



THE FALSE CLAIMS ACT: A TOOL RIPE FOR ABUSE

The Problem

The False Claims Act (“FCA”), 31 U.S.C. §§ 3729 - 3733, originally intended to ensure that government contractors complied with their contracts, has been broadly and inconsistently interpreted by courts in recent years. This has created a tool ripe for abuse by plaintiffs’ attorneys.

The FCA’s *qui tam* provision, which allows private citizens to sue on behalf of the U.S. Government, has become the dominate method for bringing FCA claims. In 1994, the U.S. Government (“the government”) brought 280 new claims while private plaintiffs, called “relators” under the *qui tam* provision, brought only 218 new claims.¹ Since 1994, relator actions have exceeded government actions each year with 2013’s totals of 754 relator actions compared to only 100 government actions representing the largest gap.² The strong financial and tactical incentives provided to relators explain such a drastic shift in FCA litigation.

The courts’ disagreements with interpreting the FCA have led to an element of forum shopping among plaintiffs. For example, the federal circuit courts are split on whether a plaintiff’s violation of a statutorily required protective seal requires dismissal of the claim, whether “collective knowledge” of several different company employees is sufficient to find a company liable under the FCA, and whether any claim made to the government is made with implied certification of perfect compliance with general regulatory provisions. The U.S. Supreme Court has the opportunity to address each of these concerns in the coming year.

¹ See U.S. Dep’t of Justice, *Fraud Statistics - Overview: Oct. 1, 1987-Sept. 30, 2015*, at 2 (2015) available at <http://www.justice.gov/opa/file/796866/download>.

² *Id.*

History of the FCA

The FCA was originally enacted in 1863 as “The Informer’s Act” to prevent unscrupulous government contractors from fraudulently selling goods and provisions to the government during the Civil War. The Act included several modern features including civil penalties for each false claim and damage multiples of the government’s losses.

During the New Deal and pre-World War II military buildup, the U.S. Supreme Court expanded the *qui tam* provision of the Act.³ That led to opportunistic relators bringing *qui tam* actions simply by copying criminal indictments. In 1943, Congress shut down the practice by requiring claims to rely on information the government did not already possess.

As defense spending increased at the end of the Cold War, Congress revised the FCA yet again in response to reports that fraud was pervasive in government contracts. And by the late ‘90s, the FCA had been interpreted to cover any payment made by Medicare/Medicaid.

Congress expanded the FCA to include additional types of fraud after the financial crises of the 2000s. However, at every step in its development, the FCA has remained specifically targeted at fraudulent actors.

The Modern FCA’s Requirements

As summarized by the 8th Circuit, “The FCA is not concerned with regulatory noncompliance. Rather, it serves a more specific function, protecting the federal fisc by imposing severe penalties on those whose false or fraudulent claims cause the government to pay money.”⁴

³ *United States ex rel. Marcus v. Hess*, 317 U.S. 537 (1943) (*with Jackson, J. dissenting at 558*: “But there is nothing in the text or history of this statute which indicates to me that Congress intended to enrich a mere busybody who copies a Government’s indictment as his own complaint and who brings to light no frauds not already disclosed and no injury to the Treasury not already in process of vindication.”)

⁴ *United States ex rel. Vigil v. Nelnet, Inc.*, 639 F.3d 791 (8th Cir. 2011) *at* 795-796.

To be successful on an FCA claim, a plaintiff must prove that a person knowingly presents or causes to be presented a false claim for payment or approval, or knowingly makes, uses, or causes to be made or used, a false record or statement *material* to a false or fraudulent claim. “Knowingly” may be satisfied with actual knowledge, actions taken with deliberate ignorance, or actions taken with reckless disregard for the truth or falsity of the information. A claim includes a demand for payment, property, or reimbursement made to the government. This definition extends to a government agent, contractor, grantee, or other recipient if the money is to be spent for governmental purposes and the government provides any portion of the money, or if the government will reimburse the agent, contractor, grantee, or other recipient.

The FCA allows private citizens to file *qui tam* actions against private actors interacting with government programs alleging that the private actor defrauded the government. In these cases, the government is the plaintiff, and the private citizen who initiates suit is deemed the relator. The FCA requires a liable defendant to pay treble damages, “per-instance” civil fines between \$5,500 and \$11,000, and the costs of pursuing the action.⁵

When the suit is filed under the *qui tam* provision, it is filed under protective seal to satisfy the statutory seal requirement. However, notice is given to the government through the Department of Justice (DOJ) to decide if it will intervene in the case. The DOJ has 60 days to make this decision, or ask for an extension of time. The action is required to remain sealed throughout this process.

If the government intervenes, then it takes the lead on the lawsuit. If it declines to intervene, then the relator may choose to continue the lawsuit on the government’s behalf. In

⁵ 31 U.S.C. § 3729(a)(1)(g) as adjusted by the Federal Civil Penalties Inflation Adjustment Act of 1990 (28 U.S.C. 2461 note; Public Law 104-410).

each case, if the action is successful, the relator may receive between 15% and 25% or up to 30% of the award respectively, plus the costs of pursuing the action.⁶

A Conflict of Incentives

The FCA provides several benefits to a relator. The high statutory “per-instance” civil fines, fee shifting provision, and treble damage multiplier quickly add up to provide a strong monetary incentive to bring an action. The allure of such a valuable award is so powerful that even plaintiffs’ lawyers whose practice focuses on representing *qui tam* relators may themselves attempt to become a *qui tam* relator on their own.⁷

The statutory seal requirement also is ripe for abuse by relators. For 60 days, only the relator and the government know the specifics of the lawsuit filed against a defendant. During these 60 days, a relator may intentionally break the statutory seal requirement to stage a media campaign against an unwitting defendant. This is particularly so in a jurisdiction that does not require automatic or likely dismissal due to an intentional violation. This media attention can be used to put pressure on either the government to intervene in the case, or on the defendant to settle early and on the relator’s terms. Each result benefits the relator. If the government intervenes, the government prosecutes the case with the relator standing to receive between 15-25% of the final award or settlement. If the government declines to intervene, the relator prosecutes the case and stands to receive up to 30% of the final award or settlement. Either option allows the relator to continue the case with added negative media attention and pressure on the defendant. Without an FCA-mandated or court-enforced penalty for breaking the protective seal, relators are heavily incentivized to do exactly that.

⁶ 31 U.S.C. § 3730(d).

⁷ *United States ex rel. Hayes v. Allstate Ins. Co.*, 2014 U.S. Dist. LEXIS 185026 (W.D.N.Y. Oct. 16, 2014).

Opportunities for Change

The U.S. Supreme Court has two opportunities to resolve on-going circuit splits which have developed under the FCA. The *Universal Health Services, Inc. v. United States ex rel. Escobar*⁸ and *State Farm v. United States ex rel. Rigby*⁹ petitions have been filed with the Court and await certiorari. ATRA has filed an amicus brief in support of each petition.

In *Universal Health Services* out of the First Circuit, the Court is asked to address whether a company, whenever it submits a claim, implicitly certifies to the government that it has complied with every applicable statutory, regulatory, and contractual provision. Courts have called this the “implied false certifications” theory.

Currently, the D.C. and First Circuits take an improperly broad view of the “implied false certifications” theory which essentially requires perfect regulatory compliance with any regulation governing the private actor, while the 3rd, 4th, 5th, 7th, 8th, 9th, 10th, and 11th Circuits have declined to expand their reading of the FCA to include general regulatory violations. The 2nd and 6th Circuits recognize the theory, but strictly limit its applicability.

In *State Farm* out of the Fifth Circuit, the Court is asked to address (1) whether there are any consequences for a *qui tam* relator who violates the statutory seal requirement by staging an extensive media campaign while the action is under seal, and (2) whether separate actions taken by employees which were unknown to each other can be aggregated and taken collectively to satisfy the “knowing” requirement as “collective knowledge” for a company even if no employee committed any violation.

⁸ *United States ex rel. Escobar v. Universal Health Servs.* 780 F.3d 504 (1st Cir. Mass. 2015). ATRA has filed an amicus brief in this case which may accessed here:

<http://atra.org/sites/default/files/documents/Universal%20Health.pdf> .

⁹ *United States ex rel. Rigby v. State Farm Fire & Cas. Co.*, 794 F.3d 457 (5th Cir. Miss. 2015). ATRA has filed an amicus brief in this case which may be accessed here:

<http://atra.org/sites/default/files/documents/State%20Farm%20v.%20Rigby%20Final.pdf> .

Currently, the 6th Circuit takes the reasonable view that a relator's suit should be dismissed as to the relator if the relator breaks the protective seal. Minimally, the 2nd and 4th Circuit engage in a balancing test which includes the prejudice and reputational harm done to the defendant before ordering dismissal. But the 5th and 9th Circuits engage in a balancing test that expressly excludes consideration of the prejudice and reputational harm done to the defendant. In no instance is the government precluded from prosecuting meritorious claims on its own behalf.

In addressing the "collective knowledge" theory, the D.C. and 4th Circuits decline to recognize it. However, the 5th Circuit has adopted the theory and the burdensome compliance measures that a government contractor must take in order to stay compliant.

An additional case is moving through the appeals process in the 5th Circuit Court of Appeals. In *United States ex rel. Harman v. Trinity Indus.*, 2014 U.S. Dist. LEXIS 973 (E.D. Tex. Jan. 3, 2014), a guardrail manufacturer modified its product from a 5" guardrail channel to a 4" guardrail channel in accordance with new safety recommendations from a transportation engineering institute but did not notify the Federal Highway Administration of the change. The FHWA subsequently reviewed, tested, and approved the changes as being in compliance with federal standards. However, after the owner of the company's main competitor brought a *qui tam* action, the court found this failure to notify the government of the change rendered Trinity Industries liable under the FCA, and entered an astonishing \$663 million judgment against the company. This case appears to establish the maxim, "if you can't out-compete them in the open market, sue them." The issues on appeal center on whether strict compliance is required in all instances and whether the government may ratify prior actions through subsequent regulatory approval.

Conclusion

The FCA has a long history of anti-fraud enforcement on behalf of the government. However, recent court rulings and statutory changes have created a burdensome compliance regime for private actors engaging with government programs. The Supreme Court must address the FCA's abuses by resolving the current circuit splits and returning the statute to its original moorings.