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FEATURE COMMENT: 2016 FCA Update

The civil False Claims Act, 31 USCA § 3729 et seq., was originally enacted in 1863 in response to allegations of fraud in Civil War procurements. The FCA has since become the Government's weapon of choice to combat fraud. As Principal Deputy Assistant Attorney General Benjamin Mizer recently stated, "The False Claims Act has again proven to be the government's most effective civil tool to ferret out fraud and return billions to taxpayer-funded programs." Department of Justice Office of Public Affairs, *Justice Department Recovers Over \$3.5 Billion From False Claims Act Cases in Fiscal Year 2015*, Dec. 3, 2015.

This FEATURE COMMENT briefly reviews the basic elements of the FCA, its qui tam provisions and enforcement statistics. It then discusses several recent FCA developments: (1) the U.S. Supreme Court's affirmation of the implied certification theory and a more demanding materiality standard, (2) expanded use of statistical sampling to establish liability in addition to damages, (3) the Supreme Court's rejection of an automatic dismissal rule for seal order violations, and (4) the Government's demonstrated interest in prosecuting individuals and the importance of *Upjohn* warnings.

Basic Elements of the FCA and Qui Tam Provisions—There are various statutory grounds on which a person may violate the FCA. This FEATURE COMMENT focuses on the two most prominent grounds set forth in 31 USCA §§ 3729(a)(1)(A)–(B). The FCA makes it unlawful for a person to knowingly (1) present or cause to be presented to the Government a false or fraudulent claim for pay-

ment, or (2) make or use a false record or statement that is material to a claim for payment. 31 USCA §§ 3729(a)(1)(A)–(B) (2009); *Hooper v. Lockheed Martin Corp.*, 688 F.3d 1037 (9th Cir. 2012); *Harrison v. Westinghouse Savannah River Co.*, 176 F.3d 776 (4th Cir. 1999). A person acts "knowingly" under the FCA if he or she acts with "actual knowledge, deliberate ignorance or reckless disregard of the truth or falsity of information." 31 USCA § 3729(b). Mistakes and ordinary negligence are not actionable. *U.S. v. Science Applications Int'l Corp.*, 626 F.3d 1257 (D.C. Cir. 2010); 653 F. Supp. 2d 87 (D.D.C. 2009).

The FCA provides for up to treble damages and, as of August 1, penalties of between \$10,781.40 and \$21,562.80 per violation (increased from \$5,500 and \$11,000). Violators are also subject to administrative sanctions, including suspension or debarment from participating in Government contracts. The FCA has a lengthy statute of limitations of no less than six years and, in some cases, up to 10 years after a violation has been committed.

The FCA permits private citizens, known as qui tam relators, to bring cases on behalf of the Government. In qui tam cases, the complaint and a written disclosure of all relevant evidence known to the relator must be served on the U.S. attorney general and on the U.S. attorney for the judicial district of the court where the case was filed. The qui tam complaint is then ordered sealed for a period of at least 60 days, and the Government must investigate the allegations and decide whether to intervene. If the Government does not intervene, the relator may proceed with the complaint on behalf of the Government. The complaint must be kept confidential and is not served on the defendant until the seal is lifted. Relators receive between 15 and 25 percent of the recovery if the Government intervenes in a case, and between 25 and 30 percent if the Government declines to intervene.

Hundreds of FCA Cases and Billions of Dollars in Recoveries—Over 700 FCA cases have been filed each year for the last five years, and 85 percent of those have been qui tam cases. DOJ Of-

Office of Public Affairs, *Fraud Statistics Overview*, Nov. 23, 2015. The Government has recovered more than \$23 billion, and, predictably, nearly all of the recoveries came from non-qui tam cases and qui tam cases in which the Government intervened. *Fraud Statistics Overview*, supra.

Escobar and the FCA’s Implied Certification Theory and Materiality Standard—Affirmation of Implied Certification Theory: The Supreme Court’s unanimous decision this past June in *Universal Health Servs., Inc. v. U.S. ex rel. Escobar*, 136 S. Ct. 1989 (2016), affirmed the FCA’s implied certification theory in certain circumstances. The implied certification theory posits that the submission of a claim for payment or approval is treated as an implied certification that the company submitting the claim has complied with all statutory, regulatory and contractual requirements, even if the claim does not contain an express certification of compliance with those requirements, so long as those requirements are material to the claim. Failure to comply with such a requirement makes the claim false or fraudulent.

The Supreme Court explained that the company’s claim for payment made “specific representations” about the services rendered by referencing payment codes that correspond to counseling services performed by designated professionals, but failed to disclose that the persons performing those services were untrained and unlicensed. The Supreme Court explained that such “half-truths—representations that state the truth only so far as it goes, while omitting critical qualifying information—can be actionable misrepresentations” under the FCA.

The Supreme Court’s decision is not an endorsement of the implied certification theory in all circumstances. For example, the decision did not answer the question of whether a straight claim for payment, without half-truths about the contracted-for goods or services, is actionable if there was noncompliance with a statutory, regulatory or contractual requirement. The outer limits of the implied certification theory are therefore still unclear, and the lower courts will continue to assess the theory’s viability on a case-by-case basis.

More Demanding Materiality Standard— Apart from the implied certification theory, the Supreme Court in *Escobar* offered guidance on the FCA’s “materiality” standard. The Court stated that expansive arguments of liability are disfavored, and a “rigorous” and “demanding” fact-based analysis

must be used. The Court added that the FCA is not “a vehicle for punishing garden-variety breaches of contract or regulatory violations,” and “[m]ateriality ... cannot be found where noncompliance is minor or insubstantial.” The Court explained that Government knowledge and course of dealing are highly relevant in assessing materiality, and materiality cannot be legislated:

[I]f the Government pays a particular claim in full despite its actual knowledge that certain requirements were violated, that is very strong evidence that those requirements are not material. Or, if the Government regularly pays a particular type of claim in full despite actual knowledge that certain requirements were violated, and has signaled no change in position, that is strong evidence that the requirements are not material.

The Supreme Court rejected the position that any requirement is material if the company knows that the Government could refuse payment if it were aware of the violation. Materiality should therefore no longer be a “gimme” argument for the Government. However, the recent case of *U.S. ex rel. Rose v. Acad. of Art Univ.*, 2016 WL 5076214 (N.D. Cal. 2016), shows that at least some lower courts will work hard to find materiality.

Rose involved an allegation that a university violated a Department of Education (DOE) regulation that prohibits universities that receive federal funding from making incentive payments to student recruiters. The university moved for summary judgment on grounds that there was no materiality since DOE was aware of the allegation against the university and did not take any action against it, and DOE had a track record of not taking action against other schools that it knew violated the ban.

The court denied the motion for three reasons. First, the court explained that Court of Appeals for the Ninth Circuit precedent holds that compliance with the ban is material and *Escobar* did not disturb that holding. *U.S. ex rel. Hendow v. Univ. of Phoenix*, 461 F.3d 1166 (9th Cir. 2006). Second, the court explained that DOE’s decision not to take action against the university was “not terribly relevant to materiality” because DOE did not cite any reasons for its inaction, and therefore there was no evidence that DOE had actual knowledge of the violation. Third, the court explained that DOE, while not suspending or debarring other universities that it knew violated the ban, took some action against the universities by impos-

ing fines and requiring that the universities make prospective reforms. The court also pointed out that DOE had recently eliminated certain safe harbors and rescinded a memorandum that stated its position that fines, and not suspension or debarment, were the most appropriate sanction for violations of the ban. *Rose* serves as a reminder that *Escobar*'s demanding materiality standard can be challenged by lower courts that are more receptive to pro-Government or plaintiff arguments.

Statistical Sampling to Establish FCA Liability—Statistical sampling refers to the use of a small sample to estimate the characteristics of a larger population reliably. In *U.S. ex rel. Martin v. Life Care Ctrs. of Am., Inc.*, 2014 WL 4816006 (E.D. Tenn. 2014), the court explained that “[i]n the context of the FCA ... statistical sampling has been generally limited to determine damages, rather than liability.” However, the court proceeded to deny a motion for summary judgment in which the company sought to defeat the Government’s use of statistical sampling to establish its liability for a large number of claims. The Government proposed to use a sample of 400 Medicaid claims that were alleged to be medically unnecessary to extrapolate to a universe of 150,000 claims. On this matter of first impression, the court explained that the issue was not whether the Government could identify each of the claims it alleged was false, but rather whether statistical sampling was the most practicable method for doing so:

Considering the evidence and argument before it, the court finds that the government could specify in detail the specific claims ... which it alleges are false, but in order to do so, it would require the devotion of more time and resources than would be practicable for any single case. ... [A]s the government has identified in its response, the purpose of statistical sampling is precisely for these types of instances in which the number of claims makes it impracticable to identify and review each claim and statement.

In concluding that statistical sampling could be used to establish liability, the court explained that it was an evidentiary question, as opposed to a question of law, and that the proper mechanism to address the company’s due process concerns was cross-examination of the Government’s expert, the company’s own witnesses and other evidence.

Following *Life Care*, another court took up the question of using statistical sampling to establish

liability in the case of *U.S. ex rel. Michaels v. Agape Senior Cmty. Inc.*, 2015 WL 3903675 (D.S.C. 2015), but came to the opposite conclusion. *Agape* involved tens of thousands of Medicare claims that were alleged to be medically unnecessary. The parties agreed that, in theory, each claim could be analyzed individually, albeit at a cost of millions of dollars and in excess of the Government’s estimate of recoverable damages. The court held that the use of statistical sampling was inappropriate. The court was sympathetic to the burden of litigating the case on a claim-by-claim basis, but it explained that there could be significant variability among the claims at issue because they involved patients with different medical conditions, and statistical sampling should be used to establish liability only if the evidence no longer exists. The court certified its ruling for interlocutory appeal to the Fourth Circuit on the ground that the use of statistical sampling to establish liability was a controlling question of law.

When it granted an interlocutory appeal in *Agape*, the Fourth Circuit subsequently became the first federal appellate court to address whether statistical sampling can establish FCA liability. *U.S. ex rel. Michaels v. Agape Senior Cmty.*, Record No. 15-2145 (4th Cir. 2015). After a year of anticipation, however, the Fourth Circuit punted on the question. The Fourth Circuit explained at oral arguments that it had reconsidered its position and that the question of whether statistical sampling can be used to establish liability under the FCA is an evidentiary question and not a question of law suitable for interlocutory appeal.

Until this question is decided at the federal appellate level, it is reasonable to assume that statistical sampling has migrated from the exclusive province of being used to establish FCA damages to also being used to establish liability, at least in cases in which the nature of the allegedly fraudulent claims does not permit efficient analysis of the entire universe of claims. At a minimum, the use of statistical sampling to establish liability will be treated as an evidentiary question as opposed to a question of law, which makes it more likely that the issue will be resolved on *Daubert* motions or at trial rather than on summary judgment.

Rejection of an Automatic Dismissal Rule for FCA Seal Order Violations—The FCA directs that a qui tam complaint shall be kept under seal until allowed to be made public by a federal district court, but it is silent about the penalty for breaking a seal order. The Sixth Circuit adopted a rigid automat-

ic dismissal rule in 2010. *U.S. ex rel. Summers v. LHC Grp. Inc.*, 623 F.3d 287 (6th Cir. 2010). However, the four other federal appellate courts that have considered the issue adopted various balancing tests to determine whether dismissal or some lesser penalty is appropriate. The factors considered include (a) when the violation occurred, (b) whether the violation was willful, and (c) the impact to the Government. See, e.g., *U.S. ex rel. Lujan v. Hughes Aircraft Co.*, 67 F.3d 242 (9th Cir. 1995); *U.S. ex rel. Rigsby v. State Farm Fire & Cas. Co.*, 2015 WL 4231645 (5th Cir. 2015).

The Supreme Court granted certiorari in *Rigsby* to resolve the circuit split, and it issued its opinion in December. The Court unanimously rejected the automatic dismissal rule for seal order violations, and held that the penalty should be left to the discretion of district courts. The Court explained that although the *Hughes Aircraft* and *Rigsby* factors appeared to be sufficient, it was unnecessary to explore these and other relevant balancing test considerations that could be addressed in subsequent cases.

Yates Memo, Cooperation Credit and Focus on Individual Employees—In September 2015, Deputy Attorney General Sally Yates issued a memorandum that specified the requirements that companies must satisfy to obtain cooperation credit in FCA and in other civil and criminal cases. The Yates memo also announced a policy of holding individual employees accountable for corporate wrongdoing. Yates, Justice Memorandum, *Individual Accountability for Corporate Wrongdoing* (Sept. 9, 2015). It stated that (1) no cooperation credit will be given to a company unless the company provides “all relevant facts” regarding the individual employees that were involved; (2) the focus should be on the employees from the beginning; (3) resolutions with companies should not release employees from liability and will not be approved without a clear plan to resolve employees’ liability; and (4) employees’ ability to pay should not be considered in determining whether to file civil cases against them. There are, however, two important clarifications: (a) companies will not be penalized for the inability to identify individual employees that engaged in misconduct if they make a good faith effort to do so, and (b) the provision of “all relevant facts” does not require companies to disclose privileged information (although facts are not privileged).

High Bar for Cooperation Credit: After the Yates memo issued, Acting Associate Attorney General Bill

Baer gave two speeches that further explained what companies must do to earn cooperation credit. Baer stated that although cooperation credit is determined on a case-by-case basis, certain commonalities have emerged: (1) companies should be proactive, e.g., point the Government towards inculpatory evidence and summarize evidence specifically to assist the Government in its investigations; (2) companies should act in a timely manner; and (3) companies should take responsibility for their misconduct and make efforts to assist the victims. Baer clarified that cooperation does not include mere compliance with subpoenas, putting the Government in the position of building the case from the ground-up, or making one-sided presentations to the Government. Baer, DOJ Office of Public Affairs, *Acting Associate Attorney General Bill Baer Delivers Remarks on Individual Accountability at American Bar Association’s 11th National Institute on Civil False Claims Act and Qui Tam Enforcement* (June 9, 2016); Baer, DOJ Office of Public Affairs, *Principal Deputy Associate Attorney General Bill Baer Delivers Remarks at Society of Corporate Compliance and Ethics Conference* (Sept. 27, 2016).

Recent Cases Demonstrate Impact on Individual Employees and Importance of Upjohn Warnings: The Government recently announced settlements in two FCA cases that required individual employees to make considerable payments to resolve their liability. In the *North American Health Care Inc. (NAHC)* case, NAHC agreed to pay \$28.5 million, and the chair of NAHC’s board and an NAHC senior vice president agreed to pay an additional \$1 million and \$500,000, respectively, to resolve allegations that they submitted Medicare claims that were medically unnecessary. DOJ Office of Public Affairs, *North American Health Care Inc. to Pay \$28.5 Million to Settle Claims for Medically Unnecessary Rehabilitation Therapy Services* (Sept. 19, 2016).

In the *Tuomey Healthcare System* case, Tuomey agreed to pay \$72.4 million following a jury verdict finding that it violated the Stark Law and thereby the FCA by paying kickbacks to physicians in exchange for patient referrals. Tuomey’s chief executive officer agreed to pay an additional \$1 million and be excluded from participating in federal health care contracts for four years to resolve his liability. DOJ Office of Public Affairs, *Former Chief Executive of South Carolina Hospital Pays \$1 Million and Agrees to Exclusion to Settle Claims Related to Illegal Payments to Referring Physicians* (Sept. 27, 2016). In both cases, the companies and the employees were required to

cooperate with the Government's subsequent investigations of other employees and companies that were involved in their illegal schemes.

These two cases establish that DOJ will not hesitate to prosecute employees. This raises the stakes for *Upjohn* warnings, which put employees on notice that in the course of an internal investigation, the companies' lawyers do not represent them and it is the companies' decision whether to waive the privilege and disclose evidence obtained from the employees. Failure to give employees clear *Upjohn* warnings could put companies in the precarious position in which they cannot disclose evidence to the Govern-

ment, and therefore cannot cooperate, because the employees who provided the evidence thought that they were providing it in a privileged setting and were protected by due process.



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