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UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION

UNITED STATES OF AMERICA <i>ex rel.</i>)	No. 04 C 3897
GREG HAMILTON and MICHELE CASEY,)	
)	
Plaintiffs,)	<u>FILED UNDER SEAL</u>
)	
v.)	JURY TRIAL DEMANDED
)	
LEO BURNETT, USA, INC.,)	
)	
Defendant.)	

AMENDED COMPLAINT

1. This is an action by *qui tam* Relators Gregory Hamilton (Hamilton) and Michelle Casey (Casey) against Leo Burnett, USA, Inc. (LBUSA) on behalf of the United States and themselves pursuant to the False Claims Act, 31 U.S.C. §3729 *et seq.* Plaintiffs seek to recover penalties and damages arising from LBUSA's false claims and fraudulent practices on a \$360 million contract for advertising services that the United States Army had awarded in June of 2000. This complaint is based upon non-public information the Relators obtained while employed by LBUSA, their personal observations of the acts and conduct of the defendant, and by non-public information they and their attorneys obtained during the investigation of this matter.

2. Since being awarded the Army advertising contract in June of 2000, LBUSA cheated the government out of more than \$20 million by engaging in fraudulent conduct. First, LBUSA falsely portrayed its internet advertising unit, called ILEO, as a third-party subcontractor when ILEO was actually a department of LBUSA. LBUSA profited both by charging higher subcontractor rates and by passing off its own fees as out-of-pocket subcontractor expenses.

3. Second, LBUSA created a fictional “blended rate” for its government billings and proposals, so that copywriters were billed to the government at the same rate as top executives. Additionally, while the hourly rate charged to the Army was supposed to be a weighted average from employees of both LBUSA and its minority subcontractors, LBUSA inflated its rates by excluding the lower minority rates from its calculations. This resulted in such egregious overbillings that the practice was internally rejected by LBUSA’s outside auditors, as well as by an external consultant hired by LBUSA to review the issue. Not surprisingly, these practices resulted in extraordinary profits for LBUSA, which were well above the industry norm – at taxpayer expense.

I. THE PARTIES

4. Relator Hamilton was an employee of LBUSA or one of its subsidiaries from June 1998 until his termination on June 30, 2004. In Hamilton’s last position with LBUSA, he was a Vice President of LBUSA, with primary responsibility for the finances of LBUSA’s internet advertising unit, ILEO, and LBUSA’s minority Hispanic unit, LA PIZ. Hamilton served in this position from September 2002, through the time ILEO was created as a department within LBUSA in January 2003, until his employment was terminated on June 30, 2004. Prior to the creation of ILEO, Hamilton was a Vice President and Director of Financial Planning & Analysis for LBUSA.

5. Relator Casey was employed at LBUSA from May 1989 until December 2004. Casey’s last position was Vice President and Corporate Controller (from February 2002), with responsibility for the company’s accounting and financial practices. During her tenure at LBUSA, Casey also served as Vice President and Director of Business Analysis & Audit Services (Internal Audit), and as Assistant Treasurer & Associate Director of Corporate Planning.

6. Defendant LBUSA is the wholly owned United States subsidiary of Publicis, a French public company. Publicis acquired LBUSA in September 2002. LBUSA's principal place of business is at 35 W. Wacker Drive, Chicago, Illinois 60601.

II. JURISDICTION AND VENUE

7. These claims arise under 31 U.S.C. § 3729 et seq., known as the "False Claims Act."

8. This Court has jurisdiction pursuant to 31 U.S.C. § 3732(a) and 31 U.S.C. § 3732(b) because this case is brought under 31 U.S.C. § 3730.

9. Venue is proper in this Court under 31 U.S.C. § 3732(a) because LBUSA transacts business in the Northern District of Illinois, and committed a number of the acts proscribed by 31 U.S.C. § 3729 in the Northern District of Illinois.

III. THE FALSE CLAIMS ACT

10. The FCA provides that any person who knowingly submits or causes the submission of a false or fraudulent claim to the government is liable for a civil penalty of up to \$11,000 for each such claim, plus three times the amount of the damages sustained by the government. The Act empowers private persons having information regarding a false or fraudulent claim against the government to bring an action on behalf of the government and to share in any recovery. The complaint must be filed under seal without service on any defendant. The complaint remains under seal while the government conducts an investigation of the allegations in the complaint and determines whether to join the action.

11. Pursuant to the FCA, Relators seeks to recover on behalf of the United States damages and civil penalties arising from defendant's false or fraudulent claims, as well as from

false or fraudulent records or statements that the Defendant used to get a false or fraudulent claim paid by the federal government.

IV. THE BUSINESS OF LBUSA

12. LBUSA is one of the largest advertising agencies in the United States. Founded in 1935 by Leo Burnett in Chicago, Illinois, LBUSA has offices in 84 countries, and employs over 16,000 people worldwide. In 2003, Leo Burnett was ranked by *Advertising Age* as the number six ad agency worldwide, with revenues of approximately \$886 million. Leo Burnett boasts of Disney, Nintendo, McDonald's, Heinz, and Kellogg's among their clients, for whom they produce television, radio, online, and print advertising.

V. THE LBUSA ARMY CONTRACT

13. The Army buys its advertising services from LBUSA. On June 27, 2000, LBUSA and the Army executed their current contract. A copy of the contract is attached as Exhibit A.¹ Linda S. Wolf, the departing CEO of LBUSA signed for the contractor; Kathy J. Dobeck of the Defense Supply Service – Washington (“DSSW”) signed for the government. Ms. Dobeck is the DSSW branch chief for contracts and grants. The contract is administered by the Defense Contract Management Agency (“DCMA,” formerly “DCMC”), in Chicago, located at O’Hare Airport. Many of the payments were made from Defense Finance and Accounting Service (“DFAS”) in Indianapolis.

14. The contract is an “Indefinite-Delivery/Indefinite Quantity (IDIQ) contract.” An IDIQ contract is basically an “agreement to agree,” which commits funds to a particular contract and lists the anticipated needs of the buying command by line item. The line items are essentially

¹ For ease of reference the Contract is Bates numbered, beginning at R0001. These page numbers are referenced below.

a shopping list of what the government intends to buy. If and when the government buyer needs to purchase the item, approvals are already in place for the specific goods or services that the government wants to buy. The specific purchase is then made through a purchase contract called a "Task Order," which specified the services purchased and the price paid.

15. Under the LBUSA contract, the government committed to an estimated minimum amount of purchases (here \$100,000), estimates of future purchases, terms for such future purchases, and a contract maximum. The maximum amount of the LBUSA contract was \$360,000,000, over a four year period (the base year plus three option years), from June 2000 to June 2004. The contract was recently extended for six months.

16. The LBUSA contract lists 12 line items, with multiple sub-items, which were all presented with estimated prices (some on a "not to exceed" or "NTE" basis). The line items fell into three types of expenses: (1) "United States Army Recruiting Advertising Program," (3) "Fixed Price Award Fee," and (2) "Other Direct Expenses."

17. The Advertising Program charges were for services provided by LBUSA. Each of these services was a labor type according to the "Advertising Agency Department," (such as "creative department," "production department," "media planning department," etc.) *See, e.g.*, Ex. A, at R0003-4, R0031-32. Each LBUSA department had a specified labor rate and description of work in the contract. Of the total contract amount, LBUSA was limited to receiving no more than \$82,483,000 for its Advertising Program work.

18. But in addition, while each line item was to be set on a Firm Fixed Price ("FFP") basis, there were also provisions for \$7,372,400 in Fixed Price Award Fees as an incentive fee for

performance. LBUSA routinely received these incentive fees in addition to its Advertising Program fees.

19. The bulk of the contract -- \$300 million dollars -- was to be used for "Other Direct Expenses" (or "ODE"). Other Direct Expenses were LBUSA's purported out-of-pocket costs for outside vendors and contractors engaged to fulfill the Army contract work. The \$300 million in ODE was specifically designed to reimburse LBUSA for its actual costs on a "pass-through" basis. As described in the contract, for Other Direct Expenses LBUSA "will be *reimbursed* for expenses chargeable to a specific task order (i.e. Travel & Per Diem, Reproduction, Graphics, and Media Placement)." (See contract line items 002, 0005, 0008, 0011, at R0006, 11, 15, 19) (emphasis supplied). Major components of Other Direct Expenses were "media buys" (such as purchases of television spots) and subcontractor work.²

20. Under standard practices in the advertising industry, LBUSA treated Other Direct Expenses for private sector customers as "pass-through" costs without mark-up or other profit added. But for Army contracts alone, LBUSA marked-up ILEO work and subcontractor work for additional profits, above and beyond the fees it was already receiving. LBUSA was well-compensated for its own management and other work concerning the subcontracts media buys, and Other Direct Expenses through its agency fees, "Executive Labor" task orders, and other scheduled labor, as well as through incentive fees. While the Army contract specified hourly labor rates for other services, no labor rates are specified for the "Other Direct Expenses."

21. Each advertising project was to be negotiated separately as a "Task Order." The Task Order is a specific agreement with the government that "will contain the final terms

² As contract amounts were on a not-to-exceed basis, the maximum amount of the contract exceeded the combined totals for ODE, Advertising Programs, and Award Fees. Each of these separate components should not have reached

regarding price, performance, delivery and other relevant provisions for each project to be performed.” (Ex. A, at ¶5(a), at p. R0023) If the government wanted services under the contract, it would submit an Advertising Direction Sheet describing the services required. In response, LBUSA would supply a proposal called a Request for Task Order (“RFTO”). The RFTO proposal would provide a detailed description of the project, including “a detailed statement of the proposed hours and expenses.” (*Id.*, at 5(e)(8), at p. R0024) Attachment II to Contract) The total price would include “the total price for in-house labor using the rates identified in the Schedule” [*i.e.* the rates set out in the contract]. (*Id.*, at 5(e)(8)(i), at p. R0024)

22. Accordingly, each RFTO proposal set out the proposed direct labor costs for each of the labor types proposed to complete the task, the amount of time proposed to complete the task, and the proposed price “based upon rates contained in the Schedule.” (Ex. A, Attachment II, p. R0028) In addition, Other Direct Expenses were listed by type and price. The direct labor and indirect labor would be added together for the “Total Price for Task Order.” (*Id.*)

23. Each RFTO and the resultant Task Order were broken down into two categories: scheduled labor and Other Direct Expenses. Under the contract, the “other direct expenses will be identified, negotiated and fixed when a task order is issued.” (Contract Line Item Numbers 002, 0005, 0008, 0011, at R0006, 11, 15, 19)

24. Each RFTO explicitly certified that “PROPOSED PRICES ARE FAIR AND REASONABLE BASED UPON THE LEVEL OF WORK NECESSARY FOR SATISFACTORY PERFORMANCE.” (Ex. A, Attachment II, R. 0028)

the maximum budgeted amounts.

25. Each Task Order was a separate purchase contract between LBUSA and the United States Army. LBUSA was only able to receive payment on the Army contract by obtaining Task Orders, and billing for services rendered under those Task Orders. The Army received separate bills (invoices) for each Task Order, as work was performed on each Task Order.

26. Each bill to the United States separated out “labor” and “other direct expenses.” “Labor” was for LBUSA’s work under the labor rate schedule specified in the contract. “Other Direct Expenses” was for subcontractor and other work described above. In further representing that Other Direct Expenses were “pass-through” costs not subject to further mark-up by LBUSA, the bills described ODE as “Out of Pocket Expenses.”

27. LBUSA represented that each invoice was for work on the Task Order specifically identified on that invoice. The Request for Task Order was also specifically identified on each invoice. In each bill to the United States, LBUSA explicitly and implicitly certified that the services called for in the task order had been rendered per the terms and specifications in the order.

28. Ray DeThorne was the LBUSA Executive Vice President and Account Director for the Army account. Mary Haggerty was the Director of Operations for the Army account.

VI. LBUSA’S ILLEGAL PRACTICES

A. LBUSA Fraudulently Profited by Treating Its ILEO Department as a Subcontractor

29. From the inception of the LBUSA-Army contract in June 2000 until January 2003, LBUSA was regularly using one of its wholly-owned subsidiaries, CAPPS, Inc. to perform certain interactive advertising services pursuant to task orders under the Army contract. The interactive services were being done by a division of CAPPS, called Chemistri. Basically, these interactive

services involved the development, maintenance and oversight of the Army's internet websites, which is a major recruiting tool for the Army.

30. In January 2003, LBUSA undertook a corporate restructuring of CAPPS, Inc. Pursuant to this restructuring, all employees of the CAPPS division known as Chemistri were terminated from Chemistri and hired by LBUSA. As LBUSA employees, they were placed within the Leo Burnett Corporate Group ("LBCG"), which was the direct marketing department within LBUSA. Thereafter, LBUSA changed the name of LBCG to ILEO.

31. Under the restructuring, ILEO had no corporate identity separate from LBUSA. ILEO was simply a department of LBUSA.

32. The decision by LBUSA to dissolve the Chemistri division of CAPPS and hire its employees under LBUSA was made at least as early as November 2002.

33. As of January 2003, all former employees of the Chemistri division of CAPPS became employees of LBUSA. They worked in the LBUSA department known as ILEO. They were treated as LBUSA employees and received all the same benefits as other LBUSA employees. Paychecks to these employees were issued by LBUSA, under LBUSA's taxpayer identification number.

34. As of January 2003, LBUSA controlled all operational and financial matters of ILEO, including its billing, accounts receivable, and cash accounts. All ILEO clients for whom ILEO provided services were considered LBUSA clients. LBUSA typically did not separately bill clients for its work; all billings by ILEO were billed on LBUSA invoices and were collected by LBUSA.

35. Since January 2003, LBUSA knowingly submitted false and fraudulent bills to the United States for services performed by ILEO as if ILEO was a third party independent subcontractor, despite the fact that ILEO was a department of LBUSA and not a separate corporate entity.

36. The work performed by ILEO should have been included as direct labor rather than as other direct expenses. The Army contract contains a specific line item and contract price for LBUSA's "interactive department." (SF 1449 Continuation Sheet, Schedule of Supplies/Services, Item Nos. 0001AL, 0004AL, 0007AL, and 0010AL, at R005, 10, 14, 18) The interactive department included "[a]ll personnel responsible for the planning, execution, and measurement of internet and other interactive or 'new media' programs."

37. By billing ILEO as an independent subcontractor, LBUSA charged the Army a higher rate for work performed by LBUSA employees working in the ILEO department, than was allowed under the Army contract. Services performed by LBUSA/ILEO were billed to the Army at the blended rate of \$180.00 per hour, the rate allowed under the Army contract for outside subcontractors, rather than the rate of \$108.00 per hour specified in the contract for interactive services performed directly by LBUSA. LBUSA charged the higher subcontractor rate even though ILEO was being billed for the sole benefit of LBUSA, which collected and kept the entire payments for ILEO's services.

38. By billing the services of ILEO as if they were being performed by a subcontractor, LBUSA knowingly and deliberately overcharged the Army for these services since at least January 2003 to the present. LBUSA accomplished this by submitting false and fraudulent Requests for Task Orders and invoices to the Army.

39. By billing the services of ILEO as if performed by a subcontractor, LBUSA also benefited from their fraudulent conduct because subcontractor billings were not limited by the \$82 million per year specified in contract line items for LBUSA's own labor. LBUSA circumvented that cap by charging ILEO billings to the \$300 million allotted for "Other Direct Expenses," out of which subcontractors were paid.

40. LBUSA implemented a number of internal corporate policy decisions in order to conceal its deliberate overcharging of ILEO's services from the Army. One such decision was to create a fake paper trail of invoices to make ILEO appear to be an outside contractor. Because ILEO was part of LBUSA, all billing for ILEO services to LBUSA clients ran through LBUSA's main billing system – except with respect to the Army contract. In April 2003 LBUSA senior management instructed Hamilton and other ILEO senior management to create monthly bills for ILEO that were submitted to LBUSA. LBUSA would then use these bills to support LBUSA's invoices to the Army, in the same manner that LBUSA treated legitimate ODE's from real third party subcontractors.

41. Because ILEO used LBUSA's internal mainframe accounting and billing system to handle its billing to all other clients, it did not have its own billing software. To remedy this, senior management at LBUSA instructed Hamilton and other management to use Quickbooks Financial Software to create monthly invoices for submission to LBUSA.

42. From January 2003 to date, LBUSA improperly billed the Army for at least \$7 million for work performed by ILEO.

43. Similarly, LBUSA knowingly submitted false and fraudulent proposals and bills for work performed by CAPPs and its Chemistri division, by treating CAPPs (and its Chemistri

division) as subcontractors when in fact CAPPS was a wholly owned subsidiary of LBUSA. From the beginning of the contract to date, LBUSA has improperly billed the Army for at least \$15 million for work performed by CAPPS and its Chemistri subdivision.

B. LBUSA Fraudulently Inflated its Hourly Billing Rates through “Blended Rate” Billing

44. From the beginning of the contract until 2003, LBUSA submitted false and fraudulent claims by overcharging the government for hourly labor rates. This was accomplished by a “blended rate,” which was a single hourly rate LBUSA charged the government, regardless of whether the work was performed by a top executive or a newly hired copy writer. For the Army contract, LBUSA inflated its blended rates by representing that higher-level employees would perform more work on the contract than they actually would perform. During performance of the contract, LBUSA had lower-level employees do as much work as possible. Typically, for private customers, LBUSA charged its clients labor rates commensurate to its employees’ level of expertise and responsibility.

45. Further, LBUSA also inflated its blended rates by excluding minority subcontractors from its calculations, because the minority subcontractors had lower rates. Including the minority subcontractors in the blended rate calculations would have lowered LBUSA’s hourly rates in the contract.

46. Internally, LBUSA recognized that the blended rates were resulting in egregious overcharges to the Army. Around mid-2003, at the direction of Eric Martinez, LBUSA hired an outside expert in government contracting, Jimmy Jackson, to review the blended rate billings. Jackson concluded that LBUSA had overcharged the government approximately \$2.5 million through the use of blended rate billing (from the inception of the contract to June 2003).

47. Immediately after receiving the report, LBUSA internally classified the \$2.5 million as a liability to the government. It also changed its labor rates to the Army. These corrective actions were directed by Martinez. However, after the \$2.5 million was internally classified as a liability, DeThorne and Haggerty informed Martinez that the \$2.5 million should be classified as income, because they claimed to have a letter the Army approving the charges. The \$2.5 million was then changed from a liability to income.

48. Ernst & Young has been LBUSA's outside auditor throughout the contract period. During the course of its 2003 audit review, the auditors reviewed Jackson's report and investigated the matter. DeThorne and Haggerty could not demonstrate to Ernst & Young that the Army had approved the overcharges, or that LBUSA could legitimately keep the \$2.5 million as income. To the contrary, Ernst & Young concluded that LBUSA should not retain the \$2.5 million it received from the government. Recognizing the seriousness of LBUSA's actions, Ernst & Young took the highly-unusual step of recommending a post-audit journal entry to subtract these funds from LBUSA's revenues.

**COUNT I:
Federal False Claims Act**

49. Relators repeats and realleges paragraphs 1 – 48 above as if fully set forth herein.

50. This is a civil qui tam action brought by Relators on behalf of the United States to recover treble damages and civil penalties under 31 U.S.C. §3729(a) of the False Claims Act.

51. Title 31 U.S.C. §3729(a) provides, in relevant part, liability for any person who-

- (1) knowingly presents, or causes to be presented, to an officer or employee of the United States Government or a member of the Armed Forces of the United States a false or fraudulent claim for payment or approval; or,

- (2) knowingly makes, uses, or causes to be made or used, a false record or statement to get a false or fraudulent claim paid or approved by the Government.

52. LBUSA violated 31 U.S.C. §3729(a) in that it repeatedly, willfully and intentionally presented false claims for payment to the Department of Defense program by and through the actions described herein.

53. LBUSA's false and fraudulent claims, and the false statements and records described above, were material to the government's acceptance of proposals and payments of billings under the Army contract.

54. As a result of LBUSA's violations of 31 U.S.C. §3729(a), the United States has been damaged in an amount in excess of millions of dollars, exclusive of interest.

55. Relators are private persons with direct, personal knowledge of the allegations of this Complaint, who have brought this action pursuant to §3730(b) on behalf of themselves and the United States.

WHEREFORE Relators respectfully request this Court to award the following damages to the following parties, and against LBUSA:

To the UNITED STATES GOVERNMENT:

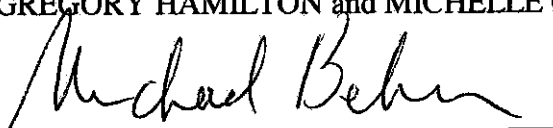
1. Three times the amount of actual damages sustained by the United States Government;
2. A civil penalty of not less than \$5,500 and not more than \$11,000 for each false claim LBUSA submitted to the United States Government;
3. Prejudgment interest and all other applicable interest;
4. Expert witness fees; and
5. All other costs of this action.

To the RELATORS:

1. The maximum amount allowed pursuant to 31 U.S.C. §3730(d);
2. Reimbursement of all expenses Relators incurred in connection with this action;
3. An award of reasonable attorneys' fees;
4. Expert witness fees;
5. All other costs of this action; and
6. Such further relief as this Court deems just and proper.

Respectfully submitted,

UNITED STATES OF AMERICA *ex rel.*
GREGORY HAMILTON and MICHELLE CASEY

By: 
One of Plaintiffs' Attorneys

Date: January 5, 2009

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