest invoice, his allegations challenge a statement that does not even appear in the referenced report. The Complaint should be dismissed in its entirety.

ARGUMENT

I. There Can Be No FCA Claim Based On Allegations That Northrop Grumman Failed To Use "Best Efforts" Under The Contract.

To state an FCA claim, Danielides must allege facts showing that Northrop Grumman "made a statement in order to receive money from the government; (2) that the statement was false; and (3) that the defendant knew the statement was false." *United States ex rel. Yannacopoulos v. Gen. Dynamics*, 652 F.3d 818, 822 (7th Cir. 2011). The claim or statement must "represent[] an objective falsehood." *Id.* at 836 (internal citation omitted). "In short, the false claim must be a lie." *United States ex rel. Durcholz v. FKW Inc.*, 997 F. Supp. 1159, 1167 (S.D. Ind. 1998), *aff'd* 189 F.3d 542 (7th Cir. 1999). The FCA is intended to protect the government from losses incurred as a result of fraud: It is *not* a vehicle for relators to raise disputes about whether a government contractor fulfilled its contractual obligations. *E.g.*, *United States ex rel. Owens v. First Kuwaiti Gen. Trading & Contracting Co.*, 612 F.3d 724, 728 (4th Cir. 2010). "While the phrase 'false or fraudulent claim' in the False Claims Act should be construed broadly, it just as surely cannot be construed to include a run-of-the-mill breach of contract action that is devoid of any objective falsehood." *United States ex rel. Wilson v. Kellogg Brown & Root, Inc.*, 525 F.3d 370, 378 (4th Cir. 2008) (internal citation omitted).

Danielides's false certification and fraudulent inducement claims each rests on the assertion that Northrop Grumman promised but failed to put forth its "best efforts" in performing the contract. *See* Compl. ¶¶ 5-7; 38-40, 51-55, 60, 75, 83, 91, 94, 102, 122, 129(a), 129(b). The term "best efforts," however, is not defined in the contract or by any applicable regulations. Although the term "best efforts" is frequently used in contracts, its meaning varies between

contracts and routinely is disputed as a matter of contract law. *See, e.g.*, *Olympia Hotels Corp. v. Johnson Wax Dev. Corp.*, 908 F.2d 1363, 1373 (7th Cir. 1990) (holding that meaning of "best efforts" depended on how that term was interpreted in similar contracts involving same promisor); *Gates v. Johnson Worldwide Assocs., Inc.*, No. 00 C 7612, 2002 WL 663586, at *5 (N.D. Ill. Mar. 28, 2002) (noting that "best efforts" clause was vague because the contract contained no "objective criteria that would enable either the Court or the jury to determine what was required"); *Garbelmann v. Creditcard Keys Co.*, No. 89 C 6020, 1992 WL 73531, at *2 (N.D. Ill. Mar. 27, 1992) (same). Danielides's allegations that Northrop Grumman falsely represented that it was using its "best efforts" in performing Phase III turn on "nothing more than his own interpretation of [that] imprecise contractual provision." *Wilson*, 525 F.3d at 378.

Danielides nonetheless insists that there is an "accepted objective criterion in federal procurement for meeting the best-efforts requirement" (Compl. ¶ 38) and that Northrop Grumman therefore was required to exhaust available funding in furtherance of the contract's objectives. *Id.* ¶¶ 5-7; 38-40, 51-55, 60, 75, 83, 91, 94, 102, 122, 129(a), 129(b). He is wrong for two independent reasons. *First*, the Phase III contract is an Other Transaction Agreement ("OTA"). OTAs are not procurement contracts, and thus are exempt from most rules and regulations applicable to government contracts, including the Federal Acquisition Regulation, Cost Accounting Standards, Contract Disputes Act, and the Truth in Negotiations Act. *See, e.g.*, Susan B. Cassidy et al., *Another Option in a Tightening Budget: A Primer on Department of Defense "Other Transactions" Agreements*, 48 PROCUREMENT LAW. 3, 4 (2013) ("One of the primary advantages of OT agreements is that they are not subject to the FAR or many procurement statutes that govern traditional federal procurements."). Tellingly, the Complaint's discussion of "best efforts" (at ¶¶ 5-6) closely tracks provisions in the Federal Acquisition

Regulations, which do not govern the Phase III contract.[2] To the extent there is an objective definition of "best efforts" for procurement contracts, that definition is not applicable to the contract here.

Second, Danielides deliberately blurs the important distinction between fixed-price government contracts and cost-reimbursement government contracts. Payments on fixed-price contracts focus on contractor *output*: The contractor agrees to deliver specific material or services for a fixed price negotiated at the outset. *See generally McDonnell Douglas Corp. v. United States*, 37 Fed. Cl. 295, 298-99 (1997). The contractor is paid the fixed amount regardless of whether it ultimately devotes more or less resources than anticipated in providing the specified deliverables. *See id.* By contrast, payment on cost-reimbursement contracts focuses on contractor *input*: The contractor agrees to use its "best efforts" to perform the work requested, and the government agrees to pay the indeterminate sum of allowable incurred costs. *See id.* For this reason, basic cost-reimbursement contracts are often referred to as "best efforts" agreements. *See, e.g.*, *Gen. Dynamics Corp. v. United States,* 229 Ct. Cl. 399, 671 F.2d 474, 480-81 (Ct. Cl. 1982); *Ne. Univ. v. BAE Sys. Info. & Elec. Sys. Integration Inc.*, Civ. Act. No. 13-12497-NMG, 2013 WL 6210646, at *6 (D. Mass. Nov. 27, 2013).

Phase III was "a *fixed price* best efforts" contract (Ex. 1, art. VI, § A.1 (emphasis added)) that expressly provides that payments were due upon the completion of specific, identified tasks,

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[2] *Compare, e.g.*, Compl. ¶ 5 ("Best-efforts contracting is commonly used in research and development type contracts where it is uncertain whether all program objectives will be met."), *with* 48 C.F.R. § 16.302(b) ("A cost contract may be appropriate for research and development work."), *and with Cost-Plus Contract*, INVESTOPEDIA, http://www.investopedia.com/terms/c/cost-plus-contract.asp (last visited July 10, 2014) ("Cost-plus contracts are commonly used in research and development activities, where it is difficult to determine in advance how much a job should cost.").

regardless of performance cost. Ex. 1, art. VI, § B.[3] In a fixed price contract, the "right to payment . . . [i]s not based on its costs or labor hours expended." *United States ex rel. Yannacopoulos v. Gen. Dynamics*, 636 F. Supp. 2d 739, 746 (N.D. Ill. 2009), *aff'd* 652 F.3d 818 (7th Cir. 2011). The difference is crucial: "Unlike the cost-reimbursement type contract in which the government bears the burden of all allowable costs, the burden is shifted entirely to the contractor in a fixed-price contract, and the government bears only the risk of over-estimating project costs (and therefore agreeing to pay an unnecessarily large fixed-price)." *Info. Sys. & Networks Corp. v. United States*, 64 Fed Cl. 599, 606 (2005). For that reason, if, in the actual performance of the contract, the contractor realizes more profit than originally anticipated, that is of no concern to the government because the contractor's obligations were "set at fixed rates" and thus the government "knew, or should have known, that [the contractor] would reap the benefits of any cost savings." *Prime ex. rel. United States v. Post, Buckley, Shuh & Jernigan, Inc.*, No. 6:10-cv-1950-Orl-36DAB, 2013 WL 4506357, at *10 (M.D. Fla. Aug. 23, 2013).

Because the term "best efforts" is typically applied only to cost reimbursement contracts, there is no recognized meaning of "best efforts" in a *fixed-price* agreement. There is only one instance of a "fixed price best efforts" government contract ever being litigated—and that series of cases, spanning over a dozen years and eventually morphing into a Federal Tort Claims Act dispute, never purported to establish an objective definition of "best efforts" in the context of an OTA fixed price agreement. *See Gen. Dynamics Corp. v. United States*, 139 F.3d 1280 (9th Cir. 1998); *United States v. Gen. Dynamics Corp.*, 828 F.2d 1356 (9th Cir. 1987); *Gen. Dynamics Corp. v. United States*, No. CV 89-6762 JGD, 1996 WL 200255 (C.D. Cal. Mar. 25, 1996); *United States v. Gen. Dynamics Corp.*, 644 F. Supp. 1497 (C.D. Cal. 1986). Instead, those cases

[3] Danielides refers to "best efforts" dozens of times, *see* Compl. ¶¶ 5, 6, 7, 9, 14, 36, 37, 38, 39, 40, 45, 49, 50, 51, 53, 54, 55, 60, 75, 83, 91, 94, 102, 122, 129, while mentioning only twice and in passing that this was in fact a "*fixed price*[] best efforts" agreement, *see id.* ¶¶ 37, 50.

concerned the altogether different situation of how a contractor can account for additional spending when it has already spent all of the fixed funding called for in the contract. To the extent that litigation is at all relevant, it is only to highlight the "ambiguous" nature of what "best efforts" means in a "fixed price" setting. *Wilson*, 525 F.3d at 377.[4]

Because there is no established definition of best efforts in the context of an OTA fixed-price contract, Northrop Grumman's alleged failure to meet best efforts is not an "objective falsehood" and thus cannot form the basis of an FCA claim. The Seventh Circuit has held that the FCA's standard is not satisfied by "mere differences in interpretation growing out of a disputed legal question involving the terms of a contract." *Yannacopoulos*, 652 F.3d at 836 (internal citation omitted); *United States ex rel. Lamers v. City of Green Bay*, 168 F.3d 1013, 1018 (7th Cir. 1999) ("imprecise statements or differences in interpretation growing out of a disputed legal question are [] not false under the FCA"); *see also Wilson*, 525 F.3d at 378 ("[R]elator cannot base a fraud claim on nothing more than his own interpretation of an imprecise contractual provision."). Rather, liability must be based on an "objective falsehood." *Yannacopoulos*, 652 F.3d at 836 (internal citation omitted). Courts therefore routinely dismiss FCA claims that are based on the "[r]elators' subjective interpretation of [defendant's] contractual duties." *Wilson*, 525 F.3d at 376-77 (dismissing fraudulent inducement claim); *see also United States ex rel. DeKort v. Integrated Coast Guard Sys.*, 705 F. Supp. 2d 519, 536-37 (N.D. Tex. 2010) (dismissing fraudulent inducement claim); *cf. U.S. Dept. of Transp. ex rel. Arnold v. CMC Eng'g*, No. 13-2759, 2014 WL 2442945, at *3 (3d Cir. June 2, 2014) (surveying case law); *United States ex rel. K & R Ltd. P'ship v. Mass. Hous. Fin. Agency*, 530 F.3d 980, 984

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[4] Indeed, in that case, the court's determination of the meaning of "best efforts" in the non-OTA contract relied exclusively on the deposition testimony of witnesses who negotiated the contract, and did not cite case law, regulations, or even expert testimony. *Gen. Dynamics Corp.*, 1996 WL 200255, at *3.

(D.C. Cir. 2008) (affirming summary judgment where parties "simply disagree[d] about how to interpret ambiguous contract language"). Because Danielides's claims rely on whether Northrop Grumman intended to or did use its "best efforts," they should be dismissed.[5]

II. The Complaint Fails To Allege That All Payments Under Phase III Were In Violation Of The FCA Under An Implied Certification Or Fraudulent Inducement Theory.

Even if Danielides could adequately allege that Northrop Grumman failed to comply with the "best efforts" aspect of Phase III, he would still need to allege that Northrop Grumman made a false statement "in order to receive money from the government." *Yannacopoulos*, 652 F.3d at 822. Danielides invokes two theories to transform *all* invoices submitted in Phase III into false claims: implied certification and fraudulent inducement. Neither theory states a claim.

A. *The Complaint's Implied Certification Theory Fails To State A Valid FCA Claim.*

In an attempt to cast a wide net of "fraud" over every invoice (thereby maximizing his potential recovery), Danielides alleges that every time Northrop Grumman submitted an invoice to the government, it impliedly certified that it was acting with his preferred reading of "best efforts." *See* Compl. ¶ 49; ¶ 129(b) ("Northrop submitted its claims for advance payments with the intention . . . not to exert its best efforts on the contract"); ¶ 129(c) ("Northrop submitted the claims under the pretense of compliance, when it knew it was in material breach of the contract"); ¶ 129(d) ("Each request for a milestone payment misrepresented and omitted material information concerning Northrop's performance of the contract, including cost and schedule

[5] A Complaint premised on the alleged breach of a vague contractual provision also cannot satisfy the FCA's scienter requirement. After all, "where disputed legal issues arise from vague provisions or regulations, a contractor's decision to take advantage of a position cannot result in his filing a 'knowingly' false claim." *United States v. Southland Mgmt. Corp.*, 326 F.3d 669, 682 (5th Cir. 2003) (en banc) (Jones, J., concurring) (citing *United States ex rel. Siewick v. Jamieson Sci. & Eng'g, Inc.*, 214 F.3d 1372, 1378 (D.C. Cir. 2000)); *accord Hagood v. Sonoma Cnty. Water Agency*, 81 F.3d 1465, 1478 (9th Cir. 1996) ("[T]o take advantage of a disputed legal question . . . is to be neither deliberately ignorant nor recklessly disregardful.") (internal citation omitted).

performance information"); ¶ 129(e) ("underlying performance of the contract"); ¶ 129(f) ("Northrop failed to meet its monthly deliverable cost and schedule reporting commitment which is integral to each and every milestone"). Danielides's boundless theory of implied certification liability cannot be squared with Rule 9(b)'s requirement that plaintiffs proceeding under the FCA "must link specific allegations of fraud to claims for government payment," *Mason v. Medline Indus., Inc.*, No. 07 C 5615, 2009 WL 1438096, *2 (N.D. Ill. May 22, 2009) (citing *Garst v. Lockheed-Martin Corp.*, 328 F.3d 374, 378 (7th Cir. 2003)), and should be rejected.

First, the Seventh Circuit has never recognized "'implied certification' in the context of FCA claims." *United States ex rel. Stone v. Omnicare, Inc.*, No. 09 C 4319, 2012 WL 5877544, at *1 (N.D. Ill. Nov. 20, 2012). Instead, FCA claims are analyzed at the "'*individualized transaction level*.'" *Id.* (quoting *United States ex rel. Fowler v. Caremark RX, LLC*, 496 F.3d 730, 741-42 (7th Cir. 2007) (emphasis in original)). That is, "specific allegations of deceit" must be "link[ed] to a[] claim for payment." *Garst*, 328 F.3d at 378. Danielides makes no attempt to do that for the vast bulk of the invoices Northrop Grumman submitted to the government.[6]

Second, even if implied certification were an otherwise viable theory, Danielides nevertheless cannot show that there were "claims being made on the government for monies that would not otherwise have been owed in the absence of fraud." *United States ex rel. Bettis v. Odebrecht Contractors of Cal., Inc.*, 297 F. Supp. 2d 272, 282 (D.D.C. 2004); *accord Luckey v. Baxter Healthcare Corp.*, 183 F.3d 730, 731 (7th Cir. 1999) (discussing materiality). Danielides's underlying allegations of fraud concern matters untethered to Northrop Grumman's

[6] Even those few courts in the Northern District that have recognized implied certification as a valid FCA theory have not done so in a context like this one. Implied certification has been limited to where the alleged implicit certification was to applicable statutes and regulations, not to any and all terms in an underlying contract. *See, e.g.*, *United States ex rel. Bidani v. Lewis*, 264 F. Supp. 2d 612, 614 (N.D. Ill. 2003) (allowing allegation that filing Medicare reimbursement claims implied compliance with Medicare anti-kickback statute).

contractual obligations and, consequently, to DHS's obligation to pay. The complaint does not, for instance, allege that Northrop Grumman was contractually committed to spend a specific amount of money on Independent Research and Development ("IRAD"), *see* Compl. ¶¶ 67-69, perhaps because nothing in the contract required it to do so, *see* Exs. 1, 4. Similarly, nothing in the contract required Northrop Grumman to spend the full amount originally budgeted for reliability testing (done pursuant to a methodology known as "FRACAS"). *See* Compl. ¶¶ 11-15, 90. Rather, the contract set a basic requirement that Northrop Grumman maintain a FRACAS database and perform certain analysis. *See id.* ¶ 13 (noting that Northrop Grumman spent funds on FRACAS). The Complaint also does not allege that Northrop Grumman presented any claim for payment to DHS for its allegedly fraudulent PASE work, *see id.* ¶¶ 113-117—indeed, it conspicuously avoids doing so, *see id.* at ¶ 115.

By the express terms of the contract, Northrop Grumman agreed only to provide the government specific deliverables. *See* Ex. 1, art. VI A.1, B.3. Tellingly, when Danielides discusses Northrop Grumman's failure to comply with its contractual obligations, his allegations refer obliquely to the "intended objective," Compl. ¶ 5, "program objectives," *id.*, "contract objectives," *id.* ¶¶ 5, 39, and "development objectives," *id.* ¶ 38, rather than to the specific milestones that Northrop Grumman actually was contractually obligated to meet.[7] Because none of these alleged improprieties were "condition[s] of payment of government money," they cannot satisfy the FCA. *United States ex rel. Gross v. AIDS Research Alliance-Chicago*, 415 F.3d 601, 605 (7th Cir. 2005); *see also Lamers*, 168 F.3d at 1019 ("Even if [a false statement] was an outright lie, the lie was immaterial because there was no requirement that the routes be

[7] *See* Ex. 1, art. VI, § A.1 (providing for "milestone payments . . . upon the completion of the acceptance criteria outlined in Attachment 3 as accepted by the Government"); *id.* art. VI, § B.3 ("Payments shall be made in the amounts set forth in Schedule of Payments and Payable Milestones, provided the OTCOTR has verified the accomplishment of the Payable Milestones in accordance with the acceptance criteria.").

mere extensions of existing routes."); 1 J. BOESE, CIVIL FALSE CLAIMS AND *QUI TAM* ACTIONS § 2.03(G)(3) (4th ed. 2012) ("[A] claim is legally false under the FCA only where the statute, regulation, or contract provision violated requires compliance *as a condition of payment*.") (emphasis added).

The closest Danielides comes to identifying a problem with something actually contemplated by the contract (rather than his own subjective interpretation of what "best efforts" requires) is his allegation that Northrop Grumman "failed to meet its monthly deliverable cost and schedule reporting commitment." Compl. ¶ 129(f). These monthly reports were generally described as deliverables in the contract, Ex. 1, art. XIV, but, importantly, were not milestone requirements triggering the government's payment obligation, *see* Ex. 4 (Payment Schedule). What is more, apparently DHS did not agree with Danielides that the monthly reports were "integral to each and every milestone," Compl. ¶ 129(f), because despite receiving what Danielides alleges were missing or incomplete reports, *id.* ¶ 46, the agency made timely milestone payments anyway, *see id.* ¶¶ 15, 29 102. The government is free to waive contractual requirements as it sees fit. *See, e.g.*, *Abcon Assocs., Inc. v. United States*, 44 Fed. Cl. 625, 629 (1999).[8] As the Seventh Circuit explained, "[i]f the government knows and approves of the particulars of a claim for payment before that claim is presented, the presenter cannot be said to have knowingly presented a fraudulent or false claim." *United States ex rel. Durcholz v. FKW, Inc.*, 189 F.3d 542, 545 (7th Cir. 1999); *accord* BOESE, CIVIL FALSE CLAIMS AND *QUI TAM* ACTIONS, at § 2.03(F). Courts routinely dismiss FCA allegations when the government knew of

[8] In any event, Danielides's allegations concerning the monthly reports are premised yet again on his subjective view that "best efforts" required Northrop Grumman to account to the government for every dollar spent and retained. *See* Compl. ¶¶ 44-46. It is irrelevant that Northrop Grumman did "not disclose[] to the United States" that it had not spent all the estimated funds, Compl. ¶ 85, because DHS contracted to pay Northrop Grumman a "fixed price" for its efforts, *see* Ex. 1, art. VI, § (A)(1). The estimated price negotiated at the beginning of a fixed-price contract "is simply that, an estimate." *Great Lakes Dredge & Dock Co. v. United States*, 60 Fed. Cl. 350, 370 (2004).

the conduct that was supposedly wrongful and yet continued to make payments under the contract. *See, e.g.*, *United States ex rel. Stierli v. Shasta Servs. Inc.*, 440 F. Supp. 2d 1108, 1113-14 (E.D. Cal. 2006) (granting motion to dismiss); *United States ex rel. Boisjoly v. Morton Thiokol, Inc.*, 706 F. Supp. 795, 809-11 (D. Utah 1988) (same); *United States ex rel. Herbert v. Nat'l Acad. of Scis.*, Civ. A. No. 90-2568, 1992 WL 247587, at *8 (D.D.C. Sept. 15, 1992) (same).

B. *The Complaint Fails To Allege Intent Not To Perform With Sufficient Particularity To State A Claim For Fraudulent Inducement.*

A relator alleging fraudulent inducement must allege that, *at the time the contract was negotiated*, the defendant had no intention of complying. *Lamers*, 168 F.3d at 1018 ("[P]romises of future compliance [are] knowingly false only if the [promisor] never intended to comply . . . ."). Intent not to perform is a critical element of a fraudulent inducement claim that serves to differentiate fraud claims from run-of-the-mill breach-of-contract claims. *Wilson*, 525 F.3d at 380. A relator must plead intent not to perform with sufficient particularity to satisfy the heightened pleading standard in Rule 9(b), which requires setting forth "'specific objective manifestation of fraudulent intent—a scheme or device.'" *Am. Diagnostic Med., Inc. v. Cardiovascular Care Grp.*, No. 03 C 8929, 2004 WL 1490268, at *2 (N.D. Ill. July 1, 2004) (quoting *Indus. Specialty Chems., Inc. v. Cummins Engine Co., Inc.*, 902 F. Supp. 805, 813 (N.D. Ill. 1995)). In other words, "[t]he plaintiff must allege sufficient facts to show that the defendant never intended to keep its word." *Id.*

Danielides alleges no such facts, let alone ones that would satisfy Rule 9(b)'s heightened pleading requirements. The Complaint contains only conclusory allegations of intent not to perform. *See* Compl. ¶ 55 ("Northrop . . . did not intend to provide Northrop's best efforts in performing Phase III."); ¶ 129(a) ("Northrop never intended to provide its best efforts in

performing the contract."). These barebones allegations are insufficient to support a claim for fraudulent inducement. *See, e.g.*, *United States ex rel. Gay v. Lincoln Tech. Inst., Inc.*, No. Civ. A. 301-cv-505K, 2003 WL 22474586, at *4 (N.D. Tex. Sept. 3, 2003) (dismissing claim because relator did not "allege facts suggesting that, at the time [defendant] entered into the Agreements [defendant] had the requisite intent to fraudulently induce the government"); *United States ex rel. Graves v. ITT Educ. Servs., Inc.*, 284 F.Supp.2d 487, 503 (S.D. Tex. 2003) (same).

In lieu of particularized allegations regarding Northrop Grumman's intent at the time it negotiated Phase III, Danielides's complaint contains a laundry list of allegations related to Northrop Grumman's supposed nonperformance under the contract. *See* Compl. ¶¶ 56-59 (alleging that Northrop Grumman did not perform sufficient reliability testing or engineering work); *id.* ¶¶ 60-61 (alleging that Northrop Grumman withheld cost and scheduling information from DHS); *id.* ¶¶ 62-63 (alleging that Northrop Grumman did not team-up with Northwest Airlines). But "facts relating to contractual nonperformance . . . are more appropriately viewed as a basis for a breach of contract action, not a fraudulent inducement claim." *Wilson*, 525 F.3d at 380. Particularly here, where there is no allegation that DHS has complained about Northrop Grumman's work, Danielides cannot invoke the FCA based solely on allegations of nonperformance. *See id.*

III. The Attached Invoices Do Not State A False Claim.

Danielides's lengthy complaint identifies only three invoices—together requesting payment of $5 million (out of what he alleges was a "$62 million government contract," Compl. ¶ 10)—that he even attempts to tie to a false statement. Each of these invoices, which are attached to the Complaint (Compl. Exs. 2–4), stated that Northrop Grumman had delivered the report associated with the relevant milestone payment. *Compare* Compl. Ex. 1 (list of

milestones). Danielides does not dispute that Northrop Grumman delivered the identified reports. Instead, he takes issue with how each of the reports described (or failed to describe) Northrop Grumman's expenditures in performing the contract. None of the three reports, however, contains any objectively false statement. And, with regard to the largest invoice at issue (Compl. Ex. 2), the Complaint focuses on an allegedly false statement that *does not even appear* in the report identified on the invoice.

Danielides's claims based on the three specific invoices founder because they turn on his view of what "best efforts"—a term that does not even appear on the invoices—required Northrop Grumman to do. He complains that each report gives the false impression that Northrop Grumman had performed all of the FRACAS testing that was required under the contract. Danielides admits that FRACAS testing was in fact done, Compl. ¶ 82; he complains, nonetheless, that Northrop Grumman did not spend enough on FRACAS testing. *Id.* ¶ 81 (Delta Design Review); *id.* ¶ 98 (Interim Reliability Report); *id.* ¶ 92 (Final Report). At bottom, his complaints are nothing more than a rehashing of his allegations that Northrop Grumman did not inform the government that it was not spending all budgeted funds. *See* Compl. ¶¶ 79-86 (alleging that the Delta Design Review was fraudulent in large part because Northrop Grumman failed to spend all the budgeted FRACAS costs); *id.* ¶¶ 88-90 (alleging that the Interim Reliability Improvement Report was fraudulent because Northrop Grumman failed to spend all the budgeted FRACAS costs); *id.* ¶¶ 92-94 (alleging that the Final Milestone Report was fraudulent because Northrop Grumman failed to spend all the budgeted FRACAS costs). On its face, the contract did not require Northrop Grumman to spend particular amounts on these tasks. *See generally* Ex. 2. The contract required, in relevant part, only that Northrop Grumman maintain a FRACAS database, analyze failure results from FRACAS, identify potential

corrective actions, and, with DHS approval, implement the corrections. *See id.* § 2.2 (describing specific tasks). For all his grumbling about Northrop Grumman's cost savings, *see* Compl. ¶¶ 82, 84, 91, 92, Danielides never alleges that it did not satisfy these contractual requirements.[9] Based on this Complaint, Danielides does not sufficiently allege breach of contract, let alone the "intentional, palpable lie[s]" necessary to state a claim under the FCA. *United States ex rel. Hopper v. Anton*, 91 F.3d 1261, 1267 (9th Cir. 1996).

Even if Danielides's allegations were enough to satisfy the FCA's pleading requirements for the Interim Reliability Improvement Report (Compl. Ex. 3) and the Phase III Final Report (Compl. Ex. 4), totaling just $1,836,500, his Complaint does not sufficiently allege fraud in the $3,324,500 milestone payment for the Delta Design Review, *see* Compl. Ex. 2. At the crux of that claim is a chart—prepared by Danielides himself, *see* Compl. ¶ 106—that he alleges Northrop Grumman presented in the Delta Design Review meeting in order to cover up Northrop Grumman's lower spending on the contract. *See id.* ¶ 106 (Chart: Baseline Spend Plan vs Actual Cost); *see generally id.* ¶¶ 105-109. But that spending chart was *never included* in the Delta Design Review materials. *See* C-MANPADS Delta Design Review (attached as Ex. 5). Instead, Northrop Grumman presented it to the government only as part of a management report unrelated to the Delta Design Review. *See* Phase III Program Management Report ("Report") at 49 (attached as Ex. 6). Because Danielides fails to "link" his "specific allegation[] of deceit"

[9] Along the way, Danielides also alleges that Northrop Grumman concealed in these reports its failure to perform "other key tasks required by the contract." Compl. ¶¶ 83, 93; *see also id.* ¶ 91. Just what all these were is unclear. Even assuming that these "other key tasks" consist solely of "test and evaluation work, manufacture and support work, and engineering work involving the emergency ground notification system," *id.* ¶ 93, those bare allegations, standing alone, hardly satisfy the requirement to "state with particularity the circumstances constituting fraud or mistake," Fed. R. Civ. P. 9(b); *see also Gross*, 415 F.3d at 605 (plaintiff must identify "the who, what, when, where, and how" of the alleged fraud). It is especially important to allege facts showing fraudulent intent with particularity when alleging that certain contractual tasks were not performed, because "failing to keep one's promise is just breach of contract," not fraud. *Garst*, 328 F.3d at 378.

concerning the Delta Design Review to the "claim for payment," *Garst*, 328 F.3d at 378, his fraud claim regarding Exhibit 2 should be dismissed.

In any event, the very documents Danielides cites undermine his attempt to cloak Northrop Grumman's actions in the specter of fraud. The report including the spending chart contained another chart—*on the very next page*—accurately showing that, as of the end of July 2007, Northrop Grumman had incurred approximately 17% fewer labor hours than originally budgeted in the contract. *See* Ex. 6 at 50. That Northrop Grumman would include such a chart showing significantly lower expenses belies Danielides's allegations that it was acting with fraudulent intent to deceive the government. "[T]he False Claims Act condemns fraud but not negligent errors or omissions." *Garst*, 328 F.3d at 376 (affirming dismissal of FCA complaint for failure to plead fraud with particularity). Indeed, even the offending chart itself shows that Northrop Grumman was not spending the full budgeted amount in performance of the contract. *See* Ex. 6 at 49; Compl. ¶¶ 106-07. If Northrop Grumman "wanted to hide the truth from the government" about how much it was not spending, Compl. ¶ 109, a chart showing incurred expenses coming in under the contract's cost estimates would seem a poor attempt to do so. Danielides's allegations do not support an inference of fraud.

Conclusion

For all these reasons, the Court should dismiss the Complaint with prejudice.

Respectfully submitted,

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Dated: July 15, 2014

CERTIFICATE OF SERVICE

I, Eric A. White, an attorney, hereby certify that the attached Defendant Northrop Grumman Systems Corporation's Memorandum of Law in Support of Its Motion to Dismiss Relator's First Amended Complaint was filed and served on all counsel of record via the Court's CM/ECF system on this 15th day of July, 2014. Simultaneous with this motion, Northrop Grumman filed a Motion for Leave to file Exhibit 5 under Seal. I certify that a copy of Exhibit 5 was delivered electronically to all counsel of record.

/s/ Eric A. White