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False Claims Act 2014 Preview – The Only Constant is Change

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Companies doing business with the Government could be more at risk than ever for a False Claims Act (FCA) investigation or lawsuit in 2014. The U.S. Department of Justice (DOJ) collected $3.8 billion in fiscal year 2013 for FCA matters, the second largest recovery ever. Although the largest portion of FCA recoveries related to health care, particularly in the pharmaceutical and medical devices industries, companies in the procurement space paid out a record $887 million in settlements and judgments. Courts also handed down hundreds of FCA decisions over the past year, many of which complicated the FCA landscape.

The types of conduct that can subject a company to FCA liability continue to change. With the Government aggressively pursuing recoveries and courts accepting an ever-changing array of legal theories, it can be difficult for a company to know precisely what conduct violates the FCA.

Wiley Rein discussed key trends in our mid-year 2013 FCA review. Here, we focus on important decisions from the second half of 2013 relating to areas that we predict will continue to affect how your company wards off or defends against FCA allegations in 2014.

The False Claims Act

The FCA is the biggest stick the Federal Government wields to recover losses resulting from fraud. A company may be subject to FCA liability if it "knowingly" submits a false claim for payment to the Government, uses a false record or statement in seeking Government payment, or avoids an obligation to pay the Government. 31 U.S.C. § 3729(a) (2009).

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Civil Fraud, False Claims, *Qui Tam* and Whistleblower Actions

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The law is expansive by definition: under the FCA's definition of "knowledge," the Act reaches not only actions a contractor takes with actual knowledge of falsity but also those made with "reckless disregard" or "deliberate ignorance." *Id.* § 3729(b). Further, according to the Supreme Court, the FCA is meant to "reach all types of fraud, without qualification, that might result in financial loss to the government." *See Cook County, Ill. v. United States ex rel. Chandler*, 538 U.S. 119 (2003).

Evaluating claims and defenses under the FCA is further complicated by the fact that the 2009 Fraud Enforcement and Recovery Act and 2010 Patient Protection and Affordable Care Act (ACA) both revised key provisions of the statute. As a result, multiple versions of the FCA may be applicable to conduct that is subject to a FCA suit, with only some revisions applying retroactively.

Government Intervention

Under the FCA, the Federal Government can decide whether or not to participate in a *qui tam* suit. Historically, the Government intervenes in fewer than 25% of *qui tam* suits that are filed, and intervention is more likely in cases where the evidence is stronger and the dollar amounts are greater.

Statistics regarding FCA litigation make it clear that the Government's decision to intervene can be monumentally important to the outcome of a case. In fact, the vast majority of cases fail where the Government does not intervene. In fiscal year 2013, *qui tam* suits in which the Government intervened resulted in settlements and judgments totaling $2.87 billion. In comparison, suits in which the United States declined to intervene only resulted in $109 million in recoveries, or 3.8% of *qui tam* recoveries and 2.9% of overall recoveries under the FCA. As such, the single biggest goal of a company and its counsel should be to convince the Government that a *qui tam* case lacks merits, and that the Government should not intervene.

However, even this landscape is changing. Increasingly, *qui tam* attorneys are exploring new and creative ways to finance and pursue FCA litigation. For example, law firms are beginning to explore obtaining outside financing while FCA litigation is pending in exchange for a share of the potential recovery and future attorneys' fees. This "venture capital" litigation could give some *qui tam* suits in which the Government declined to intervene a vigor that would have previously been impossible.

Implied Certification

One of the biggest problems facing contractors recently is that the Government can take the position that a statement is false even when it is literally true. Some courts have found that a claim for reimbursement can imply compliance with certain contract provisions or regulations, *even if they are not actually set forth in the claim*. If an entity seeks payment from the Government, yet fails to comply with these regulations or contract provisions, the Government may argue that the contractor made a false "implied certification" in violation of the FCA.

FCA cases premised on alleged implied certifications have received increased traction in recent years, as some courts have broadly interpreted the reach of the theory. In November, the U.S. Court of Federal Claims premised FCA liability on an implied certification in *Chapman Law Firm, LPA v. United States*. After a

contractor sued for costs related to its contract, the United States counterclaimed that the contractor had submitted invoices to the U.S. Department of Housing and Urban Development (HUD) impliedly representing that the contractor had conducted routine home inspections and used licensed home inspectors, when it had actually done neither. The court held that the contractor violated the FCA by making implied representations in four of the invoices.

A federal district court in Kansas, meanwhile, found the potential for implied certification liability under seemingly innocuous invoice language. In *United States ex rel. Thomas v. Black & Veatch Special Projects Corp.*, a whistleblower alleged that a contractor in Afghanistan had forged school diplomas presented to the Afghan Government in support of applications for work visas. The court recognized that representations in the claims for payment that "the sum claimed under this contract is proper and due" and that "this voucher is correct and proper for payment" were too vague to be express false certifications under the FCA. The court, however, allowed the suit to proceed to discovery because the claims for payment could have been an "implied certification."

There are limits to when an implied certification can result in FCA liability, however. In the past several months, courts in two influential jurisdictions recently expressed reservations about the theory of liability altogether. In *United States ex rel. Steury v. Cardinal Health, Inc.*, the Fifth Circuit again declined to adopt "implied certification" as a theory of FCA liability. Moreover, in *United States ex rel. Badr v. Triple Canopy, Inc.*, the Eastern District of Virginia characterized implied certification as a "questionable" theory of liability under the FCA, noting that no court within the Fourth Circuit has adopted the theory. In both cases, the courts emphasized that any certification must be a prerequisite to payment to give rise to FCA liability.

Fraudulent Inducement

Under the fraudulent inducement theory of FCA liability, whistleblowers frequently argue that even facially accurate claims for payment made during contract performance can be false if they are "tainted" by a pre-award misrepresentation. Damages awards for successful cases brought under this theory can equal the entire amount paid under the contract, trebled. It is not surprising, then, that there has been a surge of fraudulent inducement FCA cases.

As several recent court decisions demonstrate, this theory is continuing to take shape, with courts in different jurisdictions reaching differing conclusions about the contours of an actionable fraudulent inducement claim.

In *In re Baycol Products Litigation*, for example, the Eighth Circuit set forth a broad standard for when a fraudulent inducement complaint can be actionable. To survive Rule 9(b)'s requirement that fraud be pleaded with particularity, a FCA complaint must generally include details about specific requests for payment from the Government, such as invoices. The court held that a *qui tam* relator does not need to include this kind of detail when alleging that an entire contract was obtained by fraud.

In that case, the defendants allegedly tricked the U.S. Department of Defense into entering into a contract for the purchase of the cholesterol medication Baycol by misrepresenting the effectiveness of Baycol and its relationship to a side effect. The district court had dismissed this claim because no specific claims for

payment were alleged in the complaint. The Eighth Circuit reversed, reasoning that if a plaintiff pursues a fraud-in-the-inducement theory, then all underlying claims for payment under that contract are tainted and a complaint may fully allege violations of the FCA without referencing specific claims.

In a decision more favorable to defendants, in *United States ex rel. Thomas v. Siemens AG*, the District Court for the Eastern District of Pennsylvania held that proving a violation of the FCA for fraudulently procuring a contract requires evidence that the contractor's falsity actually induced the award, and not merely that it could have. The whistleblower in the case alleged that defendant Senior Accounts Manager at Siemens Medical Solutions USA, Inc. (SMS) caused the U.S. Department of Veterans Affairs (VA) to overpay for capital medical equipment by misrepresenting the extent of its price discounts to commercial customers, information that the VA used to determine a fair and reasonable price. The district court granted summary judgment to SMS.

In analyzing the whistleblower's claims, the district court concluded that the whistleblower needed to prove "that the government was induced by, or relied on, the fraudulent statement or omission when it awarded the contract." The court rejected the whistleblower's argument that he needed to show only potential and not actual reliance, reasoning that showing potential reliance only sufficed in "a typical FCA case," where a contractor bills the Government for goods or services it did not provide. By contrast, the court reasoned, proving a fraudulent inducement claim requires evidence "that the decision to award a contract was actually, not just potentially, based on a false statement." The court found no evidence that SMS's alleged omissions influenced the Government's award decision—or that they were false in the first place.

Whistleblower Defenses

In 2013, whistleblowers pocketed more than $345 million in connection with FCA lawsuits. With that sort of financial incentive, it is unsurprising that whistleblowers brought over 750 *qui tam* lawsuits in fiscal year 2013. A contractor hit with a *qui tam* complaint, however, can take advantage of an array of arguments to kick out a meritless whistleblower suit at its earliest stages. Recent amendments to the FCA have changed the situations when a whistleblower may be deemed jurisdictionally improper, however. Further, the strength and contours of defenses remain in flux as courts continue to weigh in with different views.

First-to-File:

The FCA states that "when a person brings an action under [the *qui tam* provisions of the FCA], no person other than the Government may intervene or bring a related action based on the facts underlying the *pending action*." 31 U.S.C. § 3730(b)(5) (emphasis added). The contours of this limitation have been inconsistently applied, however, leading to uncertainty as to the specific circumstances when a *qui tam* suit is precluded by a previous action.

Among other disagreements, federal appeals courts have been split on whether cases that are duplicative but do not overlap, such as when a plaintiff voluntarily dismisses an action and then refiles, are barred by the first-to-file rule. The Fourth Circuit recently held that the first-to-file rule permits duplicative *qui tam* suits, as long as the first filed action is no longer pending. This interpretation could potentially subject a defendant to multiple costly *qui tam* suits premised on the same allegations. The contractor has sought review by the

Supreme Court in *Kellogg Brown & Root, Inc. v. United States ex rel. Carter*.

Public Disclosure Bar:

The public disclosure bar precludes whistleblower suits based on publicly disclosed information, unless the whistleblower was the original source of the information. Whether information has been "publicly disclosed," and whether the whistleblower is an "original source," though, are not black-and-white issues.

Recently, two courts had differing conclusions about whether information was publicly disclosed in a civil hearing for the purpose of triggering the public disclosure bar.

In *United States ex rel. Zizic v. Q2Administrators*, the Third Circuit affirmed the district court's dismissal of a whistleblower suit on public disclosure grounds. The court ruled that the whistleblower's allegations, claiming that the defendant fraudulently billed the Government for reviews of benefit claim denials that were never performed, were based on public disclosures made in previous litigation.

There, a party in the first litigation had included facts in a summary judgment motion that the whistleblower relied on to bring a subsequent claim. According to the court, this disclosure was sufficient to trigger the public disclosure bar. Further, any new information the whistleblower added to his complaint was not sufficiently significant to give life to his otherwise deficient claims.

In *United States ex rel. Ketroser v. Mayo Foundation*, however, the Eighth Circuit used some troubling language when discussing the public disclosure bar, though the court ultimately affirmed dismissal due to the whistleblower's failure to state a claim. The case centered on whether a defendant hospital submitted false invoices to Medicare by not preparing a written report for each tissue slide prepared and billed for during surgery. The Eighth Circuit found that the public disclosure bar did not apply to the whistleblower's allegations, even though information about the hospital's reporting practices was widely available, because the "essence of the alleged fraud" had not been publicly disclosed.

Further, although the Eighth Circuit did not expressly rule on the argument, it found "sound" a whistleblower's argument that information he learned from a prior litigation was not a public disclosure. There, the whistleblower learned about the alleged fraud from discovery responses in prior litigation, meaning the information was exchanged between the parties but was never filed in court. In evaluating the argument, the Eighth Circuit suggested that public disclosure in a previous litigation is limited to information specifically filed with the court or divulged during a hearing.

Another recent decision suggests that there may be leniency to the FCA's original source requirements. Generally, to be an original source, a whistleblower must: (1) have "direct and independent" knowledge of the information on which a public disclosure is based and (2) provide the information to the Government before filing suit. In *United States ex rel. Galmines v. Novartis Pharmaceuticals Corp.*, a whistleblower alleged that a defendant pharmaceutical company wrongfully marketed the drug Elidel, and engaged in related kickback activity.

As an initial matter, the Eastern District of Pennsylvania adopted a liberal standard of when a whistleblower must disclose information to the Government to qualify as an original source. Noting that there is a circuit split on the issue, the court found that the whistleblower must simply provide his information to the Government before filing a *qui tam* suit. In reaching its conclusion, the court rejected the Sixth Circuit interpretation that a whistleblower must disclose his information to the Government before the information is made public to qualify as an original source.

Moreover, the court found that the whistleblower did not need first-hand knowledge of claims the defendant submitted to the Government to qualify as having "direct and independent knowledge," because the whistleblower merely alleged that the defendant pharmaceutical company induced third parties to submit false claims. The court found that the whistleblower's direct and independent knowledge of the scheme leading to the alleged submission was sufficient.

Non-Traditional Whistleblowers

Several recent decisions considered whether a whistleblower lawsuit can be prompted by an attorney, or even brought by the attorney himself.

The Seventh Circuit recently suggested that a *qui tam* action may survive in instances when the whistleblower's attorney, not the whistleblower himself, is the individual seeking to ferret out fraud (and a large monetary payout).

In *Leveski v. ITT Educational Services, Inc.*, the Seventh Circuit reversed and remanded dismissal of aqui tamsuit. A former recruiting employee alleged that ITT Educational Services, Inc. falsely certified compliance with incentive compensation provisions of the Higher Education Act to receive federal student financial aid funds. The court dismissed nearly $400,000 in sanctions assessed against the whistleblower and her attorneys for bringing a frivolous suit through a "manufactured whistleblower." The Seventh Circuit rejected the defendant's argument that an individual who only contemplated filing a qui tam suit after being approached by an attorney could not be a "whistleblower."

The Second Circuit, however, recently decided that a case brought by an attorney as a whistleblower against his client or employer may be improper. In *United States v. Quest Diagnostics, Inc.*, the Second Circuit found that the former general counsel of Unilab Corporation violated New York attorney ethics rules by pursuing a *qui tam* suit that relied in part on Unilab's confidential information. The Second Circuit upheld the district court's order dismissing the case and disqualifying the general counsel, his co-plaintiffs, and their lawyers from bringing a similar *qui tam* suit.

The Second Circuit found that the plaintiffs should be disqualified because it would be impossible to identify and distinguish each of the attorney's improper disclosures, meaning it would be impossible to proceed with a suit that was not tainted. The court also upheld the dismissal of plaintiffs' counsel due to the possibility that confidential information was likely improperly revealed to plaintiffs' counsel.

FCA Penalties

In addition to trebled damages, a defendant found liable for a FCA violation is subject to a penalty of $5,500 to $11,000 per claim submitted. A district court recently determined that there are constitutional limits on the number of FCA penalties that can be assessed against a defendant. Unfortunately for contractors and other entities hit with FCA suits, this issue has been resolved on appeal in a way that negatively affects FCA defendants.

In early 2012, in *United States ex rel. Bunk v. Birkart Globistics*, the Eastern District of Virginia found that awarding the minimum statutory penalty for each of 9,000-plus false claims, or over $50 million total, would be constitutionally excessive in light of the minimal harm to the Government.

The Fourth Circuit recently reversed. The court found that a $24 million penalty would not be constitutionally excessive in light of the defendant's conduct and the need for general deterrence under the FCA. According to the Fourth Circuit, the district court's reasoning would perversely encourage dishonest contractors to rack up the number of false claims accrued to avoid civil penalties altogether. The court remanded the case with instructions to amend the judgment to award $24 million and conduct further proceedings on the remainder of the Government's claim.

Wartime Suspension of Limitations Act

Imagine that tomorrow a whistleblower brings a *qui tam* suit against your company, alleging FCA violations that occurred in the 1990s. At first blush, that action might seem stale, since a FCA claim is not actionable six years after a FCA violation or three years after the Government knew or should have known of it. Yet recent case law interpreting the Wartime Suspension of Limitations Act suggests that the FCA statute of limitations rarely, if ever, applies these days.

The Wartime Suspension of Limitations Act tolls the FCA's statute of limitations while the country is at war. Courts have applied this tolling expansively, holding that it does not require a formal declaration of war and that it is in effect whenever Congress has authorized military actions. The Wartime Suspension of Limitations Act has also been applied to conduct beyond the war zone. Under some courts' interpretations, the FCA's statute of limitations has been tolled since at least 2002, when Congress authorized military actions in Iraq.

This broad interpretation raises constitutional and statutory interpretation concerns. Not surprisingly, it has been challenged. In *Kellogg Brown & Root, Inc. v. United States ex rel. Carter*, a contractor is requesting Supreme Court review of whether the Wartime Suspension of Limitations Act tolls civil, rather than just criminal, FCA cases, and whether the Wartime Suspension of Limitations Act applies even in cases when the Government has declined to intervene. In October 2013, the Supreme Court asked the Solicitor General to weigh in on the issue. The Supreme Court has not yet decided whether to review the case.

Concluding Thoughts

Relevant theories of FCA liability and successful defenses have changed even in the six months since our last FCA update. Well-settled FCA jurisprudence in one jurisdiction may be unsettled—or even contradicted—in another federal court. Given the changing and expanding theories of FCA liability, along with the multiple amendments to the FCA that can come into play, determining what conduct is problematic is more difficult than ever. Accordingly, any company doing business with the Government needs to understand what types of conduct can give rise to FCA liability today.

Companies in the procurement space can expect that whistleblowers, sophisticated and well-heeled plaintiffs' lawyers, and the Government will continue to press the limits of theories of FCA liability that yield large dollar awards. Theories premised on fraudulent inducement, and theories that involve large numbers of alleged false claims triggering penalties, will almost certainly continue to be popular. As courts express hesitation about applying such expansive theories of FCA liability, companies can also expect motivated whistleblowers to pursue new and creative theories.

Accordingly, counsel experienced in the FCA can evaluate all defenses to liability, including affirmative defenses and whistleblower-specific defenses, where applicable. The changing FCA legal landscape, of course, is yet another reason every company should have a robust compliance program and revisit its policies regularly with counsel to ensure they are up to date.