

Sixth Circuit 2-1 Ruling Addresses False Claims Act Materiality and Scienter Standards

In Short

The Decision: A divided Sixth Circuit panel held that allegations of submitting late-signed supporting documents to Medicare could plead False Claims Act ("FCA") materiality and scienter.

The Reasoning: Timing regulations were material because they were express conditions of payment intended by Medicaid guidance to prevent fraud; scienter was adequately pled because the defendant allegedly knew of compliance issues but did not investigate.

The Implications: The Sixth Circuit may not be applying the FCA's materiality and scienter precedents with the rigor apparently required by recent Supreme Court precedent, although Judge McKeague's strong dissent and a pending en banc petition may help.

A recent decision by a divided Sixth Circuit panel illustrates that circuit courts continue to wrestle with the FCA's materiality and scienter requirements following the [Supreme Court's decision in *Universal Health Services v. Escobar*](#). In *United States ex rel. Prather v. Brookdale Senior Living Communities, Inc.*, the Sixth Circuit reversed a Tennessee District Court's dismissal of an FCA qui tam suit. In our view, the decision does not apply *Escobar*'s "demanding" materiality standard or its scienter holding with the rigor the U.S. Supreme Court appeared to contemplate. The decision's implications, however, may be limited to its unique facts.

Further, Judge McKeague wrote a strong dissent. The dissent explains how the majority appears to depart from *Escobar* and may suggest arguments for other appellate courts and entities facing similar issues in other parts of the country.

The defendants recently filed their petition for rehearing en banc, asking the entire Sixth Circuit to reconsider what they argued was the majority's misapplication of *Escobar* on both materiality and scienter grounds. If granted, the en banc Sixth Circuit could provide significant further guidance on these important issues.

Background

We previously addressed [Brookdale's extended procedural background](#) and the district court's opinion granting the defendants' motion to dismiss. Briefly, the defendants (collectively "Brookdale") provide home health services to seniors and receive reimbursements through Medicare. To receive reimbursement under Medicare Parts A and B, a physician must sign a certification of need either "at the time the plan of care is established or as soon thereafter as possible." Relator Prather alleged that the defendants waited too long to obtain the signatures, rendering subsequently submitted requests for payment false under an implied false certification theory. The complaint made no allegation that Brookdale submitted requests for payment that lacked the required certification—only that the certifications sometimes were not signed by doctors (or billed by Brookdale) until after the services were provided.

The district court agreed with the relator that the timing of the certification was a condition of payment and therefore could support FCA falsity under an implied certification theory if

signed too late. But it recognized *Escobar's* holding that whether a regulatory violation is a condition of payment is just one factor in determining whether the violation is "material" under the FCA.

The district court held that the complaint did not sufficiently plead that Medicare was likely to deny reimbursement because of a late-dated certification of need. It noted that the relator failed to identify any examples where the government denied a claim on those grounds, "weighing strongly in favor of a conclusion that the timing requirement [was] not material." Additionally, in reviewing "numerous CMS publications," the court found that the timing requirement did not go to the "essence of the bargain" that the government struck. Certification prior to claim submission, not the precise timing of the pre-submission certification, was what actually mattered, making the relator's allegations immaterial. The district court dismissed the case and did not reach Brookdale's independent scienter argument.

The Majority Appears to Relax *Escobar's* Materiality and Scienter Standards

On appeal, a divided Sixth Circuit panel reversed. While citing *Escobar* as the controlling law, the majority held that the lower court erroneously "drew a negative inference" from the relator's failure to identify examples where the government had previously denied a Medicare claim based on the timing of certifications. At the motion to dismiss stage, that failure does not "weigh[] strongly" in favor of dismissal, but instead simply "provides no support for the conclusion that the timing requirement is material." The court's holding on this point was echoed the United States' position in an amicus brief submitted even though it did not intervene in the case.

Without any past government practice to guide its analysis, the majority asked whether the alleged "non-compliance is minor or insubstantial" or instead goes "to the very essence of the bargain." The majority pointed out that the timing regulations were express conditions of payment and that Medicare guidance documents demonstrated that the regulations were intended to prevent fraud. It concluded that a reasonable person would want to know whether a counterparty had complied. It further rejected an argument that the United States' failure to intervene showed that the regulation was not material. As a result, it concluded that the relator adequately pled FCA materiality.

The majority also addressed the FCA's scienter requirement under *Escobar*, even though the district court did not. The court held the complaint pled scienter adequately to avoid dismissal.

The majority noted several allegations that it believed showed reckless disregard. It pointed to the relator's allegation that employees reviewing claims prior to submission were generally "instructed to review the claims only cursorily" and "to ignore any problems." Second, specifically with regard to the timing of certifications, the relator pled an internal Brookdale email acknowledging that physicians could be uncomfortable signing certifications after services were provided. Finally, the relator alleged that Brookdale had alerted employees that the defendants' submission practices "might prompt an audit from Medicare."

According to the majority, "[o]nce the defendants had been informed ... that there may be compliance issues, they had an obligation to inquire into whether they were actually in compliance with all appropriate regulations." The defendants' alleged failure to conduct an inquiry that is "reasonable and prudent under the circumstances" was therefore sufficient to satisfy the FCA's scienter requirement on a motion to dismiss.

The Dissent Emphasizes that Relator Did Not Satisfy *Escobar*

Judge McKeague wrote a strong dissent in response to the majority's analysis, emphasizing that it was inconsistent with *Escobar's* guidance. As to materiality, the dissent explained that because the FCA is an anti-fraud statute, Fed. R. Civ. P. 9(b) required the relator to explain with particularity that the alleged errors "were significant enough to influence the government's actual payment decisions, not merely its abstract legal rights."

Further, the dissent emphasized that the relator made no allegation that the government had ever denied payment based upon the timing of certification signatures. This indicated that the complaint did not satisfy the "rigorous" *Escobar* materiality standard. More importantly, the Medicare form used to submit a reimbursement request also had no space to disclose the timing of supporting certifications. In fact, Medicare guidance and regulations did not "even hint that any late signatures are so important to ... audit or payment decisions that a provider would be expected to disclose them every time." The dissent therefore believed that the government was "not looking for the information that Brookdale omitted," suggesting that the "information is probably not material."

The dissent next explained that absent allegations indicating that the government actually had the allegedly false information in front of it when making a payment decision, omissions should only be considered "material" if they went to the "essence of the bargain." For instance, the government is entitled to presume that guns it orders can actually shoot. But the mere timing of an otherwise-valid certification that services are medically necessary, unlike the certification itself, should not rise to that level.

Building upon his materiality analysis, Judge McKeague also argued that the relator failed to "allege facts plausibly showing that Brookdale knew omitting the explanations would influence the government's payment decisions or that it recklessly disregarded that possibility." Although the relator alleged that employees were told to ignore compliance issues, there was no allegation that this instruction applied to the certification signatures at issue in the case; the whole point of the billing review that eventually led the relator to file suit was to *obtain* certification signatures.

Similarly, once the signatures were obtained, there was no requirement that the defendants affirmatively justify the timing of certification signatures during the billing process. As a result, Brookdale reasonably could have believed that it was complying once it obtained the certification signatures to support its billing requests, negating scienter.

Implications

The majority in *Brookdale* does not appear to be applying *Escobar's* "demanding" materiality requirement at the motion to dismiss stage with the rigor contemplated by the Supreme Court. Nevertheless, the defendants can argue that *Brookdale's* applicability may be limited to circumstances where the regulation at issue was an express condition of payment that the applicable agency had emphasized as an anti-fraud tool.

As for the FCA's scienter requirement, the *Brookdale* majority allowed the relator to proceed by pointing to allegations that Brookdale knew of compliance issues, knew that failure to comply could lead to a potential audit, and failed to conduct a reasonable inquiry to verify its compliance with all appropriate regulations. Given that negligence is insufficient to establish liability, see, e.g., *United States ex rel. Williams v. Renal Care Grp., Inc.*, 696 F.3d

518, 530-31 (6th Cir. 2012), the Sixth Circuit used those allegations to hold that the relator pled that Brookdale acted knowingly under the FCA.

The majority's conclusions could be significantly modified, however, if the Sixth Circuit accepts Brookdale's request to reconsider the case en banc. That petition is currently pending with the full court.

Three Key Takeaways

1. The Sixth Circuit may not be applying the FCA's materiality and scienter precedents with the rigor apparently required by recent Supreme Court precedent.
2. Judge McKeague's strong dissent provides compelling materiality and scienter arguments for other jurisdictions.
3. Stay tuned for possible en banc Sixth Circuit review and ongoing application of *Escobar* in courts around the country.

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