UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF WISCONSIN

UNITED STATES OF AMERICA, ex rel.
MARY J. PATZER and PETER CIMMA,
Plaintiffs,

v. **Case No. 11-C-0560**

SIKORSKY AIRCRAFT CORPORATION,
SIKORSKY SUPPORT SERVICES, INC., and
DERCO AEROSPACE, INC.,
Defendants.

DECISION AND ORDER

The United States alleges that defendant Sikorsky Support Services, Inc. ("SSSI") breached its contract with the Navy and violated the False Claims Act ("FCA") by subcontracting with its affiliate, defendant Derco Aerospace, Inc., on a cost-plus-a-percentage-of-cost ("CPPC") basis. The case is set for a jury trial, and this order addresses the parties' motions in limine. I assume that the reader is familiar with my prior opinions, which explain the facts and legal background of the case. *See, e.g., United States ex rel. Patzer v. Sikorsky Aircraft Corp.*, No. 11-C-0560, 2023 WL 6883637 (E.D. Wis. Oct. 17, 2023); *United States ex rel. Patzer v. Sikorsky Aircraft Corp.*, 575 F. Supp. 3d 1032 (E.D. Wis. 2021).

I. Government's Motions

A. Motion for Jury Instructions Regarding Summary Judgment Rulings and to Preclude Evidence or Argument Inconsistent with Summary Judgment Rulings

1. Preliminary jury instructions

The government asks that I instruct the jury at the outset of the case about the issues that I have already decided and the limited scope of the issues that the jury must resolve. The government has submitted a proposed preliminary instruction for this purpose. Defendants agree that I should give a preliminary instruction, but they take issue with many aspects of the government's proposed instruction. Defendants have submitted a competing proposed instruction. I too agree that preliminary instructions are in order. I will take the parties' proposals under advisement and will distribute my own proposed instruction to the parties at the final pretrial conference so that objections can be resolved before the start of trial.

2. Evidence or argument contradicting the court's ruling that SSSI and Derco engaged in CPPC contracting

The government seeks to preclude defendants from presenting evidence or argument contradicting my ruling that SSSI and Derco violated the prohibition on the use of the CPPC system of contracting. *See Patzer*, 575 F. Supp. 3d at 986–95. Although I will not allow defendants to present such evidence or arguments, I do not think that defendants are proposing to do so. Instead, defendants intend to offer evidence that the relevant decisionmakers at SSSI and Derco did not *believe* that their subcontract resulted in a CPPC violation. While defendants previously used this evidence at the summary-judgment stage to argue that they did not violate the CPPC

prohibition in the first place, that same evidence is relevant to scienter because it provides a potential innocent explanation for their conduct.

For example, defendants argued at summary judgment that the subcontract was not CPPC because Derco added a 32% markup to what it regarded as its estimated costs rather than its actual costs. Although I rejected the argument that Derco's estimated costs—the costs reflected on vendor quotes—were true estimates for purposes of the CPPC prohibition, that does not preclude defendants from trying to convince the jury that the relevant decisionmakers sincerely believed that the vendor quotes were bona fide estimates. Similarly, although I rejected defendants' argument that Derco sold parts to SSSI at firm-fixed prices, that does not preclude defendants from trying to convince the jury that the relevant decisionmakers sincerely believed that Derco sold at firm-fixed prices. Thus, although defendants will not be permitted to argue that the subcontract was not CPPC, they remain free to present evidence and argument that the relevant decisionmakers at SSSI and Derco did not believe that the subcontract was CPPC at the time they entered into it and submitted claims for payment to the Navy.[1]

The government disputes that evidence of this sort is admissible with respect to scienter. I will defer my discussion of the government's arguments on this topic until I address the government's motions in limine on government knowledge, implied attorney approval, and witnesses' post-hoc understanding, below.

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[1] The government contends that, if I allow defendants to testify about their beliefs, I should issue a limiting instruction to the jury to prevent it from thinking that defendants might not have committed a CPPC violation in the first place. Depending on the testimony, I might give such an instruction. However, the jury will be told at the outset of the case that the CPPC issue was resolved by the court, and I doubt that the jury will be confused about this issue without a limiting instruction.

3. Evidence or argument inconsistent with the court's ruling that SSSI's cost vouchers were false or that SSSI breached its contracts with the Navy

The government seeks to preclude defendants from presenting evidence or argument contradicting my ruling that SSSI's cost vouchers were false or that SSSI breached its contracts with the Navy. *See Patzer*, 2023 WL 6883637, at *12–14. In their response to the government's motion, defendants do not respond to this argument or suggest that they intend to present evidence or argument along these lines. Accordingly, I will grant this part of the motion.

4. Evidence or argument inconsistent with the court's ruling that SSSI's false vouchers were material to the United States

The government seeks to preclude defendants from presenting evidence or argument that contradicts my prior ruling that, as a matter of law, SSSI's false vouchers were material. *See Patzer*, 2023 WL 6883637, at *14–16. Again, defendants do not propose to present such evidence. However, defendants take issue with the government's argument that evidence of the Navy's knowledge of certain aspects of the subcontract between SSSI and Derco is relevant only to materiality. I will address the parties' arguments about this evidence below, in the context of the government's motion in limine regarding government approval. For now, I will merely confirm that defendants may not present evidence at trial for the sole purpose of arguing that the CPPC violation was not material.

5. Evidence or argument inconsistent with the court's ruling that Robert Schulman made a false statement to DCMA

At the summary-judgment stage, I found that SSSI's Robert Schulman falsely told the Defense Contract Management Agency ("DCMA") that Derco sold to SSSI at firm-fixed prices. *Patzer*, 2023 WL 6883637, at *21–22. The government moves to

preclude defendants from presenting evidence or argument that contradicts this finding. However, defendants do not propose to present any such evidence or argument. To the extent defendants intend to present evidence or argument that Schulman did not *believe* that his statement was false, I will allow them to do so for the same reasons I gave above in the context of the government's similar motion regarding CPPC evidence.

6. Evidence or argument inconsistent with the court's damages rulings

The government next moves to exclude certain evidence that it regards as inconsistent with my summary-judgment rulings on the measure or damages, *see Patzer*, 2023 WL 6883637, at *24–29, and my related rulings that expand upon the damages issues, *see* ECF Nos. 329 & 357. Under these rulings, the jury will be instructed that the measure of damages for the government's contract and FCA claims is the difference between what the government paid under the vouchers and what SSSI could have recovered under *quantum meruit* had it disclosed the CPPC violation. *Patzer*, 2023 WL 6883637, at *25. Moreover, I previously rejected defendants' argument that the measure of damages should be determined by asking whether the "prices" Derco charged to SSSI were "reasonable." *Id.* at 27. Instead of determining whether Derco's prices were reasonable, the jury will be tasked with valuing the elements of Derco's performance that are properly allocable to the parts-and-materials contract line items ("CLINs"). *Id.* Under my prior rulings, those aspects of Derco's performance that are properly allocable to the parts-and-materials CLINs are the parts themselves (valued at the price that Derco paid to acquire them) and any services that Derco performed in addition to its on-site support services. Because the value of the parts are

not in dispute, as a practical matter the jury's main task with respect to damages will be to determine the value of Derco's non-on-site support services, which I previously identified as the following to the extent they were not performed by on-site staff: (1) identifying sources of components and qualified vendors; (2) order-processing services performed by accounting staff; (3) receiving and paying vendor invoices; and (4) evaluating the performance of Derco's suppliers. (ECF No. 357 at 8; ECF No. 358 at 33–39.)

The government first contends that evidence regarding the Defense Contract Audit Agency's ("DCAA") audit of SSSI's 2007 incurred costs is inadmissible with respect to damages.[2] In prior orders, I provided background facts about the DCAA audit and its relationship to damages. *See Patzer*, 2023 WL 6883637, at *9–10, 28 & ECF No. 358 at 12–14. Here, the most relevant aspect of the audit is that it generated an interim report (ECF No. 241-78) in which a DCAA auditor concluded that those of SSSI's costs that consisted of its payments to Derco for parts and materials were "allowable." Under the Federal Acquisition Regulation ("FAR"), a cost is allowable only if it is "reasonable." 48 C.F.R. § 31.201-2(a)(1). Thus, the auditor's finding of allowability implies a finding of reasonableness. In prior proceedings, defendants argued that this finding of reasonableness implies that the actual prices that Derco charged to SSSI under the CPPC contract represented the fair market value of the goods and services that Derco provided, and that therefore SSSI would have been entitled to recover in

[2] The government separately contends that the same evidence is inadmissible with respect to scienter. I address this aspect of the government's argument in my discussion of the government's motion in limine concerning government approval, below.

quantum meruit the entire amount that the government already paid under the vouchers.

I rejected defendants' argument when they offered it as a reason for granting them summary judgment as to damages. *Patzer*, 2023 WL 6883637, at *28. But that ruling does not necessarily preclude defendants from using the DCAA report as evidence of the value of Derco's services. Defendants now contend that the report is admissible because the auditor's reasonableness conclusion was based on her finding that Derco's "markup" on parts was "in line with market rates." (ECF No. 386 at 21 of 27.) Thus, defendants contend, the auditor's conclusion supports a finding that the fair market value of Derco's goods and services equals the price that Derco charged under the CPPC contract.

Defendants' argument would have some force if the issue for the jury were whether the price Derco charged for parts and materials was reasonable. But, as I have explained, that is not the question. *Patzer*, 2023 WL 6883637, at *27. The CPPC violation voided Derco's prices, and the jury's task is to place a value on those of Derco's services that are properly allocable to the parts-and-materials CLINs. *Id.* The auditor's conclusion about the market price for aircraft parts and materials is not relevant to this question. The auditor did not parcel out the four types of Derco's services that are recoverable in *quantum meruit* and assign a value to them. Nor does the report provide grounds for extrapolating the value of those specific services from the auditor's finding that Derco's overall prices were in line with market rates. Thus, the report is not relevant to damages.

Even if the report had some relevance to damages, I would conclude that its probative value is substantially outweighed by the danger of confusing the issues and misleading the jury. *See* Fed. R. Evid. 403. For the reasons just stated, to the extent the report is relevant to the value of Derco's properly allocable services at all, its relevance is extremely attenuated. On the other hand, the danger that the report will mislead the jury is great. I will instruct the jury to place a value on Derco's specific services, not to determine whether the price Derco charged under the CPPC contract was reasonable. The jury would understandably be confused if, contrary to this instruction, defendants repeatedly argued that the government suffered no damages because a DCAA auditor once concluded that the price Derco charged under the CPPC contract was reasonable. Accordingly, I will preclude defendants from presenting evidence or argument that the DCAA auditor's implicit finding of price reasonableness is relevant to SSSI's hypothetical *quantum meruit* claim.

The government next contends that defendants should be precluded from arguing that Derco's prices were reasonable because they were allegedly based on Derco's indirect rates and a reasonable profit. Again, to the extent that defendants intend to argue that Derco's *prices* were reasonable, I will preclude them from doing so because the reasonableness of Derco's overall prices is irrelevant and such evidence presents a great danger of confusing the issues and misleading the jury. *See* Fed. R. Evid. 402 & 403. However, I previously ruled that Derco's indirect costs are relevant because they may represent the value of the procurement services that are properly allocable to the parts-and-materials CLINs. *Patzer*, 2023 WL 6883637, at *27; ECF No. 329 at 5; ECF No. 370 at 8.) Thus, I will allow evidence and argument about Derco's

indirect costs to the extent that such evidence or argument is designed to place a value on those specific services, rather than to establish that Derco's overall prices were reasonable.

Next, the government seeks to preclude defendants from offering evidence or argument that Derco's services fulfilled SSSI's obligation to provide on-site support or that any services performed by on-site staff are includable in the *quantum meruit* recovery, which would contradict my prior rulings that on-site services are not recoverable in *quantum meruit*. *See Patzer*, 2023 WL 6883637, at *26–27. Defendants state that they do not intend to offer any such evidence or argument, but they note that they should be allowed to provide evidence about on-site support services to the extent that it is relevant to other issues, such as the ways in which on-site employees aided other Derco employees whose services are allocable to the parts-and-materials CLINs. I agree with defendants and will not exclude evidence of on-site services provided that the evidence is not offered for the sole purpose of arguing that on-site services are recoverable in *quantum meruit*.

Finally, the government seeks to preclude defendants from offering evidence that Derco's on-site buyers did not implement the "evil" of CPPC contracting by "pay[ing] liberally" for parts because higher parts costs meant higher profits to Derco. *Muschany v. United States*, 324 U.S. 49, 61–62 (1945). As I previously noted, CPPC contracts are illegal whether or not the contractor acts on its incentive to drive up the government's costs. *Patzer*, 571 F. Supp. 3d at 989 n.6. For this reason, the government's damages are not measured as the amount of cost inflation proximately caused by the CPPC violation. *Patzer*, 2023 WL 6883637, at *25. In general, then, evidence tending to show

either that Derco acted on its incentive to inflate costs or did not so act is irrelevant to damages. However, defendants contend that evidence that Derco did not seek out higher prices remains relevant for two reasons: (1) to rebut any argument by the government that defendants inflated the Navy's costs, and (2) to support defendants' argument that Derco provided value to the government by having its procurement team seek out the best values for the Navy.

I agree that the evidence is relevant to these issues. Evidence about Derco's parts procurement process is relevant to the value of those services. Although it is true that any procurement work performed by on-site personnel must be excluded from the *quantum meruit* claim, evidence that Derco in general sought to obtain favorable pricing is relevant to valuing those of Derco's procurement services that are allocable to the parts-and-materials CLINs. Accordingly, I will not preclude defendants from presenting evidence or argument about Derco's bargain hunting.

B. Motion to Exclude Evidence or Argument Regarding Irrelevant and/or Prejudicial Issues: (1) False Claims Act Treble Damages and Penalties Provisions; (2) Lack of Criminal Prosecution; (3) Dismissal of Sikorsky Aircraft Corporation; and (4) Defendants' Affirmative Defenses

Defendants do not oppose this motion. Accordingly, it will be granted and evidence or argument concerning the following topics will be excluded: (1) The fact that the FCA allows for treble damages and statutory penalties; (2) the absence of any criminal prosecution arising from the conduct at issue in this case; (3) the fact that the Department of Justice brought FCA claims against Sikorsky Aircraft Corporation and that those claims were dismissed; and (4) the affirmative defenses that defendants pleaded in their answers, specifically (a) waiver and ratification, (b) accord and

satisfaction, (c) course of performance, (d) setoff, (e) mitigation of damages, (f) laches, and (g) statute of limitations.

C. Motion Regarding Defendants' Arguments Concerning Government Approval

In this motion, the government seeks to exclude all evidence suggesting that personnel from four different federal agencies "approved" SSSI and Derco's CPPC subcontract. Of course, the agencies had no authority to approve a CPPC arrangement, *see Patzer*, 2023 WL 6883637, at *13, 14–15, and defendants do not have evidence suggesting that a government agency knew that the subcontract violated the prohibition on CPPC contracting but allowed SSSI and Derco to operate under it anyway. For this reason, describing the evidence at issue as evidence of government "approval" of a CPPC violation is misleading. The evidence is more properly characterized as evidence suggesting that the government had knowledge of the aspects of the subcontract that made it CPPC but failed to recognize its CPPC nature. I described such evidence in detail in a prior order. *See id.* at *7–10, 18–20. In that order, I also found that the government's knowledge was not relevant to the materiality of defendants' implied false statements, *id.* at *14–16, and that defendants' evidence of government knowledge did not entitle them to summary judgment on scienter, *id.* at *18–20.

In the present motion, the government contends that defendants' evidence of government knowledge is not even relevant to scienter. However, I conclude that the evidence is relevant to scienter in two ways. First, evidence that government agencies were aware that Derco set its prices to SSSI by adding a 32% markup to the cost of each part is evidence that defendants did not try to conceal this fact from the government. If defendants did not try to conceal this fact, then it is less likely that they

knew their pricing structure violated the prohibition on CPPC contracting and were hoping to trick the government into paying for the parts anyway. Even the knowledge of government employees who had no understanding of federal procurement rules, such as employees of CNATRA, is relevant to scienter for this reason. Although CNATRA had no authority to approve payments for the parts, a defendant who intends to defraud the government is unlikely to disclose the illegal aspect of its contract to *anyone* in the government, or so the jury could reasonably think.[3]

Second, evidence of government knowledge is relevant to scienter to the extent that it supports defendants' argument that their failure to recognize that the subcontract was CPPC was not due to deliberate ignorance or recklessness. Here is where the DCAA audit report, which I discussed above, becomes relevant. The DCAA should have been able to recognize an obvious CPPC violation, even if it was not necessarily looking for one. So the fact that a trained auditor reviewed Derco's pricing as part of her review of SSSI's incurred costs and did not spot the CPPC violation is evidence that the violation was not obvious. And if the violation was not obvious, then the jury could reasonably infer that defendants' own failure to recognize the CPPC violation was not the product of deliberate ignorance or recklessness. Thus, the DCAA audit report, and evidence that DCMA—another agency with accounting and regulatory expertise—failed to detect the CPPC violation is highly relevant to scienter.

[3] Some of defendants' evidence consists of internal communications among government employees about Derco's pricing. Although defendants might not have been privy to these internal communications, the communications are relevant to the extent they disclose what defendants might have told government employees. Further, the jury could reasonably construe internal communications about the government's awareness of a fact as evidence corroborating defendants' testimony that they did not try to conceal that fact.

To be sure, the government might be able to point to reasons why DCAA and DCMA did not detect the CPPC violation, even though it should have been obvious to the parties that negotiated the contract. For example, SSSI's Robert Schulman falsely told a DCMA official in response to his inquiry about Derco's markup that Derco sold at firm-fixed prices. *Patzer*, 2023 WL 6883637, at *23. Likewise, DCAA might have been misled by defendants' representation that Derco sold at firm-fixed prices. *Id.* at *28. But reasons such as these go to the weight of defendants' evidence rather than admissibility. Although allowing defendants to present their evidence and forcing the government to rebut it may be time consuming and may challenge the jury's understanding of the facts, the evidence cannot be excluded under Rule 403. The evidence of government knowledge is highly relevant to scienter, and requiring juries to decide between competing views of the same evidence is what trials are for.

Before leaving this topic, I address the government's reliance on *United States ex rel. Durcholz v. FKW Inc.*, 189 F.3d 542 (7th Cir. 1999). That case involved a form of government-knowledge defense that turned on the government's giving the defendant advance approval to submit what would otherwise be regarded as a false claim. *Id.* at 544–45. At the summary-judgment stage, I rejected defendants' attempt to establish that form of the government-knowledge defense. I concluded that defendants' evidence did not establish that government officials with authority to approve the subcontract authorized defendants to enter into a CPPC subcontract. *Patzer*, 2023 WL 6883637, at *18–20. The government now contends that evidence of its own knowledge could be relevant to scienter only if it established the form of government-knowledge defense at issue in *FKW*. But that is not so. At this point, defendants are not technically trying to

establish a government-knowledge defense at all. Instead, defendants intend to show that the government's awareness of certain facts and its failure to detect the CPPC violation corroborates their own testimony that they did not intend to trick the government into paying invoices that were based on CPPC contracting and did not act recklessly in failing to recognize the CPPC violation. Nothing in *FKW* suggests that evidence of government knowledge cannot be used for this purpose unless it also establishes that the government formally sanctioned the defendants' illegal conduct.

Accordingly, the government's motion regarding defendants' arguments concerning government approval will be denied.

D. Motion Regarding Implied Attorney Approval and Purported Belief in Legality

The government moves to bar defendants from offering certain categories of evidence on the ground that they implicate an advice-of-counsel defense that defendants disclaimed in earlier proceedings. During discovery, the government filed a motion to compel the disclosure of certain communications that defendants had withheld based on the attorney-client privilege. The government argued that, by asserting a good-faith belief in the legality of their conduct, defendants placed the advice they may have received from counsel at issue in this litigation, thereby waiving the privilege. This argument implicated a form of waiver of the attorney-client privilege known as at-issue waiver, which occurs when "the client asserts a claim or defense, and attempts to prove that claim or defense by disclosing or describing an attorney client communication." *Rhone-Poulenc Rorer Inc. v. Home Indem. Co.*, 32 F.3d 851, 863 (3d Cir. 1994) I denied the government's motion to compel, finding that defendants had not asserted an advice-of-counsel defense and did not appear to be offering any evidence

for the purpose of showing that an employee had a good-faith belief that SSSI's and Derco's conduct was legal. *See United States ex rel. Patzer v. Sikorsky Aircraft Corp.*, 575 F. Supp. 3d 1032 (E.D. Wis. 2021). Thus, the government was not permitted to take discovery about the advice defendants may have received from counsel. Because defendants disclaimed an advice-of-counsel defense during discovery, they may not pursue such a defense at trial. And indeed, defendants continue to represent that they will not present an advice-of-counsel defense at trial. That is, their witnesses will not testify that they relied on advice from an attorney to conclude that Derco's pricing was legal. (ECF No. 388 at 4 of 14.)

But the government's motion in limine seeks to do more than preclude defendants from presenting an advice-of-counsel defense. The government contends that, under the doctrine of at-issue waiver, defendants should also be precluded from presenting evidence or argument that falls into one of the following categories: (1) evidence or argument that *implies* that an attorney had approved of their conduct, and (2) evidence or argument that defendants' employees believed in good faith that Derco's pricing complied with the law.

As to the first category, Defendants concede that they may not present evidence implying that an attorney had approved of their conduct, and they state that they will not do so. (ECF No. 388 at 4 of 14.) However, defendants contend that they may have non-attorney employees testify about "review or approval" of their pricing arrangement by Sikorsky's "compliance personnel." (*Id.* at 5 of 14.) But defendants concede that "some attorneys work in Sikorsky's compliance department" (*id.* at 6 of 14), and in any event the jurors would likely assume that a corporate compliance department was staffed by

attorneys. Thus, the jury could be misled into thinking that attorney communications factored into the advice that defendants' witnesses received from that department. Even if the approval was communicated to the contract's negotiators by a non-lawyer in the compliance department, it is possible that the non-lawyer's advice was based on an attorney's advice to the non-lawyer. In that event, the approval would have been based on an attorney's legal advice to the corporation as a whole, and defendants' reliance on such approval would indirectly raise an advice-of-counsel defense.[4]

Still, testimony by witnesses about advice received from non-lawyer compliance personnel may be admissible if defendants establish a foundation showing that the non-lawyer has relevant expertise that is not based on advice received from the corporation's attorneys. In other words, defendants may offer testimony that would not cause a reasonable jury to think that the advice was based on *legal* advice. For example, an employee with accounting expertise who works in the compliance department may provide advice from an accounting perspective. However, testimony about approval from unidentified employees in "Sikorsky government compliance" is not admissible because it implies approval by counsel. Thus, for example, defendants cannot present the testimony of one Derco employee (Peter Winkler) regarding his

[4] Defendants assert that they may testify about the general conclusions of attorneys without waiving the privilege, and they cite two district-court cases that declined to find a waiver when such general conclusions were disclosed. *See Strohbehn v. Access Grp.*, No. 16-CV-985-JPS, 2017 U.S. Dist. LEXIS 121187 (E.D. Wis. Aug, 2, 2017); *Robinson v. Morgan Stanley*, No. 06 C 5158, 2010 U.S. Dist. LEXIS 25072 (N.D. Ill. March 17, 2010). But these cases did not address at-issue waiver; they addressed a different form of waiver that applies when a client partially discloses a privileged communication outside of court. The cases do not hold that a party may *rely* on the attorney's general conclusion *to support a claim or defense* without waiving the privilege. Indeed, because such a holding would eviscerate the at-issue waiver doctrine, I would not follow those cases even if they did.

"discussions" with others in which he learned that Derco's president (William Ochsner) had "confirmed with Sikorsky government compliance that Derco and SSSI's pricing arrangement was appropriate." (ECF No. 388 at 5–6 of 14.) This testimony implies that the department as a whole—and therefore its attorneys—approved of the arrangement. Without waiving the attorney-client privilege, defendants cannot rely on this evidence.

The government's second category relates to testimony from witnesses about their belief in the legality of their conduct. Here, the government contends that the witnesses cannot testify about their good-faith belief that the SSSI-Derco subcontract was not CPPC without waiving the attorney-client privilege. To support this argument, the government relies primarily on cases from the Second and Eleventh Circuits implying that a witness waives the attorney-client privilege by testifying that "he thought his actions were legal." *United States v. Bilzerian*, 926 F.2d 1285, 1292 (2d Cir. 1991); *accord Cox v. Adm'r U.S. Steel & Carnegie*, 17 F.3d 1386, 1419 (11th Cir. 1991). These cases reason that such testimony puts the witness's "knowledge of the law and the basis for his understanding of what the law required in issue." *Bilzerian*, 926 F.2d at 1292. The cases state that it would be unfair to the opposing party to allow the witness to testify about his legal knowledge while using the attorney-client privilege to prevent inquiry into potentially relevant legal advice. *Id.*

After *Bilzerian*, *Cox*, and related cases were decided, the Third Circuit decided *Rhone-Poulenc Rorer, Inc. v. Home Indemnity Co.*, 32 F.3d 851 (3d Cir. 1994), which has become an influential case on at-issue waiver. There, the court determined that at-issue waiver should apply only in narrow circumstances where the client attempts to prove a claim or defense "by disclosing or describing an attorney client communication."

Id. at 863. The court rejected the approach of other courts that had expanded at-issue waiver to circumstances in which "the attorney's advice might affect the client's state of mind in a relevant manner." *Id.* The court's reasoning was based on the purpose of the attorney-client privilege, which is to "encourage[] the client to reveal to the lawyer confidences necessary for the lawyer to provide advice and representation." *Id.* at 862. The court recognized that the privilege comes with a cost: evidence that is relevant to a matter at issue will be inadmissible. *Id.* But that cost is outweighed by the interests of justice that the privilege serves. *Id.* Thus, "[r]elevance is not the standard for determining whether or not evidence should be protected from disclosure as privileged, and that remains the case even if one might conclude the facts to be disclosed are vital, highly probative, directly relevant or even go to the heart of an issue." *Id.* at 864. For this reason, the Third Circuit described some of the contrary authority on which the Second Circuit had relied in *Bilzerian* as "dubious." *Id.* Later, the Second Circuit itself recognized this criticism and clarified that, for at-issue waiver to apply, "a party must *rely* on privileged advice from his counsel to make his claim or defense." *In re County of Erie*, 546 F.3d 222, 229 (2d. Cir. 2008).

The Third Circuit's holding in *Rhone-Poulenc* is also designed to allow a client to better predict when the privilege might be waived. 32 F.3d at 863–64. The court reasoned that "certainty and predictability as to the circumstances of a waiver encourage clients to consult with counsel free from the apprehension that the communications will be disclosed without their consent." 32 F.3d at 863–64. In holding that a client does not waive the privilege unless he or she takes the "affirmative step" of

interjecting the attorney's advice into the litigation, the Third Circuit drew a clear line between waiver and non-waiver. *Id.* at 863.

Although the Seventh Circuit has not addressed whether a witness must waive the attorney-client privilege to testify that he or she believed in good faith that the conduct at issue was legal, it has cited *Rhone-Poulenc* with seeming approval. *See Garcia v. Zenith Elecs. Corp.*, 58 F.3d 1171, 1175 n.1 (7th Cir. 1995). Moreover, many district courts in the Seventh Circuit have found *Rhone-Poulenc* persuasive and have chosen to follow it. *See United States ex rel. Derrick v. Roche Diagnostics Corp.*, No. 14 CV 04601, 2019 U.S. Dist. LEXIS 69681, at *4–6 (N.D. Ill. April 24, 2019) (collecting cases). I, too, find *Rhone-Poulenc* persuasive and will apply its holding here. Thus, I conclude that the attorney-client privilege is not waived by defendants' raising an issue to which the advice of counsel is merely relevant. To waive the privilege, defendants must attempt to prove a claim or defense by disclosing or describing an attorney-client communication.

Applying the approach of *Rhone-Poulenc* to the government's second category of evidence, I conclude that defendants' witnesses may testify about their good-faith belief in the legality of their conduct. Such testimony is not based on the advice of counsel, and defendants have not attempted to bolster their claim by disclosing or describing attorney-client communications. Instead of relying on the advice of counsel, the witnesses will claim that they derived their subjective beliefs about the legality of their conduct though their experience in the government-contracting industry. (ECF No. 388 at 11–12 of 14.) Although any advice these witnesses may have received from counsel on this topic would undoubtedly be relevant to the veracity of their testimony,

the privilege protects such relevant evidence from disclosure. In this respect, the privilege operates no differently in this area than in other areas in which the privilege places highly relevant evidence off limits. *See* Note, *Developments in the Law—Privileged Communications*, 98 Harv. L. Rev. 1450, 1642 (1985).

Accordingly, I will mostly deny the government's motion in limine. However, the motion will be granted to the extent that defendants intend to offer evidence that Sikorsky's compliance department approved of the CPPC contract without first establishing that the advice of counsel played no role in such approval.

E. Motion Regarding Witnesses' Post-Hoc Understanding

The government next asks for an advance ruling about how defendants' witnesses may testify about their own understanding of CPPC contracting. The government contends that some witnesses have testified about their current understanding of the CPPC prohibition, even though they did not hold that understanding at the time defendants' vouchers were submitted for payment. The government describes such testimony as "post hoc understandings." It asks for orders: (1) barring defendants from offering any testimony about understandings of law or fact that the witness did not hold at the time SSSI and Derco entered into the CPPC subcontract or submitted false claims, and (2) requiring defendants to lay a foundation for the relevance of any witness testimony regarding their purported understanding of the law or the facts by establishing that such understanding arose before the CPPC contract or the false claims.

In general, I will not make any broad rulings on the admissibility of potential testimony in this area. Obviously, only relevant evidence will be admitted, and testimony

lacking a proper foundation will not be admitted. But the testimony the government discusses could be used in different ways and, depending on context, might be admissible. For example, the government contends that the testimony of Amber Zemek about her current understanding of the CPPC prohibition is inadmissible because she also testified that she was not aware of the prohibition during the time of the alleged fraud. But the cited testimony relates to her explanation of how she used the term "cost" in her prior emails. She testified that, at the time, she was not aware of the potential legal distinction between the terms "actual cost" and "estimated cost" and thus routinely used the term "cost" without differentiating between the two. (Zemek Dep. at 199:18–200:5., ECF No. 173-25.) Once she became aware of the distinction, she began using the term "estimated cost." *Id.* This testimony would be admissible to rebut any argument that Zemek's use of the term "cost" in her prior emails meant "actual costs." Further, the testimony would have an adequate foundation because Zemek would be using her own personal knowledge to explain why she used the words that she chose at the time she authored the emails in question.

Accordingly, the government's motion in limine on this topic will be denied.

F. Motion to Limit Evidence Concerning the Circumstances of the Termination of Markus Heinrich's Employment with Derco Aerospace

In support of its argument that defendants knew they had entered into a CPPC subcontract or were recklessly indifferent to the risk that they had, the government intends to present the testimony of Markus Heinrich, a former Derco employee. Heinrich will testify that, while he was still employed at Derco, he was part of a conversation with Derco's president, William Ochsner, in which the legality of Derco's "markup" was discussed. The conversation occurred after another Derco employee, Phil Bail,

questioned whether the SSSI-Derco subcontract was CPPC. According to Heinrich, Ochsner (who is now deceased) told Heinrich to "serve Bail a cup of shut the fuck up." Ochsner also said that he knew that Derco's markup was "noncompliant" but that, "if the Navy could not figure it out or identify the problem," then the markup was allowable. Ochsner also told Heinrich that he believed the Navy was "too stupid" to figure the markup scheme out. *See Patzer*, 2023 WL 6883637, at *5.

Defendants intend to attack Heinrich's credibility by arguing that he holds a grudge against Derco due to its terminating him in 2012 for violating the company's sexual harassment policy. In prior proceedings, defendants filed records from Derco's human-resources department that describe the sexually charged comments Heinrich allegedly made to his coworkers. (ECF No. 306-1 at 5–7.) Defendants also filed an email authored by human-resources staff that describes Heinrich's behavior on the day of his termination. (*Id.* at 8–9.) The email indicates that Heinrich was extremely upset and hostile. He accused Derco's HR manager, Craig Pielmeier, of behaving unprofessionally and not affording him "due process." Heinrich told Pielmeier that he wished "nothing but personal harm" for him. Heinrich suggested that the termination would hurt his wife, who had a medical condition, because Heinrich would no longer have insurance. Heinrich also: claimed that Pielmeier coerced him into signing certain documents, compared Pielmeier to Hitler and the Nazis, complained about the lack of severance pay, and accused Pielmeier of being sadistic for terminating him a week before Christmas. Although not memorialized in a record, defendants intend to call Pielmeier to testify that Heinrich threatened Derco personnel with physical violence as he was being escorted out of the building.

The government now moves to exclude all evidence about the circumstances surrounding Heinrich's termination other than the fact of the termination itself. Although the government concedes that Heinrich's potential bias as a disgruntled former employee is fair game on cross-examination, it contends that evidence that he was terminated is sufficient to allow the jury to understand that he is potentially biased. Obviously, however, the case for bias is much stronger once evidence of Heinrich's reaction to his termination is considered. According to defendants' evidence, Heinrich did not simply say he disagreed with Derco's decision and then peaceably leave the premises. He adopted a hostile stance and accused Derco of persecuting him, depriving his wife of medical care, and intentionally harming him by firing him a week before Christmas. He also threated to use physical violence. This evidence paints Heinrich as something more than a typical fired employee and suggests that he very likely has an axe to grind and may be willing to commit perjury to harm Derco. Thus, this evidence of bias is highly relevant to Heinrich's credibility.

The government contends that Heinrich's behavior at the time of his termination does not reflect bias against Derco, but bias against Pielmeier personally, who has no personal stake in the litigation. However, Pielmeier acted on behalf of Derco in his dealings with Heinrich, and the jury could reasonably infer that Heinrich's conduct toward Pielmeier reflected animus towards Derco as well, especially since Heinrich threatened to sue Derco over the termination. (ECF No. 306-1 at 8 of 9.) And as a practical matter, a person can't take a hostile stance towards a corporate entity without targeting the human beings that work for the company. No rational person would direct insults at the company logo printed on the front door. The government is free to argue to

the jury that Heinrich's grievance was with Pielmeier personally rather than with the company as a whole, but that argument goes to the weight of the evidence of bias rather than its admissibility.

The government also contends that the evidence of Heinrich's reaction to his termination should be excluded under Rule 403. First, the government contends that there is a risk that the jury will disbelieve Heinrich because of his unsavory character rather than his potential bias. However, while the evidence of bias does paint Heinrich in a bad light, the danger of unfair prejudice stemming from the jury's perception of his character does not substantially outweigh the evidence's probative value. It is simply impossible to convey the magnitude of Heinrich's potential bias without admitting evidence of his exact behavior at the time he was terminated. And as I've said, the evidence is highly probative of Heinrich's credibility. Thus, the risk that the jury will find Heinrich off-putting and disbelieve him for that reason does not tip the Rule 403 balance in the government's favor.

Second, the government contends that if evidence about the circumstances surrounding Heinrich's termination is admitted, the government will be forced to expend significant time rebutting it, which would cause a waste of time for purposes of Rule 403. However, the government does not explain what evidence it would offer in rebuttal. It does not, for example, claim to have witnesses lined up to testify that Heinrich did not engage in the conduct attributed to him on the day of his termination. At most, then, it appears that the rebuttal would consist of Heinrich's denying that he engaged in such conduct or attempting to justify the conduct, which is not likely to add significant time to

the trial. In any event, because the evidence is highly probative of bias, the danger of wasting time does not substantially outweigh the evidence's probative value.

Although evidence of Heinrich's reaction to his termination is admissible, I will exclude evidence regarding the alleged instances of sexual harassment that resulted in his termination. Evidence that Heinrich made inappropriate sexual comments prior to his termination is not probative of bias or any other proper basis for impeaching him. Indeed, defendants state that they do not intend to introduce evidence or testimony about Heinrich's misconduct in the first place (ECF No. 389 at 7–8 of 13), so this issue is likely moot. But defendants do intend to show, without getting into specific instances of the alleged harassment, that Derco terminated Heinrich for violating its sexual harassment policy. The government contends that the reason for Heinrich's termination is irrelevant and unfairly prejudicial. However, while the exact reason for the termination is not necessarily probative of bias, it is not practical to tell the jurors that Heinrich was terminated and reacted poorly to the termination without also telling them why he was terminated. The jurors would undoubtedly speculate about the reason for the termination, and they might even think that he was terminated for complaining about the CPPC violation, which would unfairly prejudice defendants. Thus, so that defendants can provide the proper context for impeaching Heinrich with bias, I will allow them to show that he was terminated because Derco believed that he had violated its sexual harassment policy. But evidence of specific instances of harassing conduct is inadmissible.

Next, the government contends that the HR records describing Heinrich's conduct are inadmissible as hearsay. Defendants do not dispute that the records

themselves are inadmissible for this reason and instead note that they will establish Henrich's conduct by asking him about it on cross-examination and/or having Pielmeier testify about what he observed. (ECF No. 389 at 9 n.6.) Thus, the government's hearsay objection is moot. However, the government contends that admitting extrinsic evidence of bias, including Pielmeier's testimony, will lead to a waste of time. But, as I explained above, the evidence of Heinrich's conduct is highly probative of bias, and therefore its probative value is not substantially outweighed by the danger of wasting time. *See also United States v. Lindemann*, 85 F.3d 1232, 1243 (7th Cir. 1996) (witness bias is not a collateral issue and may be proved using extrinsic evidence).

The remaining issue involving Heinrich is whether defendants may cross-examine him about the circumstances of his termination to show that he engaged in specific instances of untruthful conduct. Defendants represent that they have a good-faith belief that Heinrich made false statements during the investigation into his workplace sexual harassment. According to defendants, Heinrich denied using words and taking actions that multiple other witnesses corroborated, which suggests that his denials were lies. Under Rule 608(b), extrinsic evidence of these alleged lies is not admissible; however, the court may permit cross-examination about the lies if they are probative of the witness's character for untruthfulness. But allowing cross-examination about the exact questions asked and Heinrich's alleged denials would necessarily reveal the acts of sexual harassment of which Heinrich was accused. This poses a substantial danger of unfair prejudice under Rule 403(b) because there is a risk the jury would disregard Heinrich's testimony not because he lied, but because of his character for making inappropriate sexual remarks.

Still, I think a middle ground is possible. Defendants may, on cross-examination, ask Heinrich a single question about whether he lied during Derco's internal investigation into the allegations of sexual harassment made by other Derco employees. Defendants may not go into the details of the questions he was asked and the answers he gave. Further, because defendants may not prove the lies through extrinsic evidence, defendants will be bound by Heinrich's answer. This limited questioning will be sufficient to call Heinrich's character for truthfulness into question but will prevent disclosure of the unfairly prejudicial details of the alleged sexual harassment.

In short, the government's motion to limit evidence concerning Heinrich's termination will largely be denied. The motion will be granted only to the extent that it relates to specific instances of Heinrich's alleged sexual misconduct, and to limiting defendants' inquiry into specific instances of his allegedly untruthful conduct.

II. Defendants' Motions

A. Motion to Exclude Evidence Related to Dismissed, Abandoned, and Unpled Claims

Defendants move to exclude evidence related to claims that the government asserted during earlier phases of this case, but which have since been dismissed or abandoned. The government concedes that evidence relevant only to dismissed and abandoned claims is inadmissible. However, the government contends that some of the same evidence that supported the dismissed and abandoned claims remains relevant to the claims to be tried. I discuss the evidence at issue below. I also address the parties' dispute over whether the government may pursue an FCA claim based on fraudulent inducement against SSSI and Derco at trial.

1. Evidence Relating to Dismissed Claims against SAC

In its *Patzer* complaint,[5] the government alleged two claims against Sikorsky Aircraft Corporation ("SAC"), the parent company of both SSSI and Derco. One claim alleged that SAC was liable for SSSI and Derco's submission of the impliedly false vouchers because SAC had "approved" of its subsidiaries' plan to have Derco add a percentage markup to its costs. (*Patzer* Compl., Count VII.) A second claim alleged that SAC itself made false statements that induced the Navy to award the original prime contract to SSSI. (*Id.*, Count VIII.) Defendants moved for summary judgment on both claims, and I granted that motion. *See Patzer*, 2023 WL 6883637, at *20–21, 24. Defendants seek to preclude the government from presenting evidence relating to the dismissed claims at trial. Although the government agrees that it may not reference the claims against SAC at trial, it contends that some of the evidence underlying those claims is relevant to its remaining claims against SSSI and Derco. I address each category of disputed evidence separately below.

a. Cost Sheet

To support its claims against SAC, the government relied on a "cost sheet" that documented SAC's approval of SSSI's bid for the original prime contract. The cost sheet estimated that the proposal would result in a "margin" of 22% on parts. (ECF No. 241-69.) According to the government, this is evidence of SSSI and Derco's knowledge of wrongdoing because the Navy's solicitation provided that the prime contractor (here,

[5] This case is composed of two lawsuits separately commenced by different relators, Mary Patzer and Peter Cimma. Prior to consolidation, the government filed a complaint in intervention in each case. Thus, there are two operative complaints: the *Patzer* complaint (ECF No. 80 in 11-C-560), and the *Cimma* complaint (ECF No. 39 in 14-C-1381).

SSSI) was not entitled to a profit on materials; instead, the government would reimburse the prime contractor for the cost of materials. But this argument does not make sense because, as the government concedes, the cost sheet reflects that "SSSI *and Derco* expected to make over $11 million in profit on the parts. (ECF No. 381 at 4 of 15 (emphasis added).) Derco was not a party to the prime contract and was not contractually limited to recouping its costs. Instead, as SSSI's parts subcontractor, Derco was entitled to charge SSSI its catalog or market price, which could include profit. (Prime Contract B-5.f, ECF No. 260-1 at 513.) Thus, the cost sheet's reference to a profit on materials is not evidence of wrongdoing by anyone, including SSSI and Derco. Further, as I explained when I granted summary judgment to SAC on the claim involving the cost sheet, its reference to a margin on parts does not imply knowledge of a CPPC violation because prices set legally would still result in an expected margin. *Patzer*, 2023 WL 6883637, at *20. Accordingly, the cost sheet is not relevant to the remaining CPPC claims against SSSI and Derco and is inadmissible at trial. *See* Fed. R. Evid. 402.

b. Evidence that SAC, through Ochsner, "approved" a plan to violate the CPPC prohibition

The government previously argued that SAC was liable for causing SSSI to submit the impliedly false vouchers because there is evidence that William Ochsner—who held executive positions at SAC, SSSI, and Derco—was aware of the CPPC violation or recklessly disregarded the risk that SSSI and Derco had entered into a CPPC subcontract. The government argued that because Ochsner was an officer of SAC, his alleged scienter could be imputed to SAC as well as to SSSI and Derco. I granted summary judgment to SAC on this claim, reasoning that the evidence showed

that Ochsner addressed the alleged CPPC violation in his capacity as an officer of SSSI and/or Derco only. *Patzer*, 2023 WL 6883637, at *20–21.

Defendants now contend that I should preclude the government from arguing to the jury that Ochsner's knowledge implies that SAC approved of the supposed CPPC plan. In its response, the government does not state that it intends to argue that Ochsner's knowledge implies SAC's approval. However, the government notes that it will introduce evidence of Ochsner's knowledge to support its scienter arguments against SSSI and Derco. But defendants never sought to preclude the government from using the Ochsner evidence for this purpose in the first place, and therefore the parties appear to agree on these points. Accordingly, I will grant defendants' motion to the extent that it relates to evidence that SAC approved of the CPPC violation or the related fraud.

The only area of remaining dispute with respect to Ochsner is whether the government may introduce evidence that he was an officer of SAC to show the extent of his motive to engage in fraud. Although the government does not elaborate on how evidence of Ochsner's dual roles relates to his motives, I assume the government intends to argue that Derco's profitability was doubly important to Ochsner—once as an officer of Derco and once as officer of SAC—and that therefore he had extra incentive to approve of or recklessly disregard the CPPC violation. This is enough to make evidence of Ochsner's status as an executive of SAC relevant. Further, the evidence does not pose a substantial danger of unfair prejudice or any of the other concerns listed in Rule 403. The only party who could be unfairly prejudiced by this evidence is SAC, but SAC will not appear on the verdict at all. Defendants contend that the

evidence will lead to jury confusion and wasting time, but I don't see how. The government will introduce evidence of Ochsner's multiple roles to show that he had extra motivation to see Derco profit and therefore was more likely to prevent Derco from acting on Phil Bail's concerns about the potential CPPC violation. Defendants can't dispute that Ochsner was a SAC executive, and Ochsner's motive was already at issue because of the evidence of his reaction to Bail's concerns. Thus, evidence that Ochsner was an officer of SAC is admissible.

c. Statements in SSSI's Proposal

In Count VIII of the *Patzer* complaint, the government alleged that SAC made two false statements in a cover letter accompanying SSSI's proposal to the Navy to be awarded the original prime contract. In a prior opinion, I concluded that the alleged false statements in the cover letter were attributable to SSSI only, and that therefore SAC was entitled to summary judgment on the claim. *Patzer*, 2023 WL 6883637, at *24. Defendants now move to exclude evidence of the two statements on the ground that it is not relevant to the remaining claims against SSSI and Derco. The government contends that evidence of both statements remains relevant.

In the first statement, SSSI represented that it selected the subcontractors mentioned in the proposal, including Derco, through a "careful process modeled after the Navy's prime contractor selection process," and that SSSI did not select affiliated entities, like Derco, "where the best value solution came from another company." (ECF No. 271-70 at 3 of 30.) According to the government, a jury could conclude that this statement is false because SSSI has admitted that it did not engage in any formal solicitation process or bidding before selecting Derco. The government further argues

that, if the jury deems this statement false, the jury may further infer that SSSI was trying to "conceal the terms of its relationship with Derco from the Navy." (ECF No. 381 at 6 of 15.) Although the government doesn't further explain how this inference is relevant, I assume the idea is that, if the jury believes both that the statement was false and that SSSI was trying to hide something, then the jury might also think that SSSI and Derco were trying to hide a CPPC violation that they had not yet committed. Needless to say, this chain of inferences is highly speculative. The government is trying to use a statement that is essentially puffery (the statement means little more than "we selected our subcontractors carefully") to establish scienter for a CPPC violation that occurred several months after the statement was made. To the extent that the statement is even relevant, its probative value would be far outweighed by the need for mini-trials on issues such as whether the statement is false, whether anyone at the Navy understood this statement to mean that SSSI had formally bid all subcontracts, and whether the SSSI executives who wrote or approved the statement hoped that it would prevent the Navy from looking too closely at the SSSI-Derco relationship and discovering the eventual CPPC violation. Accordingly, I will exclude evidence of the first statement under Rules 402 and 403.

In the second statement, SSSI stated that it "agree[d] with all terms, conditions, and provisions included in the solicitation." (ECF No. 241-70 at 3 of 30.) The government contends that this statement is false because one such term or condition was the prohibition on CPPC contracting, and the government believes that defendants intended to violate that prohibition at the time they submitted the proposal. But the statement is not evidence that SSSI intended to commit a CPPC violation at the time. At

most, it shows that SSSI told the government that it agreed not to engage in CPPC contacting. But that fact is not relevant to any matter in dispute at trial. SSSI's defense is not that it mistakenly believed that the prime contract allowed it to enter into a CPPC subcontract. Its defense is that it did not realize that the subcontract was CPPC in the first place. In any event, even if the government needed to prove that SSSI was aware of the CPPC prohibition, it could do so more directly by pointing to the provision in the prime contract that expressly forbids CPPC subcontracting. (Prime Contract p. 562, ECF No. 260-1.) Getting to the same point through the cover letter would waste time, since the prohibition does not appear in the letter and the jury would need to be told how the statement in the letter implies an agreement not to engage in CPPC subcontracting. Further, because the contract contains an express CPPC prohibition, the cover letter would be needlessly cumulative. Accordingly, evidence of the second statement will be excluded under Rule 403.

2. Evidence of Labor Chargebacks

In its complaints, the government alleged that an accounting arrangement between SSSI and Derco known as a chargeback amounted to illegal kickbacks and violated contractual and regulatory provisions that required SSSI to pass any discounts on parts and materials on to the government. In earlier proceedings, I dismissed the kickback claim, *see United States ex rel. Patzer v. Sikorsky Aircraft Corp.*, No. 11-C-0560, 2018 WL 3518518, at *6–7 (E.D. Wis. July 20, 2018), and granted summary judgment to defendants on the discount claim, *Patzer*, 2023 WL 6883637, at *30–31. Defendants move to exclude evidence relating to these claims. The government agrees that evidence that is relevant only to the chargeback claims is inadmissible. However, it

contends that evidence of the existence of the chargeback arrangement itself is admissible to provide the jury with the full picture of how SSSI and Derco carried out their respective roles in the case.

The chargeback arrangement related to the on-site logistics support personnel at the airfields. SSSI and Derco initially intended for Derco to directly employ those workers. However, for various administrative reasons, it turned out to be easier to have the on-site personnel formally designated as SSSI employees and to have SSSI pay their salaries and benefits. Nonetheless, the on-site personnel were supervised by Derco and, for all intents and purposes, were agents of Derco rather than SSSI. Because these employees were carrying out work for which Derco was financially responsible under the subcontract, SSSI and Derco agreed that SSSI would receive a credit equal to the amount of the labor costs against Derco's invoices for parts and materials. This credit took the form of the chargebacks.

At trial, the jury will need to hear about the work of the on-site personnel to understand the subcontractual relationship and to assess damages. Further, the jury will need to know that the on-site personnel were Derco's agents rather than SSSI's, but that ultimately it was SSSI's responsibility under the prime contracts to provide the on-site support services to the Navy in exchange for a fixed price. Although it may technically be possible to have everyone at trial pretend that Derco directly employed the on-site personnel, I conclude that it is better to just present the jury with the actual facts of the SSSI-Derco arrangement. Evidence of those facts is not prejudicial to defendants, and the internal mechanics of how the chargebacks worked is not hard to understand. Thus, although I will preclude the government from arguing or suggesting

that the chargebacks were unlawful in any respect, I will allow the parties to present evidence of SSSI's nominal employment of the on-site personnel and of the chargeback arrangement so that the jury may understand the full context of the relationship among the Navy, SSSI, and Derco.

3. Evidence Relating to Withdrawn Claims

During a pretrial conference, the government stated that it was withdrawing three clams, two of which are relevant here: (1) an FCA claim based on SSSI's Certificates of Final Indirect Costs, and (2) a claim under the Truth in Negotiations Act ("TINA") against SSSI. Defendants have moved to exclude evidence or argument related to these claims, and the government agrees that evidence or argument related solely to those claims is inadmissible. Although the government notes that some of the evidence relating to the TINA claim is relevant to proving scienter on the remaining claims, I do not understand defendants to be arguing that the evidence in question is inadmissible. Thus, defendants' motion will be granted to the extent that the parties may not reference the withdrawn claims, and that evidence of the following is excluded: (1) SSSI's yearly certification that the costs used to calculate its Certified Indirect Cost Rate Proposal were allowable and did not contain any expressly unallowable costs, and (2) the requirement that SSSI disclose and certify its "cost or pricing data" during negotiations for the Bridge Contract.

4. Fraudulent Inducement against SSSI and Derco

Defendants contend that the government recently asserted a new fraud-in-the-inducement claim against SSSI and Derco, and they contend that because the government did not plead or otherwise disclose this claim until after the close of

discovery and the deadline for filing dispositive motions, the government must be precluded from mentioning this claim or presenting evidence to support it at trial. Because I agree that the government is attempting to add a new claim to the case at the eleventh hour, and that allowing it to do so would unfairly prejudice defendants, I will bar the government from presenting the claim at trial.

Courts have recognized promissory fraud, or fraud in the inducement, as a viable theory of FCA liability. *See United States v. Molina Healthcare of Ill., Inc.*, 17 F.4th 732, 740 (7th Cir. 2021). To prove such a claim, the government must show that the defendant made a promise for the purpose of inducing the government to enter into a contract at a time when the defendant knew that it would not perform the promised act. *Id.* at 741. In its *Patzer* complaint, the government included a count (Count VIII), in which it alleged that SAC—but not SSSI or Derco—made false statements to induce the Navy to award the T-34/44 contract to SSSI. (*Patzer* Compl. ¶¶ 113–16.) The alleged false statements that supposedly induced the contract were the two statements from SSSI's cover letter that I discussed above: the statement that SSSI chose its contractors carefully, and the statement that SSSI agreed with all terms and conditions of the solicitation. I granted SAC's motion for summary judgment on this claim, concluding that the statements were not attributable to SAC. *Patzer*, 2023 WL 6883637, at *24. In that order, I specifically noted that although the statements were attributable to SSSI, the government had not brought a claim against SSSI based on the statements made in the cover letter. *Id.* at *24 n.12.

Seemingly in response to my entry of summary judgment on the fraudulent-inducement claim against SAC, the government has recently indicated that it believes it

has brought similar claims against SSSI and Derco. With respect to the original prime contract, the government points to SSSI's statement in its cover letter to the proposal that it agreed with all terms and conditions of the solicitation, and to the prohibition on CPPC subcontracting that was incorporated into the prime contract. The government contends that, at the times that SSSI and Derco made the proposal and signed the contract, they had no intent to comply with the prohibition on CPPC subcontracting. With respect to the Bridge Contract, the government again notes that it contained a prohibition on CPPC subcontracting, and it contends that because SSSI and Derco were already engaged in CPPC subcontracting, they signed the Bridge Contract while intending to violate that prohibition.

For several reasons, defendants were understandably surprised by the government's unveiling of these fraudulent-inducement theories against SSSI and Derco. First, although not required to do so, *see Bartholet v. Reishauer A.G. (Zurich)*, 953 F.2d 1073, 1078 (7th Cir. 1992), the government organized its complaints into counts, and in so doing steered defendants away from interpreting the complaints as containing fraudulent-inducement claims against SSSI and Derco. The only count in which the government mentioned fraudulent inducement was Count VIII of the *Patzer* complaint, which the government brought against SAC only. The government brought separate FCA counts against SSSI and Derco in the *Patzer* and *Cimma* complaints, but none of those counts mentioned fraudulent inducement or alleged that SSSI or Derco defrauded the government by making promises in its contracts with the government that it intended to breach. Rather than alleging that the prime contracts themselves contained fraudulent statements, the government specifically identified the false

statements as: (1) SSSI's vouchers (*Patzer* Compl. ¶¶ 81 & 90; *Cimma* Compl. ¶ 57); (2) Derco's invoices (*Patzer* Compl. ¶ 86; *Cimma* Compl. ¶ 53); (3) Schulman's August 2009 email (*Patzer* Compl. ¶¶ 93–94); and (4) SSSI's CY2006 to CY2012 Certificates of Final Indirect Costs (*Patzer* Compl. ¶¶ 98–99). To be sure, in the *Patzer* complaint, the government also alleged that, at the time the prime contract was executed, "SAC and SSSI had no intention of following" the prohibition on CPPC contracting. (*Patzer* Compl. ¶ 41.) However, the government later used this allegation to support only its fraudulent-inducement count against SAC. (*Id.* ¶ 114.b.)

In light of the government's misleading pleading choices, defendants understandably did not construe the complaint as alleging fraudulent-inducement claims against SSSI and Derco until the government first raised this possibility after the close of discovery and the deadline for filing dispositive motions. Because allowing the government to recharacterize the complaint on the eve of trial would unfairly prejudice defendants, I will not allow it. *See Chessie Logistics Co. v. Krinos Holdings, Inc.*, 867 F.3d 852, 859 (7th Cir. 2017) (although party is not required to plead legal theories, court may prohibit plaintiff from introducing new legal theories when doing so would unfairly harm defendant or the case's development); *Vidimos, Inc. v. Laser Lab Ltd.*, 99 F.3d 217, 222 (7th Cir. 1996) (same).

Second, the government compounded its misleading pleading choices through its statements made at pretrial conferences and its response to defendants' motions for summary judgment. After the close of discovery, I held two pretrial conferences for the purpose of enabling defendants to identify the claims and legal theories that the government intended to pursue at trial. I scheduled these conferences after the parties

filed briefs raising disputes over the procedures for filing motions for summary judgment. *See generally* ECF Nos. 224 to 231. The first conference was held telephonically, and the minutes of that conference (ECF No. 230) briefly summarized the discussion. The minutes reflect that the government stated it would pursue, among other claims, "FCA claims based on CPPC contracting based on fraudulent inducement and submission of claims for payment." However, the minutes do not identify the defendant or defendants to the fraudulent-inducement claim and thus did not alert defendants or the court that the government intended to pursue not just the fraudulent-inducement claim against SAC pleaded in Count VIII of the *Patzer* complaint, but also fraudulent-inducement claims against SSSI and Derco that were not pleaded in any count of any complaint. The minutes also state that "[a]t the court's suggestion, the parties agreed to an in-person conference at which the government will more precisely identify the claims and issues it intends to try and the claims/legal theories that can be dismissed without additional motion practice." At this later conference, the government presented the court and defendants with a statement of the claims it intended to pursue and of those that it was abandoning. That statement is attached to the minutes of the conference. (ECF No. 231 at 3.) As is relevant here, the government stated that it would pursue "False Claims Act claims against Sikorsky Aircraft Corporation, Sikorsky Support Services, Inc., and Derco Aerospace, Inc. based on illegal cost-plus-a-percentage-of cost subcontracting." (*Id.*) But the statement did not specifically mention a fraudulent-inducement claim against any party.

Following the conferences, defendants filed a motion for summary judgment "on all causes of action brought under the False Claims Act to the extent they are

predicated on alleged violations of the prohibition on cost-plus-a-percentage-of-cost contracting." (ECF No. 232 at 1.) Defendants then specified the counts of the *Patzer* and *Cimma* complaints that the motion targeted, which were every last FCA count relating to CPPC contracting that the government had alleged against SSSI, Derco, and/or SAC but had not withdrawn at the pretrial conference. (*Id.*) Defendants' brief in support of the motion included arguments for granting summary judgment on the governments' fraudulent-inducement claim against SAC. (ECF No. 233 at 34–39 of 40.) Although the brief did not mention a fraudulent-inducement claim against SSSI or Derco, that was because the government had not pleaded such a claim in any count of its complaint and did not mention such a claim at the pretrial conferences. When the government filed its brief in opposition to the motion for summary judgment, it again did not mention such a claim. Nor did it argue that even if the court granted summary judgment on every last FCA count in the complaints, as requested in defendants' motion, the government would still be entitled to proceed to trial on fraudulent-inducement claims against SSSI and Derco. In deciding the motion for summary judgment on all FCA claims, I expressly noted that the government had not asserted a fraudulent-inducement claim against SSSI, *Patzer*, 2023 WL 6883637, at *12, and I had no reason to think that the government intended to pursue such a claim against Derco.

Had the government mentioned its supposed fraudulent-inducement claims against SSSI and Derco in response to defendants' motion for summary judgment, defendants surely would have moved for summary judgment on those claims, too. Indeed, some of the arguments that defendants developed for granting summary judgment on the fraudulent-inducement claim against SAC could have been applied to

the same claims against SSSI and Derco. But at this point, the trial is only three weeks away, and it's not possible to resolve a fresh motion for summary judgment on the government's new claims without postponing the trial, which would lead to undue delay. So allowing the government to pursue the claims at trial would effectively deprive defendants of their procedural right to move for summary judgment. And it would unfairly prejudice defendants to have to defend against claims at trial that the government did not clearly plead and did not explicitly mention at any time during discovery, during pretrial conferences held for the express purpose of identifying the claims to be pursued at trial, or during briefing on motions for summary judgment. *See Aldridge v. Forest River, Inc.*, 635 F.3d 870, 875 (7th Cir. 2011) (district court has discretion to grant motion in limine that prevents party from raising a new legal theory on the eve of trial). Accordingly, the government may not pursue fraudulent-inducement claims against SSSI or Derco at trial.

B. Motion to Exclude Evidence or Argument Related to Relator Patzer's Retaliation Claim

Mary Patzer is the relator who initiated this action in 2011. In the original complaint, she alleged that Derco applied a markup to parts procured under the SSSI-Derco subcontract in violation of government regulations and its own disclosure statements, which provided that Derco could not sell material to an affiliate at "price"—that is, with profit added rather than at cost—unless the material was "commercial." *See* FAR 31.205-26(e). Patzer also alleged that Derco fired her because she told her superiors about her concerns, in violation of the FCA's anti-retaliation provision. 31 U.S.C. § 3730(h)(1). In a prior order, I denied Derco's motion for summary judgment on the retaliation claim. *United States ex rel. Patzer v. Sikorsky Aircraft Corp.*, No. 11-C-

0560, 2023 WL 6880605 (E.D. Wis. Oct. 17, 2023). Patzer and Derco later settled this claim, and I dismissed it at their request. Defendants now move to preclude the government from presenting evidence or argument related to the retaliation claim. They contend that the retaliation claim is irrelevant to the CPPC issues remaining in the case, and that any probative value would be substantially outweighed by the danger of unfair prejudice, confusing the issues, and wasting time. The government does not oppose the exclusion of evidence that Patzer asserted a retaliation claim or that it was resolved. However, the government argues that I should not exclude evidence of (1) Patzer's supposed "warnings" regarding CPPC contracting and Derco's pricing, (2) defendants' failure to respond to her warnings; and (3) the fact that Derco fired Patzer after she raised her concerns. The government contends that such evidence is relevant to scienter.

Initially, it is important to note that Patzer's pre-termination warnings did not relate to the CPPC issues that will be tried. Instead, they related to a separate compliance issue that the government has not pursued in this case, namely, the commerciality issue mentioned above and discussed in detail in my order denying summary judgment on the retaliation claim. *Patzer*, 2023 WL 6880605, at *1–2. Although Patzer wrote an email prior to her termination in which she mentioned that CPPC contracts are illegal (ECF No. 287-6 at 3), Patzer never "warned" anyone that she thought the SSSI-Derco subcontract was CPPC. Patzer's email mentioning the illegality of CPPC contracting does not even explain what CPPC contracting consists of, much less give the opinion that Derco may have violated the rule prohibiting such contracting. Patzer simply interjected the CPPC statement as an aside while answering

a colleague's question about a different matter. In her own declaration, Patzer stated that her conversation with this colleague "reminded" her of a conversation she had with Phil Bail, in which he expressed his concern that the SSSI-Derco subcontract might be CPPC. (Patzer Decl. ¶ 14, ECF No. 287.) But Patzer goes on to state that she "did not specifically mention concerns about CPPC contracting" to anyone. (*Id.* ¶ 28.)

It is also important to note that Patzer did not have an airtight retaliation claim. Although I denied summary judgment on the claim, that was only because it was *possible* for a reasonable jury to find that she was terminated for raising the commerciality issue. Patzer was terminated as part of a reduction-in-force, and Derco provided legitimate, non-retaliatory reasons for including her in the reduction, namely, that she had poor interpersonal skills and Derco was moving away from government work and no longer required her expertise in government accounting. Although I concluded that circumstantial evidence would allow a reasonable jury to conclude that these reasons were pretextual, Patzer did not have a smoking gun, and a jury could have easily concluded that the termination was not retaliatory.

Because Patzer's warnings and retaliation claim related to a non-CPPC compliance issue and the evidence of retaliation is not strong, evidence relating to the alleged retaliation is not probative of defendants' scienter. The government's relevance argument seems to be that because a jury could find that Derco ignored Patzer's warnings about an unrelated compliance issue and then fired her for raising the red flag, it is more likely that Derco also recklessly ignored Phil Bail's warnings about the potential CPPC violation. The argument seems to treat Derco's ignoring Patzer's warning and then firing her as "prior bad acts" under Rule 404(b), in that the

government is suggesting that they show that Derco has a propensity to ignore or cover up compliance issues. But, even if this is not inadmissible character evidence, it is not probative of scienter in the first place because the connection between Patzer's warnings about the commerciality issue and Derco's handling of the CPPC issue is speculative. A company's response to one compliance issue at one time does not imply anything about how it would handle a separate compliance issue at a different time.

In any event, even if evidence that Derco ignored Patzer's unrelated warnings and terminated her for making them were probative of scienter, I would exclude the evidence under Rule 403. For the evidence to have any relevance at all, the government would first have to prove that Derco recklessly ignored Patzer's warnings about the commerciality issue and/or terminated her for making them.[6] *See* Fed. R. Evid. 104(b) ("When the relevance of evidence depends on whether a fact exists, proof must be introduced sufficient to support a finding that the fact does exist."). This would entail not just a mini-trial, but a full-blown trial on the retaliation claim. Obviously, trying the retaliation claim would delay the trial of the CPPC issue and waste time. Not only would the government have to introduce evidence of retaliation and Derco's alleged indifference to her warnings, but defendants would then have to rebut the claim by introducing evidence of its legitimate reasons for terminating Patzer and show that it did not recklessly ignore her concerns about commerciality. Moreover, because the retaliation claim depends on the commercial-item compliance issue, trying that claim

[6] In my summary-judgment decision on the retaliation claim, I wrote that Derco did not respond to certain of Patzer's concerns. *Patzer*, 2023 WL 6880605, at *2–3. But these were not factual findings that Derco "ignored" Patzer's warnings. Rather, at summary judgment, I had to state the facts in the light most favorable to the plaintiff. Thus, the government would be required to independently prove at trial that Derco ignored Patzer's warnings.

alongside the CPPC-compliance claim presents a substantial danger of confusing the issues, as these are both complex regulatory issues that lay jurors will struggle to understand. Because the connection between Derco's response to Patzer's unrelated warnings, on the one hand, and its knowledge of the CPPC violation, on the other, is speculative to begin with, any probative value of the retaliation evidence is substantially outweighed by the danger of confusing the issues and wasting time.

Before concluding, I clarify that, by granting defendants' motion in limine, I am not precluding the government from introducing evidence about the CPPC violation itself simply because Patzer used that evidence to support her retaliation claim. Here, I am thinking mainly of an email from Dawn Katucki, who worked in SAC's government-accounting department, in which she advised Derco and SSSI employees that if the SSSI-Derco subcontract did not contain fixed prices and the parties were creating prices on the fly, "then it really might be a cost-plus-percentage of cost situation." (ECF 284-15.) Katucki's email followed a broader conversation about Patzer's commerciality concerns and, for that reason, has some connection to the retaliation claim. Although I am excluding evidence about the retaliation claim, evidence about Katucki's email and the conversation surrounding it is admissible because it relates to defendants' knowledge that the subcontract was CPPC. Likewise, any testimony by Patzer about her involvement in discussions about CPPC contracting—such as her discussions with Katucki and Bail—is admissible for the same reason.

Accordingly, defendants' motion to exclude evidence or argument related to Patzer's retaliation claim will be granted.

C. Motion to Exclude References to the Illegality of Defendants' Conduct

Defendants move to preclude the government from describing the CPPC arrangement as "illegal" conduct. Because I have already determined that defendants violated federal law by entering into such an agreement, it is technically true that defendants engaged in illegal conduct. However, defendants contend that, because the word "illegal" is often used to describe criminal conduct, using that word here would be unfairly prejudicial and have the potential to confuse and mislead the jury by making it seem as though the court had already determined that defendants are criminals. *See* Fed. R. Evid. 403. Defendants propose that the government be limited to using terms such as "prohibited" or "impermissible" to describe the CPPC arrangement.

In general, I agree with defendants that the term "illegal" could be used in prejudicial fashion. Although I have determined that the subcontract violated federal laws prohibiting CPPC contracting, it is possible that the violation was unintentional. The jury's task will be to decide whether defendants intended to violate the rule against CPPC contracting or were recklessly indifferent to the risk that they were violating it. If the government repeatedly describes my CPPC finding as a finding that defendants engaged in illegal conduct, there is a risk that the jury will think that, because defendants have done something illegal, they must have done it on purpose. But whether defendants violated the prohibition on CPPC contracting on purpose is the very issue that the jury must decide, and that decision should be based on the evidence of scienter presented at trial, not on inferences drawn from my prior findings.

Still, for several reasons, I will not enter a pretrial order prohibiting the government from using the term "illegal." First, some of the documentary evidence

already uses the term "illegal" when describing a CPPC arrangement. For example, Mary Patzer advised a colleague working on one of the subcontracts at issue that "Cost plus percentage of Cost pricing is illegal." (ECF No. 287-6. at 3.) The government should be permitted to use the term "illegal" when referring to such evidence. Second, terms and phrases other than "illegal"—such as "unlawful" or "contrary to law"—arguably have the same potential for unfair prejudice, and I do not want to be in the business of policing the government's vocabulary to ensure that it is using the most neutral terms possible. Instead of granting defendants' motion in limine, I will be on the lookout at trial for government rhetoric that strays into unfairly prejudicial territory and will entertain specific objections as they arise. Again, the concern I will guard against is the government's framing its arguments in way that implies that, because the court has already determined that defendants used an illegal or prohibited form of contracting, defendants must have committed fraud or intended to break the law.

D. Motion to Exclude Arguments Addressing Jurors' Interests as Taxpayers

Defendants move to preclude that government from presenting arguments at trial that address the pecuniary interests of jurors as taxpayers. It is well-established that such arguments are improper, *see Moore v. Tuleja*, 546 F.3d 423, 429 (7th Cir. 2008), and the government states that it does not intend to present them and does not oppose defendants' motion. Accordingly, this motion will be granted.

E. Motion to Exclude Certain References to Lockheed Martin Corporation

In 2015, Lockheed Martin Corporation ("LMC") acquired defendant Sikorsky Aircraft Corporation, including SAC's wholly-owned subsidiaries SSSI and Derco. Defendants seek to exclude certain references to LMC, namely: (1) references to its

acquisition or ownership of defendants; (2) references to its financial responsibility for any judgment against defendants, and (3) any argument implying that LMC is an actual or *de facto* defendant. Defendants contend that evidence of these matters is irrelevant and unfairly prejudicial.

The government does not dispute this motion except to the extent that it would prevent it from exploring the potential bias of two witnesses who now work for LMC, Amy Skaar and David Kegley. At the time of the events giving rise to this suit, these witnesses were employed by Derco. Skaar was Derco's Chief Financial Officer and Kegley was Derco's Director of Domestic Logistics. The government contends that it should be allowed to point out that, because LMC is the ultimate parent company of SSSI and Derco, LMC has a financial interest in the testimony of these witnesses, and that therefore the witnesses, who might wish to please their current employer by giving favorable testimony, are potentially biased.

I agree that the potential bias of these witnesses is a permissible area of inquiry. *See Abernathy v. Eastern Ill. R.R. Co.*, 940 F.3d 982, 992 (7th Cir. 2019). Further, the government's pointing to LMC's status as defendants' parent would not be unfairly prejudicial under Rule 403. In discussing unfair prejudice, defendants focus on the jury's possibly perceiving LMC as a "deep pocket." (ECF No. 368 at 7–8 of 9.) But a typical juror is likely to regard both LMC and Sikorsky as equals in this regard, as both are known to the general public as large defense contractors. Because the jurors will already know that defendants were affiliated with Sikorsky, their knowing that defendants are also subsidiaries of LMC will not meaningfully alter their perception of

defendants' financial wherewithal. Further, I will not allow the government to make any arguments based on LMC's size or wealth.[7]

Accordingly, although I will grant defendants' motion to the extent that it applies to evidence or argument unrelated to Skaar and Kegley's potential bias, I will allow the government to ask these witnesses about their employment at LMC and to point out that LMC, as the ultimate parent company of all defendants, has a financial interest in the outcome of this suit.

III. Conclusion

For the reasons stated, **IT IS ORDERED** that the government's motion for jury instructions regarding summary-judgment rulings and to preclude evidence or argument inconsistent with summary-judgment rulings (ECF No. 369) is **GRANTED IN PART** and **DENIED IN PART**.

IT IS FURTHER ORDERED that the government's motion to exclude evidence or argument regarding (1) False Claims Act's treble damages and penalties provisions, (2) lack of criminal prosecution; (3) dismissal of Sikorsky Aircraft Corporation; and (4) defendants' affirmative defenses (ECF No. 371) is **GRANTED**.

IT IS FURTHER ORDERED that the government's motion regarding defendants' arguments concerning government approval (ECF No. 373) is **DENIED**.

[7] In their reply brief, defendants state that LMC has been the subject of protests due to its perceived financial gains from the conflict between Israel and Palestine. But this is the kind of attention that nearly all military contractors receive, and it will be no secret at trial that defendants are military contractors. So again, mentioning LMC will not increase the danger of unfair prejudice that already exists due to Sikorsky's involvement.

IT IS FURTHER ORDERED that the government's motion regarding implied attorney approval and belief in legality (ECF No. 375) is **GRANTED IN PART** and **DENIED IN PART**.

IT IS FURTHER ORDERED that the government's motion regarding witnesses' post-hoc understanding (ECF No. 377) is **DENIED**.

IT IS FURTHER ORDERED that the government's motion to limit evidence concerning the circumstances of the termination of Markus Heinrich's employment with Derco Aerospace (ECF No. 379) is **GRANTED IN PART** and **DENIED IN PART**.

IT IS FURTHER ORDERED that defendants' motion to exclude evidence related to dismissed, abandoned, and unpled claims (ECF No. 359) is **GRANTED IN PART** and **DENIED IN PART**.

IT IS FURTHER ORDERED that defendants' motion to exclude evidence or argument related to Patzer's retaliation claim (ECF No. 361) is **GRANTED**.

IT IS FURTHER ORDERED that defendants' motion to preclude the government from referencing the illegality of defendants' conduct at trial (ECF No. 363) is **DENIED**.

IT IS FURTHER ORDERED that defendants' motion to exclude arguments addressing jurors' interests as taxpayers (ECF No. 365) is **GRANTED**.

FINALLY, IT IS ORDERED that defendants' motion to exclude certain references to Lockheed Martin Corporation (ECF No. 367) is **GRANTED IN PART** and **DENIED IN PART**.

Dated at Milwaukee, Wisconsin, this 18th day of April, 2024.

/s/ Lynn Adelman
LYNN ADELMAN
District Judge